

IT study 2024, part 2 – Less costs, more value?

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Creating transparency about the value of IT spending

In our latest IT study, we embark on an exciting journey through the dynamic landscape of current IT trends, delving into how IT executives can adeptly navigate these changes. At the forefront of our exploration is the impending AI revolution, a transformative force compelling companies to gear up for an "AI-ready" future.

Building on this foundation, our publication shifts focus to a pressing issue: the significant and increasing cost of information technology. We begin by taking stock of the primary cost drivers, which leads us to a pivotal question: What is the true value of IT? This inquiry reveals a complex challenge—how to justify increasing investments in technology whose benefits often remain obscure or unquantified.

We outline five critical challenges in determining IT's value and present a strategic roadmap for organizations to adopt a clearer, value-centric approach. This shift enables companies to manage costs more equitably and efficiently. To bring our discussion to life, we conclude with a compelling case study from a multinational corporation, offering invaluable insights into executing a successful "cost-to-value pivot."

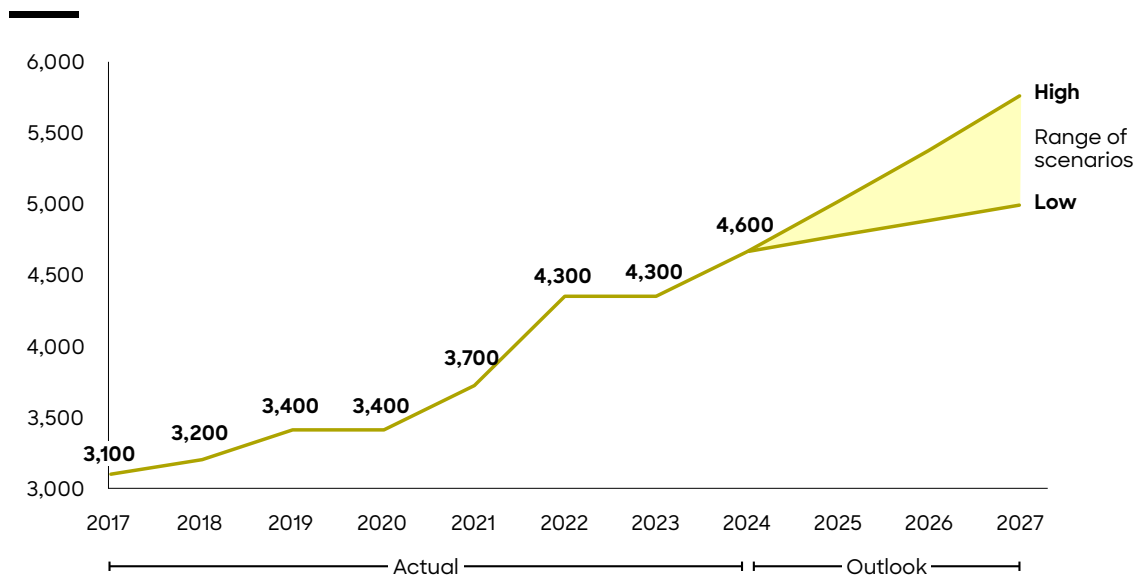
- **Costs, costs and more costs?**

So much promising technology, so little money...

Current developments in AI in particular leave many a CEO and CIO with stars (or dollars) in their eyes at the potential benefits and rewards. And then there are all the expectations placed on cloud services, the need for green IT and, for many, the overdue requirement to upgrade enterprise software. C-level executives are thus forced to ask: How do we measure the value of what we invest in IT? And how do we identify those investments that add the most value for the company? These are the questions addressed - and, we believe, answered - in this publication, beginning with a survey of what factors are driving IT spending growth.

IT costs continue to rise

Worldwide IT spending, 2017-2027 [EUR bn]



Source Roland Berger expert analysis in Mid 2024 based on meta-study on IT cost development forecasts

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After a sudden burst of investment in IT during the pandemic, Gartner recorded a growth of 7% in 2024 - fueled, in our view, by three key drivers:

#1 Spending on cloud and IT services

Drawing on research from our RB project results, we see an increase by more than 20% in 2024 as vendors' prices go up and more use is made of these services. Organizations buying in external expertise to make up for their lack of internal talent is also leading to increased spending on IT services.

