CIOs Need an IT Financial Plan, Not Just an IT Budget

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Initiatives: IT Cost Optimization, Finance, Risk and Value

Annual IT budgeting practices alone do not support a longer-term impact assessment of the enterprise's technology investments. CIOs must construct a strategically aligned, contextualized IT financial plan to demonstrate IT's financial value beyond the annual budget cycle.

Overview

Key Findings

- Poorly forecast or unanticipated run costs arising from technology investments across the enterprise leave CIOs perpetually reacting to cost pressures during the annual budgeting process. This drives short-term, low-value, high-risk financial management decisions in order to meet annual budgeting targets.
- Annual IT budgeting practices do not support a longer-term or holistic impact assessment of technology investments across the enterprise.
- There is a growing appetite for technology investment among management boards and an expectation for the CIO to play a strategic role in investment decision making.
- Many CIOs remain under pressure to stabilize IT costs or even reduce them, even as enterprisewide technology investments increase and require additional funding for foundational and new IT capabilities.

Recommendations

CIOs seeking to establish effective IT financial management must:

- Demonstrate the value of IT's current spend and future, long-term investments against business outcomes by aligning IT's planned initiatives and spend to achieve the enterprise strategy.

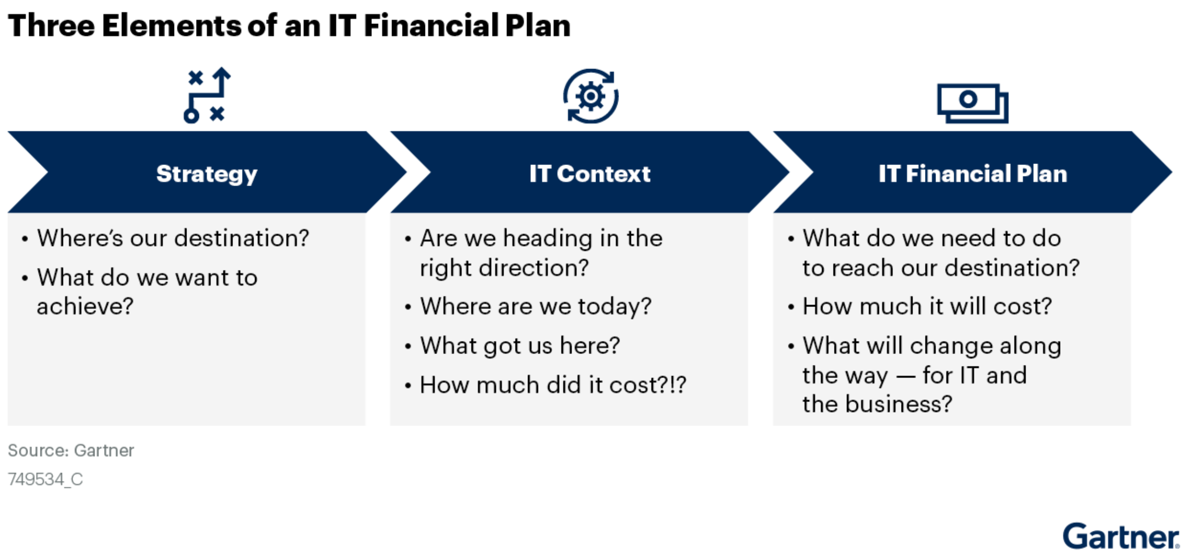
- Establish IT's context by creating a two-year retrospective view of IT's finances, a current baseline of IT's costs and the business services being delivered.
- Exhibit proactive management of current IT activity and spend, and anticipate the financial impacts of new, strategically aligned technology spend, by developing a strategic, contextualized, IT financial plan spanning at least three years.

