

Will your digital investment strategy go from virtual to reality?

Learn eight key actions to help improve your digital strategy and realize a return on digital investments



The better the question. The better the answer.
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Executive summary:

- ▶ Digital leaders have clearer strategies and better technical execution, resulting in a higher return on digital investment and revenue growth.
- ▶ The internet of things (IoT), cloud and AI become table stakes as digital spend accelerates, but most companies have yet to realize the full technology benefits.
- ▶ C-suite executives have differing preferences on organic vs. inorganic digital investment strategies. Digital M&A is more likely to exceed expectations.

After years of heavy technology spending, CEOs, chief digital officers and other senior executives are feeling the pressure to realize a return on digital investment (RODI). Budget constraints in the pandemic economy, deals that fail to deliver as promised and the rapid pace of digital transformation across organizations threaten to turn digital promises into mere buzzwords – unless organizations can prove the value of their investments to the bottom line.

The EY team and Oxford Economics surveyed 1,001 executives with technology decision-making responsibility across industries worldwide about their digital strategies and results. The EY-Parthenon *Digital Investment Index (DII)* study, conducted in the third quarter of 2020, provides a snapshot as organizations recalibrate strategies in response to the COVID-19 pandemic. Among the questions asked in the survey are: What technologies are you investing in? Are you acquiring startups, creating partnerships or building capabilities internally? How many executives are measuring RODI as a key performance indicator (KPI), and what returns are they seeing? What are you doing differently as a leading company? Business analytics firm CB Insights provided additional data analysis around deals and technology adoption.

The results show that some technologies, such as cloud computing and artificial intelligence (AI), have become table stakes, but scaling these digital initiatives remains a challenge. Executives are not yet aligned on investment strategies and struggle to measure the returns on their investments. The leading practices of a select group of leading companies provide a possible way forward for organizations struggling with these issues.







This survey synopsis highlights five areas

1 Lessons from the most high-performing digital investors

2 How to improve digital investment benefits

3 Aligning on investment vehicles

4 Overcoming barriers to scale

5 Establishing robust metrics

This synopsis concludes with eight recommendations for senior executives.

1

Lessons from the most high-performing digital investors

Meet the digital leaders

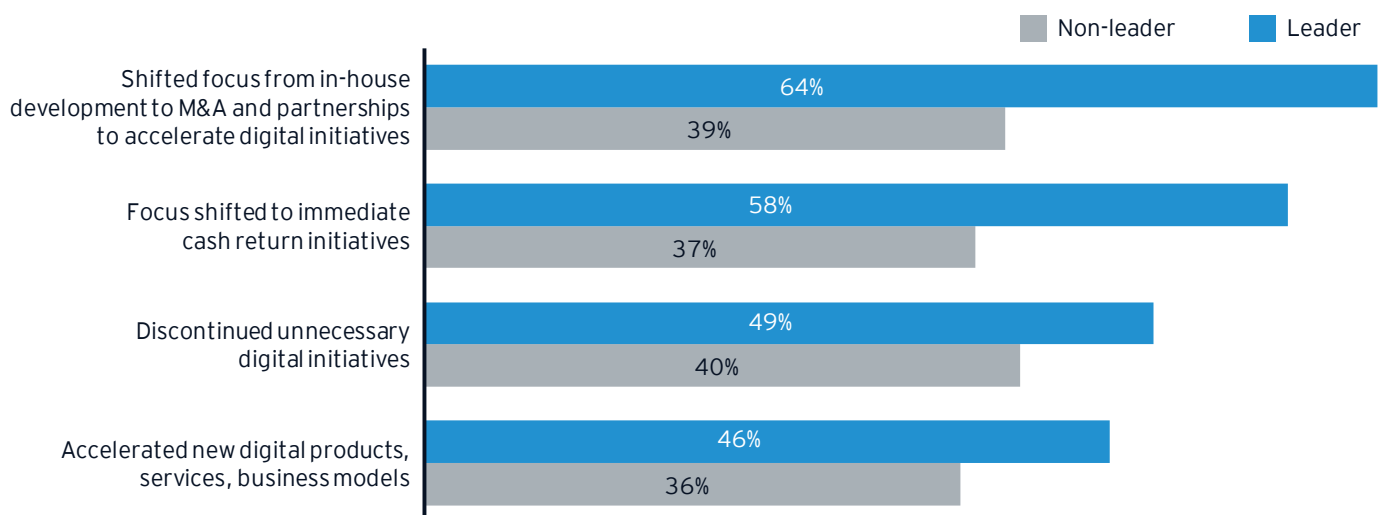
We identified a select group of survey respondents who have achieved higher RODI and say they are digital leaders in their industry. These respondents:

- ▶ Represent just 9% of the survey's 1,001 respondent sample
- ▶ Achieve around six percentage points more RODI compared to non-leaders
- ▶ Report stronger revenue growth over the past two years (49% report revenue growth above 6% over the past two years vs. 29% of others) and expect strong growth in the future
- ▶ Have more mature strategies for their digital investments and ways to execute them

Figure 1 below shows how digital leaders are boosting their resilience as they enter the next phase of the pandemic.

Figure 1: Leaders are future-proofing the enterprise

Q. Please rate the status of the following actions considered by your company regarding enterprise resilience.





Digital leaders have a strategic advantage

In addition to accelerating new digital products, services and business models, digital leaders are much more likely to:

- ▶ Have a clearly defined strategy for digital (48% vs. 36% of others)
- ▶ Reprioritize their digital initiatives to focus on those with immediate cash returns, while discontinuing unnecessary initiatives
- ▶ Dedicate funds saved to accelerate new digital products, services and business models
- ▶ Invest in the right emerging technology to execute on that strategy (53% vs. 45%)

That technology mix is more likely than others to include investments in IoT, cloud computing and advanced cyber defense – showing that digital leaders are creating a strong foundation (through cloud and cybersecurity) to rapidly accelerate emerging technology solutions (such as AI and IoT).

To meet their strategic goals, nearly three-quarters of executives say they are shifting to M&A and partnerships to accelerate digital initiatives (see Figure. 1) – on average, digital leaders are shifting approximately five percentage points of their investment mix from building internally to M&A. That shift is important, as the EY survey shows that these investment vehicles are more likely to perform above expectations (see Section 3, “Aligning on investment vehicles”).

For now, digital leaders are an elite group. Which digital leader traits can other companies adopt as they chart a path forward?