#2 Cyber-security

As cyber-threats increase in both number and sophistication in a geopolitically tense world, large organizations will likely ramp up their cyber-security budgets to protect data and systems. The ongoing adoption of cloud technologies, the normalization of hybrid workforces, the stellar rise of Generative AI (GenAI) and a dynamic regulatory landscape are all factors in this development. Based on our experience of budget planning we see an year-on-year increase in data privacy and cloud security budgets alone of 24% in 2024.

#3 Ongoing investment in software

While support for SAP ECC is set to end within the decade, our research on the German market – confirmed by a recent DSAG investment report – shows that less than half of user organizations have so far upgraded to SAP S/4HANA. ERP transformations will therefore continue to be a major (and expensive) cost factor going forward.

Implications

As IT investments continue to rise, it is crucial to quantify the expected business value of IT investments in terms that resonate with business leaders, such as revenue growth, cost savings, improved customer satisfaction and enhanced productivity. Similarly, highlighting how IT investments can mitigate risks, ensure compliance with regulatory requirements, support innovation and make the organization more agile can also strengthen the value case. In practice, however, linking IT investments to the value they create can be very challenging. We believe that IT budgets will continue to rise in the coming years, albeit with moderated intensity as organizations start to focus more on managing their IT costs. Based on our understanding of past trends, we forecast a long-term growth rate of approx. 5% for the coming years.

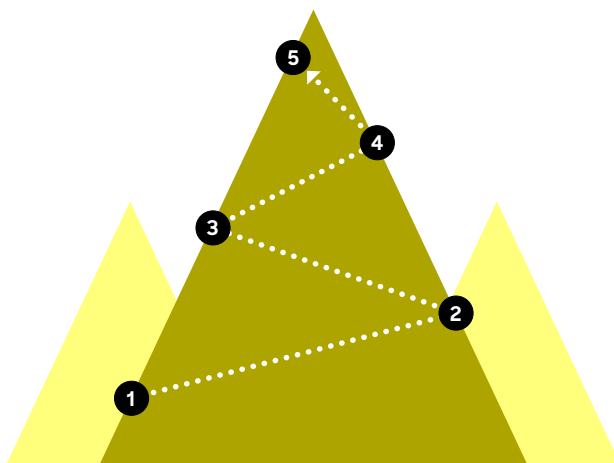
- **What is IT worth?**

The challenges of demonstrating the value of IT investments

In many organizations, IT controlling capabilities have not developed in line with larger IT budgets, while key IT projects such as ERP transformations have experienced significant budget overshoots. This is making it harder for many CIOs to justify the continued growth in spending on IT that is necessary to make IT organizations ready for the future e.g., by implementing AI in daily work of all employees and to modernize key elements of IT infrastructure (e.g. ERP).

A mountain to climb?

Five challenges must be overcome to translate opaque costs into transparent value



- 1 Establishing the baseline**
Establishing a baseline of IT expenditure is difficult in many organizations because IT expenditure is part of several budgets.
- 2 Identifying the value drivers**
The often indirect contribution of IT to business value makes it difficult to isolate the specific value IT adds to organizational success.
- 3 Determining the most effective overall IT spend**
Cost-effective management of individual departments is necessary, as well as ensuring that these efforts contribute to a cohesive and efficient overall IT strategy.
- 4 Maintaining strategic flexibility**
A comprehensive approach ensures that IT not only fulfills current requirements but is also resilient and scalable for future challenges.
- 5 Managing the risk/reward ratio effectively**
Establishing a cost conscious culture includes fostering awareness of risks when cutting costs in order to avoid creating future costs as a result of today's savings.

Source Roland Berger

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Let us look at each challenge in turn:

1 Challenge 1

Establishing the baseline

Establishing a baseline for IT expenditure is difficult in many organizations because IT expenditure is part of several budgets. Regional and business IT budgets, for example, can form a "shadow" budget that, according to recent project experience, can account for up to 40% of a large company's total IT spend without ever showing up in the baseline. Moreover, a one-sided focus on costs often makes it difficult to clearly assign the value of IT investments to specific business units. Consumption-based costing with limited governance by the IT organization can make cost controlling for the services provided to business users difficult. Also, SaaS solutions that are used directly by business units without the involvement of the IT department can be a hidden but painful driver of overall IT costs.