Introduction

Annual IT budgeting cycles can restrict IT financial management to the cost-focused reporting requirements set by central finance for executive review. Our research shows that while IT perceives itself as effectively collaborating with finance on cost management, finance (and several other business functions) does not perceive IT in the same light. [1] Research with CFOs shows that during the budgeting cycle, IT is, in fact, perceived as siloed, technology-centric and short-sighted. [2]

To overcome these perceptions and significantly improve their financial management credibility, CIOs must develop a strategically aligned, contextualized IT financial plan (see Figure 1). This will enable them to demonstrate their effective management of the current technology cost base and their suitability to effectively govern and manage enterprisewide growth in technology investment. Gartner estimates that, worldwide, enterprise IT spend across all industry markets will increase 6.2% in constant U.S. dollars in 2021, with an expected 6.3% constant-currency, five-year compound annual growth rate (CAGR) through 2025 (see Forecast Analysis: Enterprise IT Spending Across Vertical Industries, Worldwide).

Figure 1: Three Elements of an IT Financial Plan



Three key mindset shifts are required for CIOs to succeed in implementing an IT financial plan (see Table 1).

Table 1: Three Mindset Shifts Required to Implement an IT Financial Plan

(Enlarged table in Appendix)

Mindset Shift	Commentary
IT's financial plan must have a broader focus than simply formal IT costs (see Note 1).	▪ IT does not operate or spend in a silo. IT must, therefore, involve various functions and disciplines to develop its financial plan and demonstrate the inherent financial and nonfinancial interdependencies between them. ▪ Articulate how IT's spending links to enabling business outcomes and, in turn, is impacted by business-led or strategic decisions.
IT "spend"/"cost"/"finance" must always be considered in relation to the activities, business-facing services and capabilities that IT delivers.	▪ IT spend should not exist unless it has a direct, causal link to a business outcome. ▪ To justify investments necessary to sustain "business as usual" operations, CIOs must connect them to the overall strategy (see How to Address 'Run the Business' IT in Strategic Planning).
IT financial transparency is about more than just cost. CIOs must have a strong, agile base of financial information (see Note 2).	Information required includes: ▪ General ledger reporting of all IT spend, enterprisewide ▪ Vendors and contract management ▪ Asset value and asset utilization ▪ Capitalization policies ▪ Strategic investment governance frameworks ▪ Benchmarking metrics

Source: Gartner (August 2021)

By succeeding in these mindset shifts and developing a strategic, contextualized IT financial plan, CIOs are better equipped to respond to business leaders asking for "higher value, more strategic things." [3]

Analysis

Align IT's Planned Initiatives and Spend to Achieve Enterprise Strategy

Enterprises should have only one strategy — the business strategy — and information and technology (I&T) must be a core part of it. This requires focusing the IT organization on creating a set of inputs, or key chapters, that are embedded directly in the business strategy (see Toolkit: IT Strategy Template — Embedding Information and Technology in Business Strategy). An effective IT financial plan will reflect, in terms of spend and investments, the IT activities that need to take place to implement the business strategy.

Close collaboration with business peers to integrate IT into the business strategy must go beyond an articulation of IT initiatives or technologies. Business peers who buy into IT's solutions and enablement need to be prepared to pay for the performance they want achieved. The IT financial plan articulates the price for that performance and forms the means by which the business is made aware of, and signs up to, the longer-term, technology-funding commitments.

The symbiotic nature of the strategic and financial relationship between the business and IT means that the IT financial plan must articulate the wider, less obvious financial implications of strategic alignment. In practice, this means two things (see Figure 2):

1. IT must think beyond the confines of its own budget to identify, articulate and communicate the total cost implications of technology.

    - Impacts to the CIO's budget accountabilities are captured in the IT financial plan, and are reflected in the near term in the annual IT budget.

    - Impacts to the financial accountability of other executives should be, at the very least, communicated to them, with the explicit expectation that they are captured in their own budgets and financial plans.

2. Requests for the funding of technology investments are no longer the sole purview of the CIO. Instead, they are made by the business executive in partnership with the CIO, who, together, in the wider funding discussions for the strategic initiatives, present both sides of the return-on-investment equation for the technology funding.

Figure 2: Wider Financial Implications of Strategy Articulated in IT Financial Plan

Wider Financial Implications of Strategy Articulated in IT Financial Plan

■ Financial impacts articulated by the IT financial plan and communicated to all relevant functions.

