



# Future of IT

Dynamic investment

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# Effective cost optimization is critical for the market-speed enterprise

Today's hyper-competitive and fast-changing global environment is prompting forward-looking enterprises to accelerate their investment in transformational IT capabilities. To deliver continuous digital innovation — and reveal the true value of technology spending in the digital economy — these enterprises are re-engineering the technology funding process.

To become agile, market-speed organizations, many are embracing *dynamic investment* for its breakthrough ability to forge a new financial connection between IT spending and value — one that aligns enterprises as never before with their ever-evolving markets and ongoing technology needs.

Unfortunately, a widening 'digital divide' exists today as global enterprises modernize to enhance agility, efficiency, and competitiveness. As digital leaders transform for the future, left behind are those without the insight to spend on technology in a manner that is as agile as their enterprise. The widening gap between leaders and those left behind is creating conditions for a 'winner-take-all' market.

Our previous article in this series examined the need for *cost transparency*. Cost transparency reveals the value of technology by identifying and classifying costs, defining cost drivers, and using the timely collection of cost data to inform smart decisions. This 'building block' is a foundational enabler for digital leaders to 'cross the divide' and harness the power of dynamic investment.

## Cost optimization challenges prevail in the race to transform

While it may be tempting to jump to this transformed way of funding value we call dynamic investment, we urge you to not forget cost transparency can reveal opportunities to better optimize the existing IT estate. The leaner the current IT operating model is, the greater the reward may be when shifting to dynamic investment. In this second article of the dynamic investment series, we illustrate how some successful enterprises approach *cost optimization* to get more value from their ongoing technology spend now and in the future.

## Aligning IT and finance teams in new ways

Numerous approaches are employed today by enterprises tackling the need to optimize technology costs. Unfortunately, IT and finance typically work toward valid but divergent objectives in this pursuit.

Technologists want maximum flexibility, while finance-types seek structure and predictability.

KPMG professionals often see flawed, unsustainable initiatives result when IT teams address cost takeout and optimization without much involvement from finance. The reverse is also true. These teams often face the challenge of making sense of technology's increasingly sophisticated function and value.

IT and finance should be aligned as never before on how technology costs are identified and classified, and how to reduce cost from those insights. They must also collaborate with a shared appreciation



for substantial shifts in how technology goods and services are purchased and provided. Long-term capital purchases (e.g., depreciable datacenter equipment) have been largely replaced by highly variable operational expenses bound by different contracts (e.g., cloud service provider agreements). It is only in pursuit of understanding each-other's perspectives on these trends can IT and finance be effective in figuring out how to make dynamic investments in technology.

## Finding cost optimization opportunities

By bringing IT and finance teams together to collaborate in new ways and manage costs effectively, enterprises can identify 'quick wins' to help eliminate costs in areas such as:

- 1 Infrastructure run and maintenance;
- 2 Licensing costs, including over-subscription and the use of costly licenses for simple activities;
- 3 Unmanaged spending on cloud resources;
- 4 Duplicated investment in technologies and solutions;
- 5 Time-intensive 'management' overhead (minimizing things like stage gates, council reviews, layers of reporting, etc.)

Firms operating without a centralized IT procurement-finance function, or experiencing a high level of shadow IT activities, can benefit from an exercise to rationalize costs. Opportunities also exist for enterprises with no direct linkage between IT/digital service costs and consumption, and those lacking regular reporting on IT costs and consumption. As you can see, cost transparency is an important enabler to refine cost optimization opportunities.

A rationalization exercise demands you 'take nothing for granted,' and results should be reviewed by an independent party not involved in the day-to-day operations. This is essential to identify duplicate investments and unmanaged or uncontrolled resources.

An important note not to be forgotten: digital transformation is not necessarily about IT cost reduction, but cost optimization frees up funds for higher priority needs that can accelerate the pace of change. Recovered funds can be deployed with greater velocity and effectiveness when enterprises leverage the principles we are about to articulate for dynamic investment...