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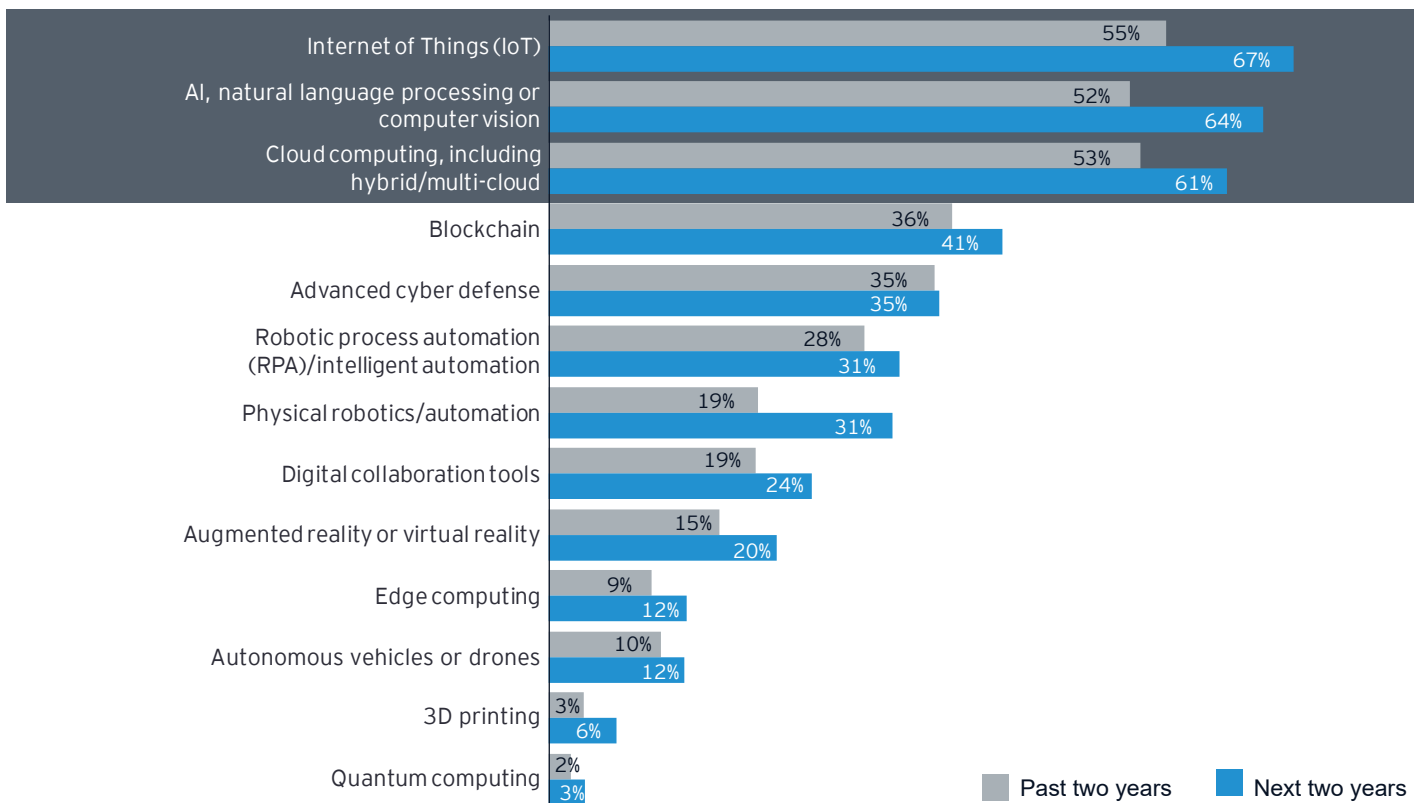
How to improve digital investment benefits

Futureproofing technology investments

Nearly two-thirds (62%) of executives agree that organizations must radically transform their operations over the next two years. To do that, executives are starting to turn to emerging technologies. Figure 2 shows that IoT, AI and cloud computing have become table stakes. Executives also predict large jumps in investments in automation and digital collaboration tools. While these investment plans are not on par with those of digital leaders, the gap is closing.

Figure 2: IoT, AI and cloud computing are table stakes

Q. In which of the following emerging technologies has your company focused its investments over the past two years and next two years? (Select up to five.)





Slow going on reaping technology value

Progress in realizing the full benefit from emerging technologies is slow. Just 15% of executives say they have realized the full value from their cloud investments – perhaps the most foundational of the table stakes, as it enables many other emerging technologies. Just 7% say they have realized the full benefits from AI and IoT. Most of these technology investments appear to be in the launch or acceleration phase – close to realizing benefits, but not quite there yet.

This survey shows similar results when it comes to progress in digitizing core processes across the organization, with just 2% realizing full benefits and two-thirds in the early development (34%) or launch (30%) stage.

Understanding what stands in the way of benefit realization

Those executives still in the development stage of digitization should be careful – 79% say that digital programs stall in that early phase. And the reasons are legion:

- ▶ 65% say digital programs stall due to lack of skills or talent
- ▶ 59% cite a lack of budget
- ▶ 58% cite poor-quality data or the lack of a strong data analytics function as top data-related challenges

The data piece of the equation is critical. Executives need to validate that data is shared easily within the organization by breaking down silos and supporting a strong data analytics function. Digital leaders pursue a dual track: focusing on short-term value where data is available today (e.g., pricing data analytics), while at the same time building the necessary data infrastructure for the future.