2 Challenge 2

Identifying the value drivers

It is tricky to identify what exactly drives value for the organization in the IT spend analysis. IT often serves as an enabling infrastructure that supports various business processes rather than directly driving outcomes. Benefits such as greater operational efficiency, enhanced customer satisfaction and better decision-making capabilities are realized as multiple departments use the IT systems in a collaborative effort. However, this makes it hard to isolate the specific value IT adds to any given department, and hence to the success of the wider organization.

3 Challenge 3

Determining the most effective overall IT spend

Another critical challenge is to determine what IT support setup is the most effective. Finding the optimal IT spend for the whole organization means combining what is best for each individual department with an IT strategy that is cohesive and efficient at enterprise level. However, since the true value of basic IT infrastructure often remains hidden to business decision-makers, arriving at (accurate) numbers for the organization as a whole is challenging.

4 Challenge 4

Maintaining strategic flexibility

The return on investment (ROI) from a given IT decision must be weighed against how that decision could affect the flexibility to adapt to future needs. Such decisions must meet not only today's operational needs but also the strategic needs of tomorrow. Organizations that properly factor such considerations into investment decisions can build robust, secure, and adaptable IT systems that effectively support long-term business objectives.

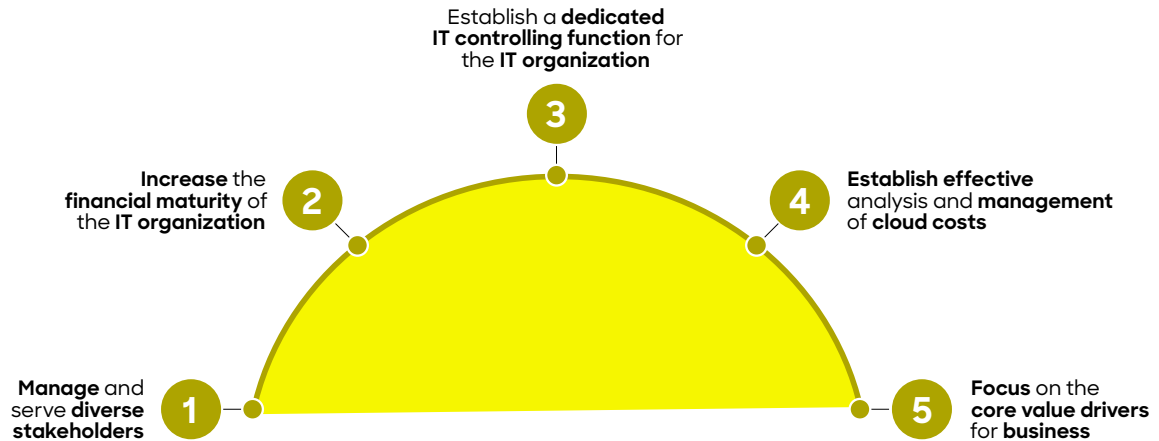
5 Challenge 5

Managing the risk/reward ratio effectively

It is one thing to cut costs but another thing entirely to cut corners. Ill-judged savings that compromise compliance with data protection legislation or leave loopholes in IT security, for example, can have costly and damaging consequences further down the line.

Implications for cost steering

IT organizations need to understand five key lessons to become cutting-edge value centers



Source Roland Berger

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1 Lesson 1

Manage and serve diverse stakeholders

IT controllers must proactively manage the varying information needs of diverse stakeholder groups: Business leaders, for example, need levers to plan and manage their IT costs and support. CIOs want business stakeholders to understand the business value and the cost of the IT products offered to them. And finance and controlling experts understandably want benchmarking information and specific IT controlling solutions.

2 Lesson 2

Increase the financial maturity of the IT organization

CIOs need to nurture more mature financial controlling for their IT organizations. The aim should be to shift from cost center management to value center management, focusing on the value that IT contributes to the company's strategic positioning. This change of mindset can help avoid the trap of short-term cost savings that can potentially destroy value later on. But it can also help the CIO to argue the case for continued IT investment in a challenging economic environment.

3 Lesson 3

Establish a dedicated IT controlling function for the IT organization

A dedicated IT controlling function that adopts a holistic approach to IT cost management can help IT organizations to identify and manage the value of their spend. The application of Technology Business Management (TBM), for example, fosters transparency by categorizing costs and clearly linking them to business value. That in turn gives CIOs valid benchmarks and enables them to steer IT budgets more effectively. Building on this IT transparency, the organization can fine-tune its IT billing and demand forecasting to enable accurate demand forecasts and effective IT planning to coordinate and prioritize new projects. Requests for IT products and services can be bundled and external procurement can be optimized.