## The dynamic investment journey is not linear

Combined with ongoing optimization of past spend (some do it monthly), adopting a principled, forward-looking dynamic investment model makes holistic spend management a possibility by:

- **Replacing static budgeting cycles with dynamic funding:** The dynamic model replaces annual budgeting with a timely and flexible process. The goal is to fund innovation on a rolling basis. The key to this process is that funding adjusts to prevailing needs;
- **Implementing product financial management:** Enterprises need to shift from *project* financial management to *product* financial management. Supporting technology teams need to align to product development and product owners should organize products;
- **Changing funding governance:** Governance of funding is critical to replacing traditional project budgeting with product funding. A new governance model should include guidance on roles, decision-making authority, and the processes by which funding decisions are adjudicated.

These core principles of dynamic investment are our preview to the *When*, *What* and *How* of the dynamic model. Supporting actions to evolve in key finance and accounting areas include: the need for leaner and simplified *value cases*, updating of *capitalization policies*, and evolving *financial analytics*, including reporting, analytics and metrics related to spending, economics, and value.

Our key message to clients is this: the journey to dynamic investment is not linear, with cost transparency and cost optimization staged as building blocks that have cumulative effects. KPMG firms are here to help — and we believe there is no time to lose in narrowing today's growing digital divide.

# The journey begins with a new window on cost transparency

In the race to leave the global pandemic's disruptive impact behind and embrace new opportunities for growth, forward-looking enterprises are accelerating their investment in transformational IT capabilities. In today's hyper-competitive reality, these enterprises recognize that funding rapid digital innovation using diverse investment models can pose significant financial-transparency issues, under-utilization of new capacity and ongoing challenges to technology budgets.

To help reduce reliance on legacy technology and capitalize on game-changing capabilities such as enterprise SaaS, distributed cloud infrastructure, artificial intelligence and automation, re-engineering the finance and technology-funding process is now critical.

More enterprises are turning to *dynamic investment* for its ability to forge a new financial connection between IT spending and value, ultimately enabling rapid and continuous change in technology funding and implementation. Enterprises turning to dynamic investment are becoming aligned as never before with their customers, markets and ever-evolving technology needs.

## Cost transparency is the first step to dynamic investment

Unfortunately, as leading organizations respond to today's challenging market dynamics, we are witnessing a growing 'digital divide' in which enterprises trail competitors on the need for modern tech funding that enhances agility, efficiency, and competitiveness in

today's digital economy. Organizations on the wrong side of the digital divide are finding it increasingly harder to compete and this widening gap is creating conditions for a 'winner-take-all' market.

Slower-moving enterprises are struggling with cost transparency challenges related to *identifying and classifying digital-innovation costs, understanding cost drivers, and using the timely collection of cost data* to inform and enhance decision making.

A key challenge that we observe is a lack of knowledge concerning the need to establish a modern cost-management framework that is specific to IT and digital capabilities. This typically leads to a number of issues and limitations — including an inability to generate relevant data and timely insights into classifying, measuring and allocating technology costs.

It's common to see organizations relying on various 'shortcuts,' for example consolidating IT and digital innovation costs into a single line item, and allocating investment using generic drivers such as the ratio of revenue versus costs, or employee headcount and

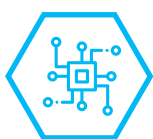


related staffing costs. This generic cost allocation tends to be relatively ambiguous in determining costs and can typically prompt ongoing debate and disagreement regarding the 'fairness' or 'appropriateness' of IT and digital-innovation spending. In addition, many organizations still have a number of 'shadow' IT activities in which associated costs are not captured or analyzed in a centralized and productive manner.

Establishing a dedicated team possessing the skills needed to create an appropriate IT/digital cost-management framework is essential to resolving today's challenges and delivering both new levels of cost transparency and insights into the *value* of IT and digital-innovation spending.

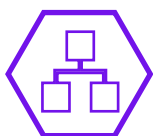
## Solving today's cost-transparency challenges

Cost transparency is important to consider to enhance identification and classification of costs while accurately identifying cost drivers and tapping into the power of data-based insights — as a critical enabler to become more agile and responsive to the demands of their markets.