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Aligning on investment vehicles

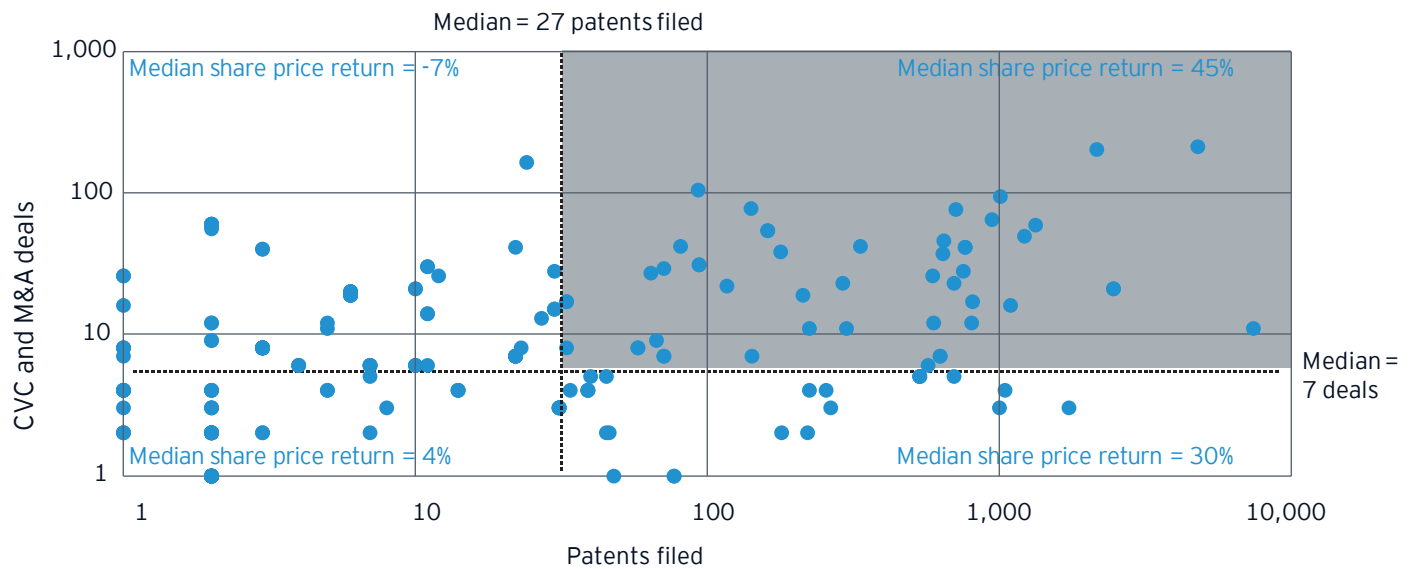
Shifting to digital M&A and partnerships

This survey shows that executives know which technologies they need to succeed in a digital future. But there is misalignment when it comes to the investment vehicles they use.

Additional data analysis from CB Insights shows that spending more on digital M&A, corporate venture capital (CVC) deals and patent filings may lead to higher median share price returns (shown in the upper-right gray quadrant, of Figure 3).

While balancing the development of in-house capabilities, as well as M&A, CVC and partnership investments, survey respondents are more likely to say digital M&A exceeded expectations (52%) than any other investment vehicle. (Partnerships come in second place, with 45% saying they exceeded expectations.)

Figure 3: Number of CVC and M&A deals vs. patents filed, by company
January 2017-August 2020





Executives need to be aligned on investment strategy

Digital M&A may be more likely to exceed expectations for some, but the risk of failure is high. A lack of executive alignment or collaboration may doom digital M&A initiatives from the start. Executives who report that digital M&A investments met or were below expectations cite misaligned sources of value as the top reason (64%).

That misalignment is concerning. With more than half of executives planning to use digital M&A or partnerships to accelerate digital initiatives, it is essential to make sure the goals and values of an organization and those of acquired or partner firms are coordinated. Internal alignment is also challenging – just 43% of executives agree that digital leaders from functional groups are fully aligned on their organization's digital M&A strategy.