	Strategic Priority A				
	Led By	**Enabled By**			**Total**
Function	**Marketing**	**IT**	**HR**	**...**	
Direct Funding Required Years 1 to 3	$xxx	$xxx	$xxx	$xxx	**$xxx**
Indirect Tech. Financial Impacts (Cost and Benefits) Year 1 to 3+	($xxx)	$xxx	$xxx	$xxx	**$xxx**

E.g., Benefits from FTE efficiencies enabled by technology

E.g.,
- Run/Maintenance
- Licenses
- Upskilling/Recruiting IT Staff
- Training Users

Source: Gartner
FTE = full-time-equivalent
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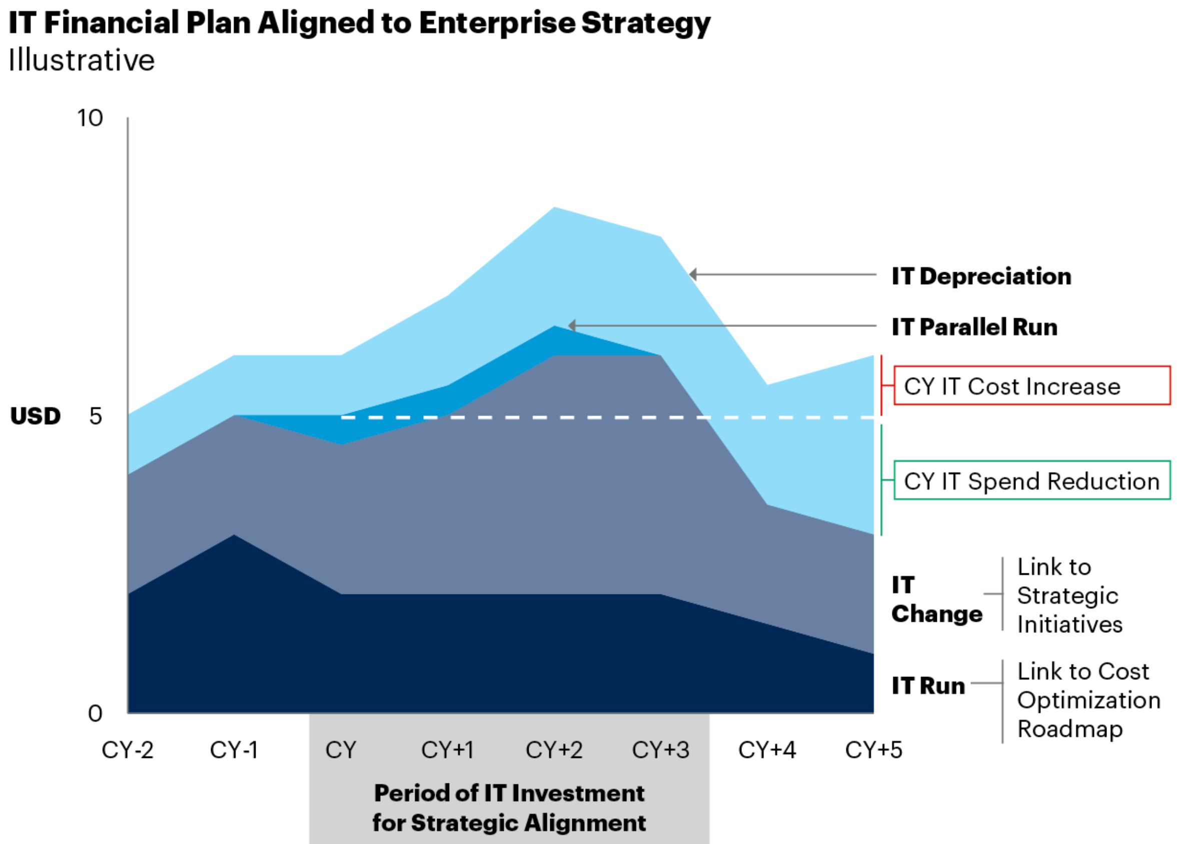
Strategic alignment forces a longer-term perspective. Proactive forecasting of the near- and longer-term IT funding required to enable the strategy, shifts IT spend discussions from those of cost, to those of value for the enterprise. This allows even “traditional IT” investments, such as infrastructure upgrades or data lakes, to be shown as forming the basis of strategic enablement and preparing the ground for the value of the future.

