EVALUATING PERFORMANCE

Measuring Your I.T. Superiority

BY PAUL A. STRASSMANN

During a review of the effectiveness of information-technology operations, directors sitting on corporate boards would usually like to avoid hearing about technical topics such as "architecture" or "networking strategies."

The directors—who usually have a limited amount of time to devote to an examination of technology spending—tend instead to focus on whether steadily rising technology costs actually deliver a competitive advantage to their company.

A chief information officer who wants to successfully withstand such an inquiry should seek out credible evidence to make a case. Essentially that means showing, and quantifying, how the company spends less than key rivals on information technology while simultaneously delivering superior results to shareholders.

Where to begin? Start by reviewing the financial statements of your company and those of your rivals, identifying technology spending as well as other expenditures and metrics such as employee head count.

Then, calculate key cost ratios, such as technology spending versus revenue, and key performance ratios including return on shareholder equity for your company and your rivals (see worksheet at right).

If the cost ratios are lower and performance ratios are higher than those of your competitors, you will have a better shot at getting your request for information-technology spending plans approved by the board of directors—or even possibly keeping your job for another few years.

TOOL: How Do You Rate Against Rivals?

One approach to demonstrating the effectiveness of your technology operations is to compare your company against its rivals, using data from financial statements. Use the worksheet below to calculate cost and performance ratios to find out whether you run a superior shop—or one that needs improvement.

The example here assumes a company with 7,812 employees and an annual information-technology. budget of $91.9 million.

CAUTION: Getting an accurate number for a competitor's technology spending can be tricky. Costs reported on audited financial statements are acceptable, but outsourced information-technology operations may be classified as "cost of goods." You will need to investigate further.

INSTRUCTIONS: Fill in your own numbers in the column labeled "Your Company" as well as research results for "Your Competitor," and do the calculations described at left. Continue the evaluation for as many competitors as available data allows. Or log on to GO.BASELINEMAG.COM/SEP05 and download the spreadsheet from our Premium Tools Library.

	BASICS	YOUR COMPANY	YOUR COMPETITOR	EXAMPLE
A	I.T. spending, all departments, in $000			$91,915
B	Revenue, in $000			$2,165,913
C	Sales, general & administrative costs, in $000			$625,089
D	Profit before extra items, in $000			$398,925
E	Shareholder equity, in $000			$2,537,638
F	Cost of capital (%)			6.83%
G	Number of employees			7,812
H	Average compensation/employee			$62,187
I	Total compensation costs, in $000 (**G x H ÷ 1,000**)			$485,806
	COST RATIOS			
J	I.T. spending/revenue (**A ÷ B**)			4.2%
K	I.T. spending/compensation (**A ÷ I**)			18.9%
	PERFORMANCE RATIOS			
L	Return on shareholder equity (**D ÷ E**)			15.7%
M	Information Productivity* ((**D - (F x E)**) ÷ **C**)			36.1%

	I.T. SUPERIORITY EVALUATION (Circle the answer that applies to your company and competitor)			
J	**I.T. spending/revenue** (low ratio = superior)	Superior/Inferior	Superior/Inferior	
K	**I.T. spending/compensation** (low ratio = superior)	Superior/Inferior	Superior/Inferior	
L	**Return on shareholder equity** (high ratio = superior)	Superior/Inferior	Superior/Inferior	
M	**Information Productivity** (high ratio = superior)	Superior/Inferior	Superior/Inferior	

BOTTOM LINE: ANSWER "SUPERIOR" TO THREE OR MORE, YOU'VE BESTED YOUR RIVALS. BUT THAT STILL MIGHT NOT BE GOOD ENOUGH.

*TO CALCULATE THE INFORMATION PRODUCTIVITY RATIO, SEE *GO.BASELINEMAG.COM/INFOPROD*