Alignment and collaboration pay off. Executives who reported that partnerships and digital M&A met or exceeded expectations were significantly more likely to say that they were implemented by multiple executives (e.g., a combination of CFO, CIO and others).

In order to create an investment strategy that meets goals across the organization and adds value, executives need to be aligned around the mix of investment vehicles used by the organization – and continue that collaboration when it comes to taking ownership and directing those investments. Breaking down organizational silos and playing to executives' individual strengths (e.g., relying on chief digital officers to develop in-house capabilities, while tapping CEOs to lead on M&A) are the best ways to develop a successful investment strategy.

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Overcoming barriers to scale

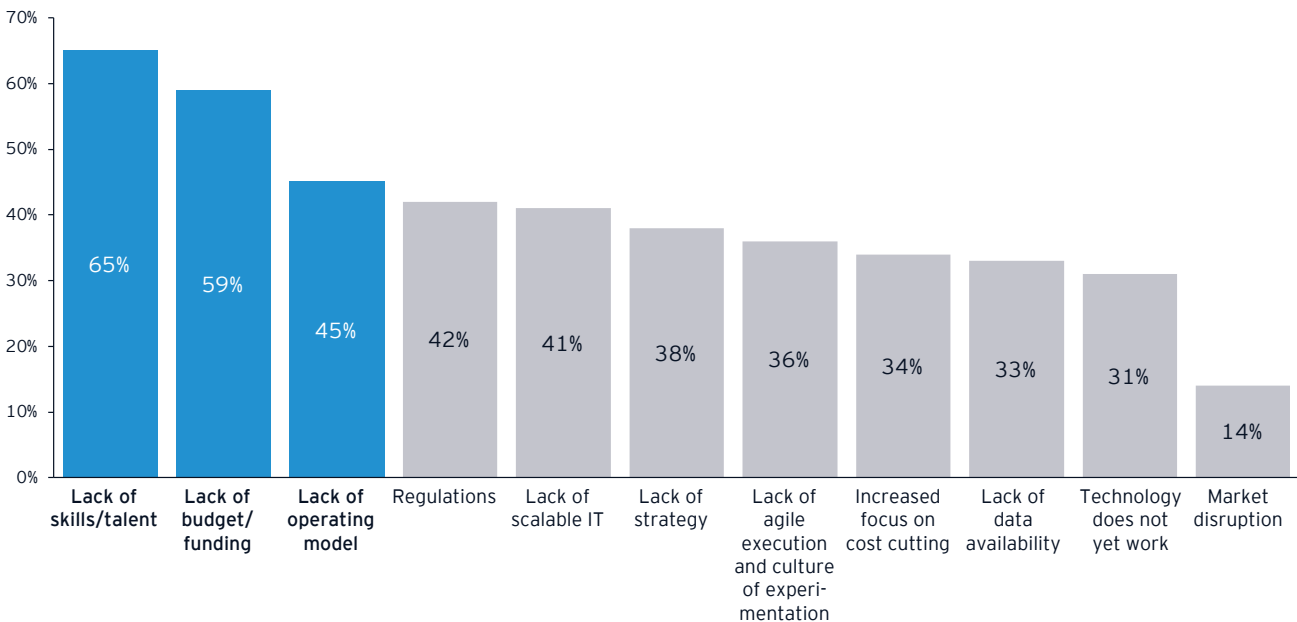
Lack of skills and budget stalls digital programs

Organizations without a clearly defined digital strategy are putting themselves at risk. But even the most flexible and technology-enabled strategies can be hamstrung by other issues. Figure 4 shows that a lack of skills (65%) and a lack of budget (59%) are the top barriers to digital programs, with a lack of an operating model not far behind (45%).

These barriers help explain why less than 10% of all respondents – including digital leaders – say they are currently realizing the full benefits of their digital efforts.

Figure 4: Skills, budget and operating model challenges hamstring digital programs

Q. What are the top reasons why your company's digital programs are stalling? (Rank the top three.)



Top barriers to scale

① Lack of funding

Insufficient capital can hinder the ability to grow from pilot project to scale. Proper due diligence, a clear business case and an understanding of internal competition for resources are essential prior to initiating new digital initiatives and investing significant resources.