Lastly, IT and vendor performance monitoring draws on KPIs built around value for money to ensure optimal vendor pricing. The alternative to this kind of granular transparency and control is what we often see in practice today: IT organizations overwhelmed by the complexity of managing costs across various departments, but with limited formal authority.

4 Lesson 4

Establish effective analysis and management of cloud costs

The same rigor that is put into analyzing 'conventional' IT budgets must also be put into the analysis and management of cloud costs. Financial operations practices for the cloud (FinOps) help organizations to efficiently manage and optimize their cloud expenditures, ensuring they get the most value from their cloud investments while maintaining financial control and transparency. Real-time monitoring of cloud usage and costs is the bedrock of FinOps but must be complemented by an effective cost allocation mechanism that enhances accountability by assigning cloud costs unambiguously to specific teams, projects or departments. This data also makes cost drivers transparent, which is vital for budget planning across the wider organization.

More accurate planning can then result in rightsized cloud resources and realistic savings plans, all of which must be integrated within an organizational governance framework comprising policies, procedures and best practices for cloud cost management. Automated policies become a viable option for more mature organizations to optimize costs and reduce manual intervention. Interestingly, while 82% of companies surveyed by the FinOps foundation have formal FinOps teams, only 13% actually say they have a mature FinOps practice. As long as this crucial tool remains underused, however, valuable cost management opportunities will continue to be squandered.

5 Lesson 5

Focus on the core value drivers for business

Focusing on the core value drivers enables IT organizations to optimize the value they deliver to the business, thus supporting the organization's growth and profitability. CIOs that can demonstrate the value of IT will be better able to manage budgets that support key capabilities and important innovations such as AI, cloud spending and cyber-security while also funding necessary long-term IT transformations such as ERP transformation.

• **Advancing to maturity - A case study**

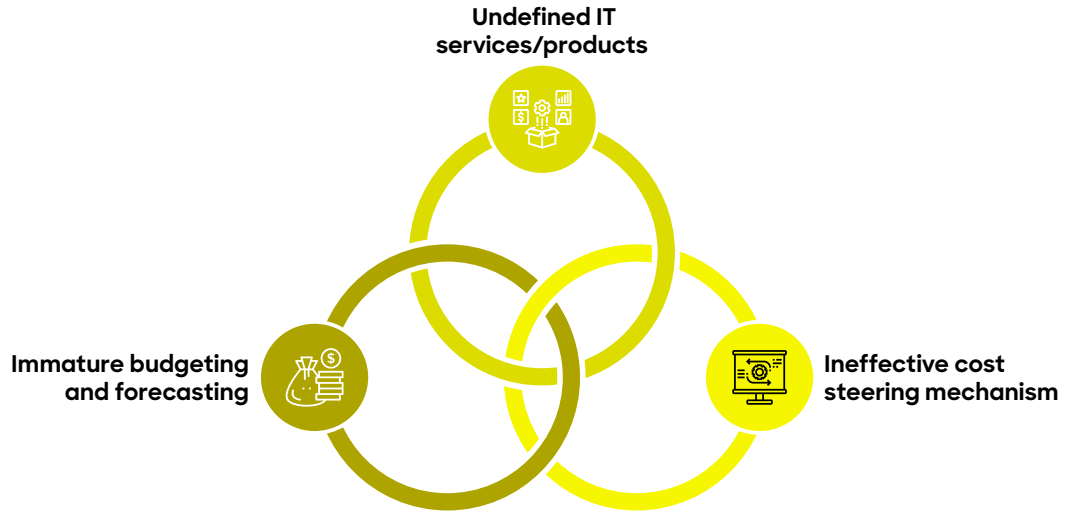
How one European multinational tackled organizational and IT cost optimization

A large multinational manufacturing firm with European roots faced the dual challenge of managing rising IT costs and overcoming unclear links between IT expenses and business value. The company wanted to reduce running costs but maintain or even increase spending on innovation. Initial analysis revealed deficiencies in key areas of IT controlling, prompting the organization to implement a structured approach to address three key challenges:

Key challenges in optimizing IT costs

Three areas for improvement to contain rising costs and clearly assign IT expenses to business value

