Creating Strategic Differentiation with Information Technology

[A Diagnostic]

by John Hagel III

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Basic Observations

Few companies today are harnessing the potential to create strategic differentiation through information technology.

IT alone cannot create strategic differentiation - it is only an enabler. IT creates options that must be effectively exploited through focused business initiatives.

Nick Carr is right: competitors can copy virtually any individual business initiative leveraging information technology. This has three implications:

1. **Companies must aggressively measure return on IT investment** - companies often over-estimate the differentiation available from IT investment and under-estimate the investment required

2. **Building institutional capability for continued initiatives** is the only real source of sustainable advantage

3. Since individual initiatives provide only fleeting advantage at best, it is helpful to **define a longer-term strategic direction that can provide a context for waves of initiatives** that reinforce each other and accelerate movement towards longer-term areas of opportunity
I. Do you know where you are going?

In these uncertain times, senior management is often unwilling to develop a perspective on long-term business trends and their implications for the company. They insist that the future is too uncertain and focus instead on near-term events and needs.

The risk is that this approach tends to become very reactive. Reactive businesses tend to spread their resources too thinly because they lack any framework for prioritizing based on longer-term impact. Individual initiatives tend to have limited impact, because attention spans are short and new initiatives arise to drain resources from initiatives already launched. Without a clear view of longer-term requirements for success, companies will also find it very difficult to pursue effective outsourcing strategies since they will lack a framework for deciding which capabilities are truly strategic.

In this environment, IT investments will rarely result in strategic advantage. Strategy dissolves into tactics and tactical investments rarely produce lasting advantage.

Diagnostic Questions

- Does your company have a clear view of how information technology is likely to reshape your relevant markets over the next five to ten years?

- Does your company have an equally clear view of the implications for the kind of business you will need to operate in these markets to continue to create value?

- Are these views effectively shared among your senior managers and across the rest of the organization?

- Has senior management struck an appropriate balance to provide enough clarity for effective decision-making while recognizing the inherent uncertainty that precludes detailed blueprints of future direction?
II. Are you achieving as much impact as possible?

Because senior management is not effectively aligned around a common strategic direction, companies rarely have sufficient focus in terms of operational priorities. Operational initiatives tend to become too broad in a vain effort to cover as many bases as possible or to satisfy as many decision-makers as possible. In an environment of scarce resources, these initiatives rarely receive the critical mass of resources necessary to achieve significant business impact.

IT resources similarly become stretched. We are all familiar with the lengthening queues of requests for IT and the games that are played in manipulating the queues to get favored treatment. In these conditions, IT investments rarely achieve more than parity with competitors. Strategic differentiation requires too much focus.

Diagnostic Questions

- Has your company been sufficiently aggressive in using IT to enhance product or service economics?

- Are there opportunities to use IT to add value creating (and revenue generating) services around existing products and services?

- Are there opportunities to use IT to significantly reduce component costs in existing products?

- Has your company effectively leveraged the capabilities of IT to fundamentally rethink the core operating processes of the company - supply chain management, customer relationship management and product innovation and commercialization?

- Does your company think broadly enough about the innovation opportunities in core operating processes that span across multiple enterprises - i.e., are there opportunities to increase the performance of supply chain partners or distribution partners through the use of IT?
• Are these innovation efforts appropriately balanced between the use of IT to reduce operating cost, to increase asset leverage and to generate additional growth?

• Has your company systematically determined how IT might be used to support more effective practices among employees?

• Does your company focus on using IT to enhance the practices of "pivotal employees" - i.e., employees whose decisions and actions have a disproportionate effect on the economics of the enterprise?

• Does your company encourage employees to undertake "bottom up" innovation in work practices with the use of IT?

• Does senior management agree on the two to three near-term (six to twelve month) IT-enabled operating initiatives that will be most important in accelerating movement toward the longer-term strategic direction of the company?

• Are these two to three operating initiatives appropriately funded so that the anticipated impact will be achieved?
III. How do you define success?

Strategic differentiation requires discipline. Not only must investments be rigorously justified in advance, the results must then be regularly measured and compared to earlier projections. Focusing on near-term (six to twelve month) operating results helps management to assess progress towards longer-term objectives and to refine initiatives to ensure greater impact. If companies don’t have clear yardsticks to measure progress, they will doubtless see a lot of motion, but very little movement.

Strategic differentiation presumes basic operational integrity and protection against malicious intrusions. Companies often get distracted by grand visions and fail to focus on the basics of IT operations. Without the foundation in place, it is a waste of time (and money) to seek differentiation.

Diagnostic Questions

- Does your company require clear and compelling business cases for major IT investment initiatives?

- Does management insist upon measurable operating results from these investment initiatives within six to twelve months of the investment decision?

- Does management require regular updates regarding the operating results and economic impact of IT investment decisions to determine if targets have been met?

- Does management understand the IT-related vulnerabilities of the enterprise and has it taken appropriate steps to ensure secure and predictable IT operations?
IV. What is required to move even faster?

Corporations face many obstacles in terms of accelerating movement towards longer-term strategic directions. Almost all of these obstacles are organizational in nature - inadequate skills or staff, structures that do not reflect market needs, systems that are inflexible, or cultures that are too bureaucratic, political or risk averse.

Massive organizational change efforts rarely achieve desired results. Instead, management needs to focus on waves of near-term organizational initiatives to strengthen capability. They must create tight feedback loops to more rapidly assimilate learning and changed behaviors into the organization.

In focusing on capability building, management must learn to look beyond the enterprise boundaries. One of the most powerful ways to accelerate movement is to leverage business partners who provide complementary world-class capability.

IT can play a significant role in facilitating capability building. In the end, the most powerful strategic differentiation available from IT will be in creating the institutional capability to rapidly innovate business processes and practices on an ongoing basis. Individual initiatives may be copied, but IT enabled institutional capability is much harder to replicate because of the complex and tight weaving together of the various elements of organization - staff, skills, systems, structure and culture.

Diagnostic Questions

- Does management have clear agreement on the two to three highest impact organizational capability programs that can be implemented within the next six to twelve months?

- Does management effectively deploy IT to support learning initiatives both within the organization and across key business partners?

- Does the company create tight performance feedback loops around a few "closely watched numbers" that determine overall operational performance of the business?
- Does the company use IT effectively to facilitate discussions and document learning among key participants regarding shortfalls and variability in performance results?

- Does management use IT effectively to track exception handling in key operating processes and to mobilize stakeholders to resolve exceptions in the near-term and to reduce exceptions longer-term?

- Does management fully exploit the capabilities of IT to support high impact skill-building programs both within the enterprise and with key business partners?

- Does management effectively use IT to access world-class capabilities from other companies and to focus its own organizational resources on the areas where it can achieve significant differentiation?
About John Hagel

John Hagel III has nearly 30 years experience as a management consultant, author, speaker and entrepreneur, and has helped companies improve their performance by effectively applying information technology to reshape business strategies. John currently serves as co-chairman of the Silicon Valley-based Deloitte Center for the Edge, which conducts original research and develops substantive points of view for new corporate growth.

Before joining Deloitte, John was an independent consultant and writer. Prior to that, he held significant positions at leading consulting firms and companies. From 1984 to 2000, he was a principal at McKinsey & Co., where he was a leader of the Strategy Practice. In addition, he founded and led McKinsey’s Electronic Commerce Practice from 1993 to 2000. John has also served as senior vice president of strategic planning at Atari, Inc., and earlier in his career, worked at Boston Consulting Group. He is the founder of two Silicon Valley startups.

John’s blogs: The Big Shift (HBR) and EdgePerspectives blog.
See also: JohnHagel.com »