② Unsuitable operating model

Companies must examine whether they have the right operating model in place prior to initiating new digital initiatives. The operating model must be agile and align to both the business and the IT structure currently in place.

③ Scarcity of talent resources

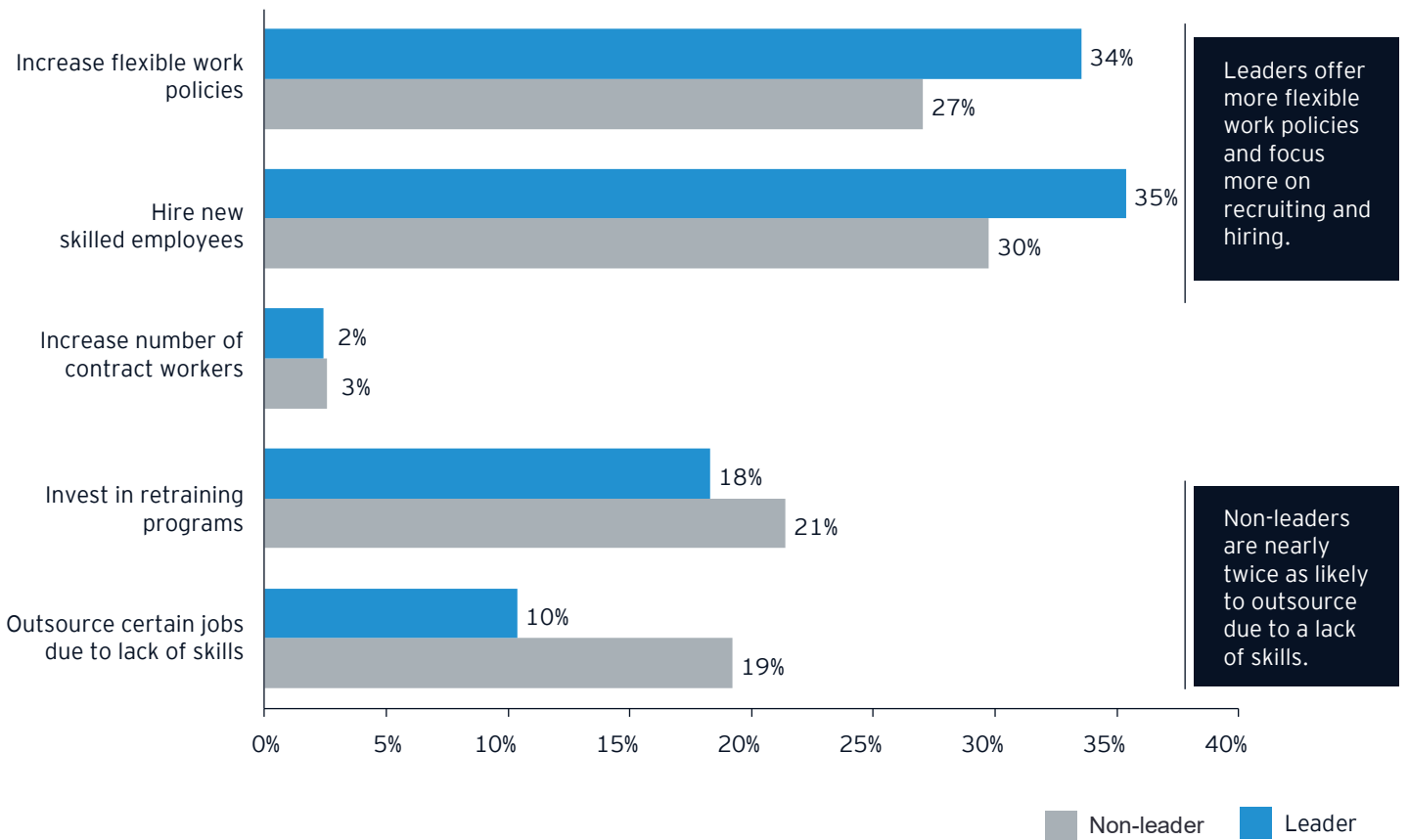
Competition for tech talent and data scientists continues even during the recent pandemic. Larger, traditional companies can't always compete against an exciting startup with an innovative environment. Companies should properly articulate the type of talent that they need and look at alternative sources, such as partnerships and acquisitions.