Establish IT’s Context via a Two-Year Retrospective View of IT’s Finances

A clear starting point or “baseline” is required to develop an effective IT financial plan. The baseline should set out, at a point in time, by defining how much is spent on IT and on what. Benchmarking exercises, like Gartner’s IT Budget & Efficiency Benchmark tool, provide a snapshot and comparison to peers of IT cost and enable an assessment of IT’s efficiency. However, the baseline for the IT financial plan is not only about efficiency. It is also about effectiveness. Current spend should be tied to current services, an assessment made of its effectiveness at supporting today’s business outcomes and its capabilities for enabling those of the future. Together, effectiveness and efficiency form the cornerstones of cost optimization and value enablement (see Expert Insight Video: IT Finance Training — Strategic Cost Optimization).

The baseline should be given a context by looking back two years. This is so that the CIO and executives can all understand what has led to the current state. While time should not be wasted trying to get a “perfect” historic picture, material financial impacts or variances should be highlighted and explained clearly in business (not technology) terms. This context provides a starting block for the link between IT costs and their business drivers; for example, highlighting the link between prior business-led capital expenditure (capex) investments and increased IT run and depreciation (see Figure 3).

Figure 3: Visual Summary of IT Financial Plan Aligned to Strategy



Source: Gartner
CY = current year
Note: Capital expenditure not depicted here as it would duplicate depreciation impacts
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The baseline forms the foundation of the IT financial plan. It can be used to identify and form plans to address current areas of ineffective and inefficient spending, as well as to identify and close the gaps in future IT-enabled business capabilities aligned to strategy (see Create and Communicate an Enterprise Cost Optimization Roadmap). As shown in Figure 3, optimization activities to drive efficiency or absorb new run costs can be immediately juxtaposed against the increased spending impacts of new, strategically aligned investments.

When forced into a “change nothing” scenario by restricted funding, the CIO can use the baseline to show how the run/change proportions of current funding levels will shift as increasingly inefficient technology absorbs greater resources, but delivers less business value. Alternatively, as represented in Figure 3, when facing a period of significant technology investment, the baseline can be used as a point from which changes to IT spend and progress in technology-enabled business capabilities should be measured and communicated.

Details from the IT financial plan on current-year/next-year spending should be carried through to the IT budget. The IT budget should be a more detailed reflection of the high-level, strategically aligned IT financial plan, and any changes agreed on in one should be reflected in the other. Use Toolkit: How to Present Your IT Budget to the Board of Directors as a guide for how to present IT budget movements to senior executives.

Develop an IT Financial Plan Spanning at Least Three Years

Additional IT costs resulting from business decisions (but often incurred much further down the line), are captured in the longer time frame of an IT financial plan. As shown in Figure 3, the high-level, long-term view of IT spend (excluding depreciation) and IT cost (including deprecation) can provide a very quick and visual reflection of the overall financial impacts driven by the strategic investment decisions being made.

The planning process that drives the IT financial plan (and in turn, the IT budget) must be led by and owned by IT. Highly visible and active involvement by the CIO and IT leadership team will immediately elevate the importance of the IT financial plan and drive focus across the IT function. Do not assume it is the role of the accountants on your team to lead or develop the IT financial plan. They are likely to have a role in terms of process governance, data collection, consolidation and reporting, but the plan must be driven by and owned by IT as a reflection of its alignment to business outcomes. Table 2 shows the improvements driven by a shift from annual budgeting to IT financial planning.

Table 2: Improvements in IT Financial Management Enabled by an IT Financial Plan

(Enlarged table in Appendix)