### Identification of technology costs:

The finance function is a key influencer in developing a dynamic-investment approach, making it crucial that IT and finance are aligned on how technology costs are identified. To run at market speed and make quick pivots, enterprises need a real-time view into the specific cost elements of the technology portfolio and the levers available to adjust costs, quality, performance and consumption. Close collaboration that aligns the IT and finance functions to create a new view into the true cost of technology spending — including 'shadow' technology costs embedded in initiatives led by other departments — is critical to enhancing cost transparency.



### Classification of costs:

Aligning IT and finance teams on how technology costs are classified requires IT and finance to collaborate using a common language. The classification 'taxonomy' must evolve from outdated approaches in which IT costs are assigned to macro categories with a limited view of financials or project spending. This approach makes it hard to create a comprehensive view of technology costs from both IT and enterprise-wide perspectives. This all leads to new ways of working — with cost data continuously analyzed and refined to provide finance, accounting, IT and the rest of the enterprise with significant new reporting views.



### Identifying cost drivers:

Cost drivers related to technology spending are traditionally pre-built and based on considerations such as headcount, vendors, applications and infrastructure components, making it hard to change the cost drivers for various analytical purposes. As financial analytics evolve, information will be available based on the cost driver of choice and related to the activities they represent, with easily adaptable views making effective reporting quick and easy.



### Timely collection of cost data:

Replacing static IT budgeting cycles with a new reliance on timely data unlocks powerful capabilities to anticipate and rapidly address emerging technology needs. Smart decision-making demands that enterprises understand the impact of costs and investments across the entire organization. While finance is typically the gatekeeper of data and the insights it can offer on costs, true IT cost transparency fosters close collaboration, ongoing dialogue and new alignment between IT spending and the finance function.

# Prioritizing technology investment becomes critical to business success in today's reality

The need for businesses to rapidly innovate and pivot in response to ever-changing market conditions, trends and business needs has never been greater. Agile, market-speed organizations pursuing modern digital capabilities, services and customer experiences are recognizing that amid the 'need for speed' in the digital economy, the IT function itself needs to develop the ability to rapidly re-prioritize and re-allocate resources to deliver the most value as business opportunities emerge.

In a market-speed operating model, businesses can rapidly pivot, seize new opportunities, quickly exit poorly performing investments and de-risk large initiatives. For the IT organization to run at speed, re-engineering the technology finance and funding process is becoming a significant areas of focus.

Funding technology innovation using antiquated investment models can cause misalignment between business and IT priorities, under-utilization of new capacity and ongoing challenges to technology budgets. As digital leaders are discovering, the *dynamic investment* funding model forges a new connection between IT spend and business *value* — ultimately enabling agile technology funding and digital innovation that is indispensable today in the race for growth and competitive advantage.

For *cost-transparency* and *cost-optimization* to be fully exploited amid today's typical resource, staffing and budget challenges, dynamic investment should deliver new capabilities to *prioritize* technology spending based on improved transparency and on the business value that innovation can deliver. This helps to meet evolving customer, marketplace and technology needs.

Rather than prioritizing innovation investment at the beginning of an annual review process and shuffling resources as required, prioritization should be continuous and based on both past and expected future value produced. Prioritization of technology initiatives under the dynamic investment model can be done using 'scenario modeling' — calculating the best method to maximize business value amid funding and resource constraints. Dynamic investment also provides businesses with a balanced scorecard approach that combines quantitative ROI considerations with qualitative data that can provide timely marketplace insights and enhanced decision making on innovation spending.

## Bringing IT and finance teams together

Unfortunately, as emphasized in our previous articles in this series, while digital leaders are responding to today's challenging market dynamics, we are witnessing a growing 'digital divide' as most businesses trail leading competitors on the need for a modern tech-funding model that enhances agility, efficiency and competitiveness. Organizations on the wrong side of the digital divide are finding it increasingly difficult to compete and this widening gap is creating conditions for a 'winner-take-all' market.