Skill at scale

To effectively scale digital investments, the organization needs to be empowered with the right skills. Figure 5 shows that the digital leader group is more likely to focus on hiring new employees to boost their digital skill sets, while non-leaders are more likely to be re-skilling existing employees or outsourcing.

Figure 5: Leaders look outside the company to obtain skills

Q. Which of the following has your company done to enhance the digital skills available to you?



To overcome key barriers to realizing value, companies will require highly skilled employees and an effective, flexible digital operating model. Yet, only half of executives say their operating model meets their goals. Operating model issues, combined with skills and strategy shortages, explain why many organizations are struggling to scale their digital initiatives.

Though the barriers are similar for new business development and core process digitization, the best ways to remove those barriers differ. For example, operating model issues for a new digital business may be better solved through a structured approach that can include creating clearly defined milestones, bringing in new native digital talent and clearly defining outcomes. On the other hand, digitizing the core may center around agile, cross-functional teams. Regardless of the objective, companies must be able to experiment and discontinue initiatives that are not working.

5

Establishing robust metrics

Return on digital investment: RODI advantage

In a cash-constrained environment, proving the value of all investments – including digital – takes on increased importance. While more than three quarters of executives say that digital initiatives have been critical to their organization’s success over the past two years, putting firm numbers on this success remains a work-in-progress.

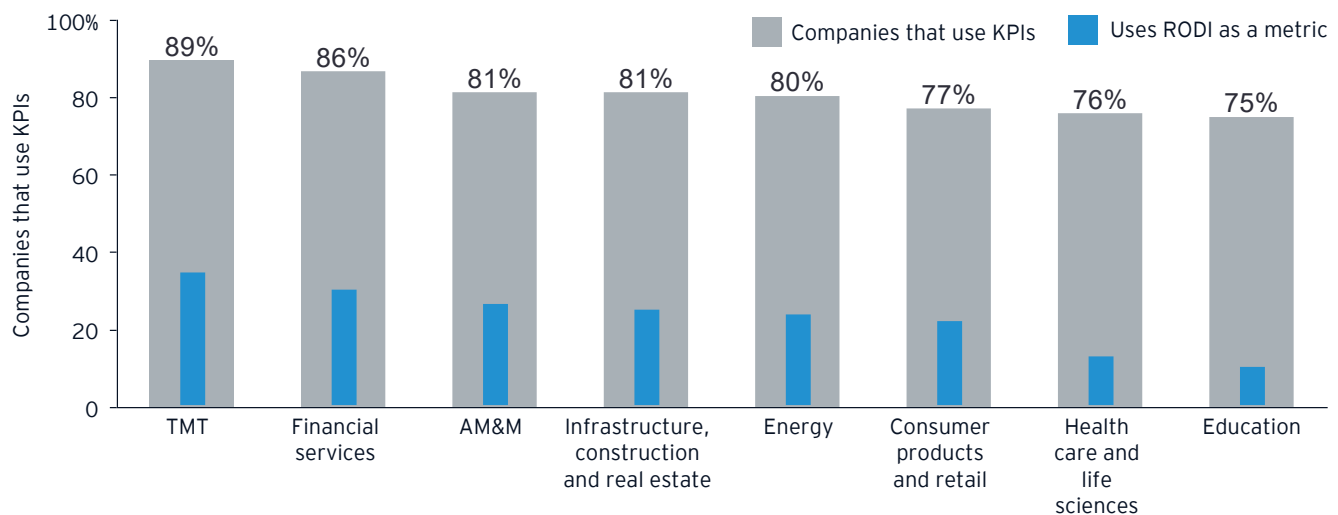
Less than a quarter of executives say they actively measure the return on investment for their digital initiatives, though other KPIs are more common, including KPIs about financial performance (57%) and operational efficiency (46%).