	From: Annual Budgeting	To: IT Financial Plan	Improvement
Financial scope and perspective	▪ Traditional IT costs ▪ IT as a cost center and service provider	▪ Traditional IT costs ▪ IT-business financial interdependencies	▪ IT spend is synchronized to technology impacts happening outside of IT ▪ Fewer "surprises" for IT to fund business-demand-driven run costs
Time frame	▪ Current Year	▪ Prior two years to three years or more	▪ Longer-term financial perspective to better inform and challenge short-sighted decision making ▪ The budget shows an annualized view of a long-term financial plan; it should not be viewed in isolation without the context of a longer-term time frame (over three years)
Perspective	▪ Internal to IT	▪ Outward-looking ▪ Strategically aligned	▪ IT utilizes strategic context to build financial plans and better integrate with the enterprise ▪ Improved funding prioritization and trade-off discussions ▪ IT plans and financials become less technology-, and more business-focused ▪ Reduced "shadow IT" through increased IT responsiveness and articulation of total technology cost impacts
Accountability	▪ CIO control and accountable	▪ CIO control ▪ Increasingly shared accountability for funding with business peers	▪ Technology funding requests made by the business executive in partnership with the CIO, presenting both sides of the ROI equation
Implementation	▪ Finance/accountant-led	▪ CIO/IT leadership-team-led	▪ Improved alignment of spend to IT activity ▪ Ultimately enables better alignment of IT spend to business outcomes and the business value of IT
Involvement/inputs from	▪ IT budgetholders	▪ Cross-IT involvement from IT operations (including business analysts, IT program/project management office, IT HR and sourcing, procurement and vendor management) ▪ Early, reciprocal and active involvement of business units, business functions, product owners, corporate finance	▪ Improved IT accountability and connection to business value ▪ Flexible, responsive IT financial plan, reflective of business decisions and changes ▪ Near- and longer-term financial impacts of nonfinancial constraints and operational decisions articulated and built into the plan

Source: Gartner (August 2021)

Cross-IT and business stakeholder involvement is vital in the IT financial plan process because technology funding is not the only potential constraint to the effective implementation of an IT plan. Other constraints — such as availability of skilled resources or the capacity of business units to adopt technology change — will all impact implementation and IT cost.

Constraints mean choices will need to be made. For example, the changing shape of a deployment plan to accommodate market/business-unit—specific constraints will drive near- and longer-term financial impacts in IT. While it may be assumed deployment plan changes will be agreed at the project or program level, it is important to feed impacts of changes into the wider IT financial plan. Here, their upfront articulation can instigate discussions about the desired balance between business risk, business value and increased IT cost.

Brought together, a contextualized, strategic IT financial plan will be a key tool for the CIO to communicate the financial implications of IT's enablement of enterprise strategy, enabling better informed executive decision making.

Evidence

[1] The 2020 Gartner Business Cost Optimization Through a Crisis Study was conducted to understand how organizations' cost management practices before and during the COVID-19 crisis allowed them to be ready for the rebuilding phase into the "new normal" (see Cost Optimization Lessons Learned Through a Crisis).

The research was conducted online from August through October 2020 among 314 respondents from North America, Europe and Asia/Pacific, across all industries, except government, and in organizations with annual revenue of at least $250 million.

Respondents were screened for involvement in enterprisewide cost management in their organizations. The study was developed collaboratively by Gartner analysts and the Primary Research team (see Figure 4).

Disclaimer: Results of this study do not represent global findings or the market as a whole, but reflect the sentiment of the respondents and companies surveyed.

Figure 4: Cost Management Collaboration Ratings Across IT and Other Functions

Cost Management Collaboration Varies by Function

Percentage of Respondents Rating Their Cost Management Collaboration as High

- Relatively Low Collaboration Perceived Between Functions
- Moderate Collaboration Perceived Between Functions
- Relatively High Collaboration Perceived Between Functions

A's perception of collaboration with B	A: Finance n = 39	Supply Chain n = 36	IT n = 40	Customer Service n = 32	Marketing n = 40	Sales n = 37	Human Resources n = 40	Operational Roles n = 40
B: Finance	-	69%	83%	81%	65%	65%	78%	74%
Supply Chain	55%	-	58%	62%	42%	54%	54%	46%
IT	51%	42%	-	66%	48%	30%	68%	55%
Customer Service	50%	31%	62%	-	48%	44%	44%	56%
Marketing	47%	31%	55%	32%	-	58%	38%	40%
Sales	43%	33%	53%	43%	54%	-	32%	38%
Human Resources	59%	42%	60%	53%	45%	54%	-	50%
Operational Roles	67%	75%	68%	59%	51%	41%	65%	-

n = varies, excluding not sure

Q: How would you rate the level of alignment and collaboration between your function and each of the following functions in support of cost management?