As we stress to clients, in the race to innovate and transform, dynamic investment is essentially about funding innovation at scale. Success in today's fast-moving and hypercompetitive environment requires a modern culture of innovation, speed and agility — with each 'experimental' technology initiative repeatedly and routinely tested against a clear articulation of its value and viability. Successful experiments should be granted more funding to continue to grow and produce value, while failed ones should be quickly scratched to free up scarce resources.

While assessing ROI remains a key factor in prioritizing and pursuing technology innovation, relying exclusively on traditional business cases or three-year technology-innovation roadmaps is no longer viable. The need for speed in today's reality demands a new approach. Prioritizing technology investment and innovation in ways that enhance and sustain agility, growth and business value has become indispensable.

Unfortunately, many organizations continue to pursue a quantitative approach that tends to prioritize ROI over all other measures of value during IT funding reviews. Aligning technology and finance teams on both the benefits and ROI of technology initiatives remains a struggle, with technology leaders typically challenged by finance on the need to clearly articulate the *value* that innovation can deliver, thus impeding their ability to innovate quickly.

A traditional, pure-ROI approach to innovation spending favors proven or 'safe' technology initiatives backed by data that promises appropriate returns. Connection to other forms of value is limited, with controls put in place to manage IT investment via backward-looking analysis of scope, schedule and budget performance. In many cases, current technology in use by the business will likely be allowed to run its course until innovation becomes critical and unavoidable — while the digital divide grows wider.

This dated approach limits necessary innovation that is agile, continuous and truly responsive to market trends and evolving business needs not always reflected in the bottom line. IT investment needs to be engineered with a direct connection and line of sight into products and the value generated for the organization.

### Turning to a balanced scorecard

We are advising businesses on the need to uplift their digital maturity and capabilities in order to gain a broader perspective that supports smart decision making on technology investment and its overall value to the business. Prioritizing investment is key and dynamic investment's ability to provide a balanced scorecard approach to investment is the inevitable way forward.

Combining quantitative considerations with qualitative data and metrics delivers crucial insights in key areas such as market trends, customer satisfaction and experience, brand awareness and reputation, operational improvements, risk mitigation and compliance and skills needs.



Success with this approach implies new levels of collaboration and agreement among business leaders within the tech and finance functions on emerging data insights and the investment needed for a timely, agile response to business and marketplace conditions.

In our work with a major Australian banking client, we helped the organization take a new approach during a major initiative to shift core banking services to cost-saving cloud platforms. The typical ROI-based approach would have been to simply assess the initiative's short-term impact to the bottom line. Beyond savings and financial returns, the bank's cloud innovation initiative adds value to the business by enhancing key areas such as customer service and operational agility — significant non-financial benefits that simple ROI measurement does not capture.

But by bringing IT and tech finance leaders together to evaluate *both* the financial returns and non-financial benefits of its costly cloud initiative, we positioned the bank to take a long-term view of how cloud capabilities can ultimately add value to the business.

### Replace project budgeting with product funding

Today's business leaders ultimately need to understand and be accountable in new ways for the efficient allocation of resources, the cost implications of every technology-funding decision and the value being delivered to the business.

Unfortunately, IT governance often remains misaligned to balancing risk and technology performance. A single governance model focused on predictability and accountability has traditionally been viewed as suitable for all IT spending. However, a single monolithic governance model — and the lack of transparency regarding both IT spend and business value — often produces IT investment decisions that are poorly informed and inefficient.

The focus should shift from tracking and predictability to enabling the flow of value. The dynamic investment governance model replaces traditional *project budgeting* with *product funding*, addressing key considerations such as decision-making policies, roles and rights among leadership regarding technology investment.

To maximize the agility of the business and its growth opportunities, technology stakeholders who are closest to the products and value streams need to acquire a new voice in the process and its prioritization decisions. Done right, a new approach allows for faster technology advancement that will likely enhance growth and prosperity for the business.