Although the ultimate goal is to measure the financial return on investment, in early stages of a digital investment there might be other operational KPIs to measure, such as user adoption, customer retention or user feedback.

Among the sectors represented in this survey, technology, media and telecom (TMT); financial services; and advanced manufacturing and mobility (AM&M) are the most likely to use KPIs in general, and around one-third of them use RODI as a measurement (see Figure 6).

Figure 6: Measuring RODI may lead to higher returns

Q. Do you currently measure the impact of your company’s digital investments?



Overcoming barriers to accurate RODI measurement

Measuring RODI is not always easy. More than half of executives say the lack of a clearly defined strategy and goals is a top barrier to measuring RODI. Companies must have an effective governance model in place to quantify success, focusing on results and scale.

Skills and data gaps often prevent companies from measuring the success of digital initiatives. Executives must work to obtain talented employees (through new hires or re-skilling), while breaking down intracompany barriers to data sharing so they can correctly measure their RODI and meet strategic goals.

Recommendations for executives

It is clear from the EY DII survey results that executives have work to do to improve their digital investments – and to accurately measure that payoff. We recommend the following actions:

1. Determine a clear strategy that details digital spend, technology requirements and a coherent path to execute. Few survey respondents say they have a clearly defined strategy, and even fewer say those strategies are flexible. Both are necessary to weather disruptions and succeed in the future.
2. Identify sources of funding early in the process and create the right interventions to ensure proper usage of funds.
3. Align executives on the right investment mix of “build, buy, partner or corporate venture” and develop an integrated approach to accelerate digital initiatives and achieve strategic goals. Depending on the digital initiative, tech requirements and internal capabilities, build, buy, partner may lead to different RODI and speed of implementation.
4. Revisit your operating model to ensure agility and that it can accommodate key external constituents for talent (e.g., ability to bring in and leverage strengths of external entities, including tech partners, startups and universities.)
5. Consider digital M&A as a means to further accelerate post-pandemic digital performance and use partnerships to close funding gaps.
6. Focus on hiring and retaining top talent, securing access to funding and improving operating models, while learning from the digital leaders to achieve the full benefits of digital investments.
7. Establish a strong governance model and KPIs to manage digital initiatives in order to accurately measure RODI, identify potential weaknesses in digital strategy, learn and adjust.
8. Rebalance your portfolio of initiatives during the pandemic. For example, cash-generating initiatives should be prioritized in the short term to fund future growth through new digital products and services.



About the survey

- ▶ EY teams have developed a global C-suite executive survey, the EY-Parthenon *Digital Investment Index*, to help management understand how to improve the digital strategy and enhance the RODI.

Survey details include:

- ▶ 1,001 C-suite executives: CEOs, CDOs (Chief digital officer), CFOs, CSOs, CIOs
- ▶ Conducted between September and November 2020
- ▶ Geography: 60% Americas, 20% Europe, 20% Asia-Pacific
- ▶ Company size: \$1b+ in annual revenue, one-third with \$10b+

Sector insights:

- ▶ Advanced manufacturing and mobility
- ▶ Consumer
- ▶ Education
- ▶ Energy
- ▶ Financial services
- ▶ Health care and life sciences
- ▶ Infrastructure, construction and real estate
- ▶ Private equity
- ▶ Technology, media and telecommunications

Produced in association with Oxford Economics.



CB Insights provided the following research:



- ▶ Assessed the digital transformation efforts of 224 companies
- ▶ Provided the underlying data on corporate investments, M&A strategy and patent filings
- ▶ Sectors and geographies were consistent with the Oxford Economics survey
- ▶ Technologies analyzed include, but are not limited to, cloud, AI, IoT, cyber, autonomous vehicles, robots, blockchain, augmented reality/virtual reality and robotic process automation.

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