Case study



Source Roland Berger

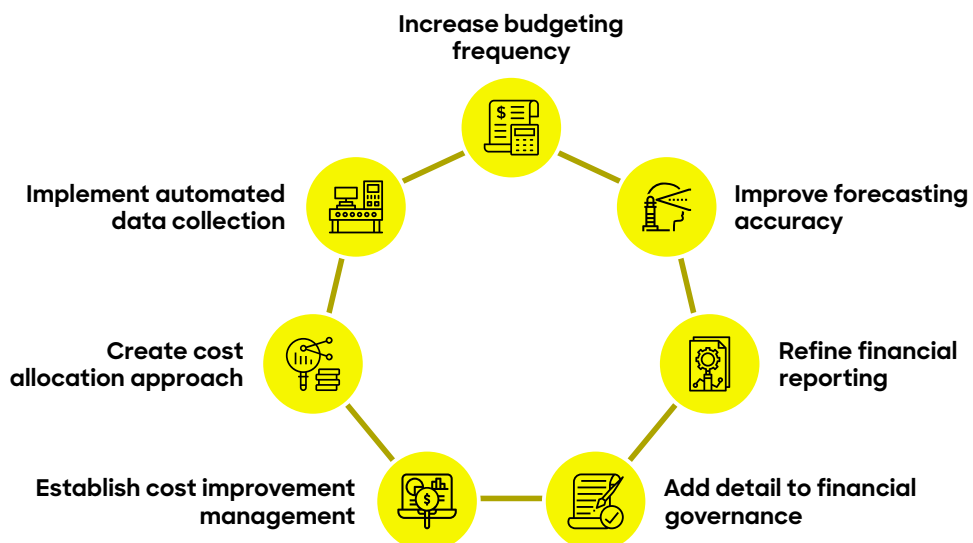
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Immature budgeting and forecasting practices made it difficult to accurately estimate IT costs and align them with the overall business strategy. At the same time, undefined IT services and products throughout the organization made it hard to allocate costs effectively and understand the value provided by IT. Lastly, the lack of any effective cost steering mechanisms at departmental level created difficulties in monitoring and controlling IT expenses.

Seven steps taken in response

Actions taken to address key challenges to optimizing IT costs

Case study



Source Roland Berger

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The company responded to the identified challenges with seven focused measures:

- 1. Increase budgeting frequency:** A monthly rolling forecast approach made budgets more accurate and aligned IT expenses with business needs.
- 2. Improve forecasting accuracy:** Scenario planning provided insights into potential future IT costs under different scenarios, facilitating better decision-making and resource allocation.
- 3. Refine financial reporting:** Interactive dashboards were developed to provide key stakeholders with real-time visibility of IT costs and performance.
- 4. Add detail to financial governance:** Proactive risk management was integrated in the overall business strategy to identify and address potential cost risks, minimize cost-related uncertainties and ensure effective financial governance.
- 5. Establish cost improvement management:** Continuous cost monitoring regularly evaluated cost-saving opportunities to drive ongoing cost optimization and implement identified efficiency measures.
- 6. Create a cost allocation approach:** A multi-driver activity-based costing approach was built around a product-centric IT framework to allocate costs and resources more accurately.
- 7. Implement automated data collection:** An improved IT service management tool was set up to enable automated data collection, facilitating informed decision-making and effective cost control.

By addressing deficiencies in the ways described above, the company successfully enhanced cost transparency, improved budgeting accuracy and aligned IT expenses with business value. The company achieved its goal of reducing running costs while increasing spending on innovation, driving greater efficiency and value within the organization.

• **Talk to us!**

This whole discussion - why IT costs are rising, how best to steer those costs and how to precisely measure the value that IT systems add for whom - gives top management everywhere plenty of food for thought. But it also underscores the urgent need for action. Shifting from cost-center structures to what we have called value centers is not merely a matter of renaming: It demands a shift of mentality, a change of culture. That said, the benefits of doing so - not least the transparency and equity of who pays how much for what - are certainly compelling.

On all these issues, Roland Berger would relish the opportunity to talk with you about where your organization is heading and how we can help. Many years' project experience have given us a wealth of expertise in harnessing the power of technology to drive innovation, enhance efficiency and achieve sustainable growth. To set the ball rolling, simply call or mail us. We look forward to hearing from you!

Further reading

- [IT study 2024 - Trends, challenges and implications](#)
- [The GenAI-driven transformation](#)
- [SAP S/4 HANA transformation](#)

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