In conclusion, today's business leaders need to ask themselves if their business is truly generating appropriate value from its technology spending and innovation. In today's fast-evolving reality, where the pace of change continues to accelerate, businesses also need to consider the ultimate 'cost' to the business of not innovating and transforming in ways that can support future growth and competitiveness. Digital leaders are showing the way and there is no time to lose in the race to innovate and adapt at the speed of the market.

# Getting started

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Navigating our new reality has been a real game changer. It has revealed a growing digital divide between businesses that were already down the path of transformation and others struggling to keep pace.

Surviving in the new reality requires businesses to deliver at speeds today's customers expect. To accomplish this, the way IT operates must be reimagined. It needs to employ an operating model that is agile, dynamic, and adaptive to both business needs and market demands in order to deliver at varying speeds and scale.

This market speed operating model must be portfolio driven — meaning from how people are organized and governed all the through to the technology architecture that supports it — and designed around the specific value streams of the business and its unique velocities, attributes, and characteristics.

In a hyper-connected world, IT needs to deliver on the promise of the connected enterprise. The future of IT is about removing friction and adding new capabilities to enable a front, middle, and back office that is laser focused on a profitable, customer-centric, digitally enabled business.

Explore how KPMG professionals can help IT evolve its operating model, culture, skills, relationships, and ways of working to deliver value in a digital world.  
[Visit our website](#) or contact us below.

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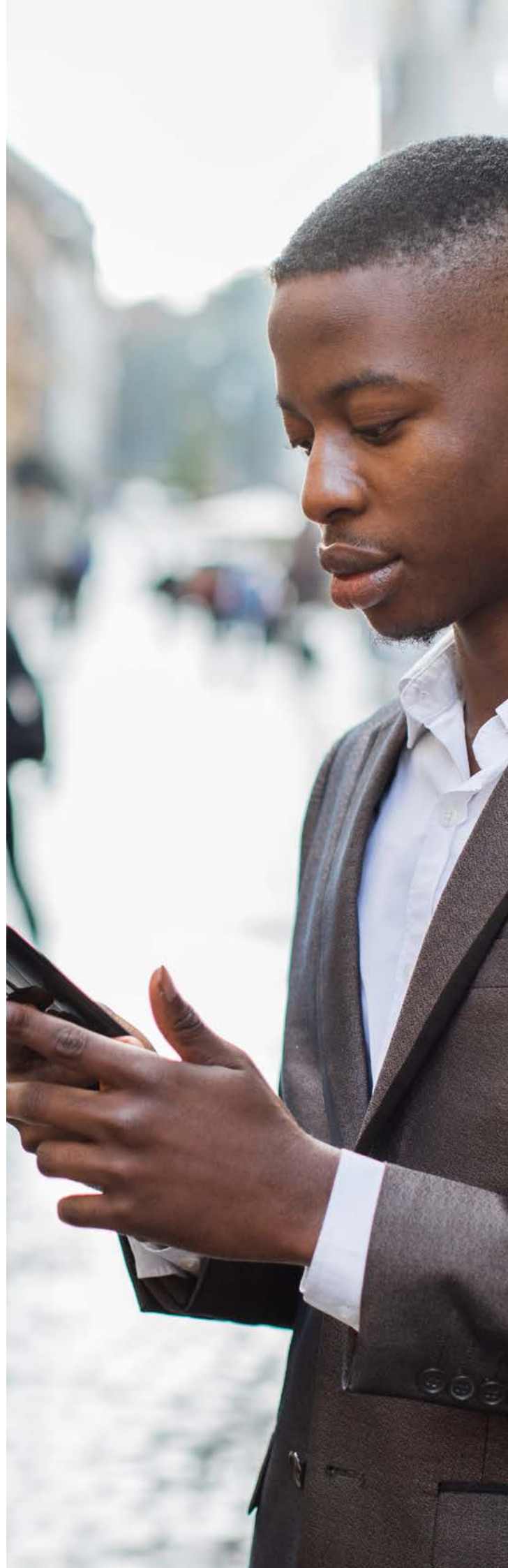
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