Source: 2020 Gartner Business Cost Optimization Through a Crisis Study

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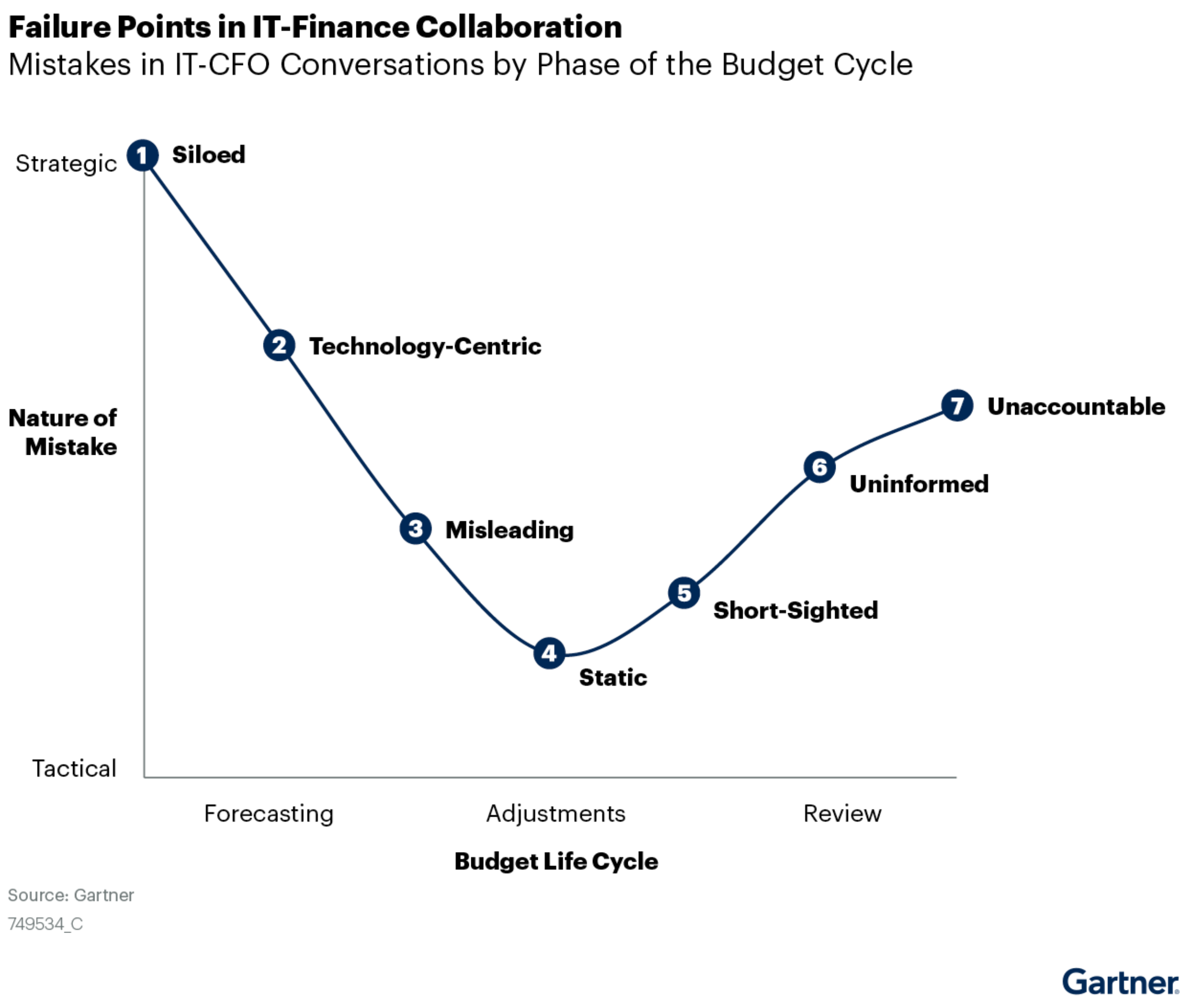
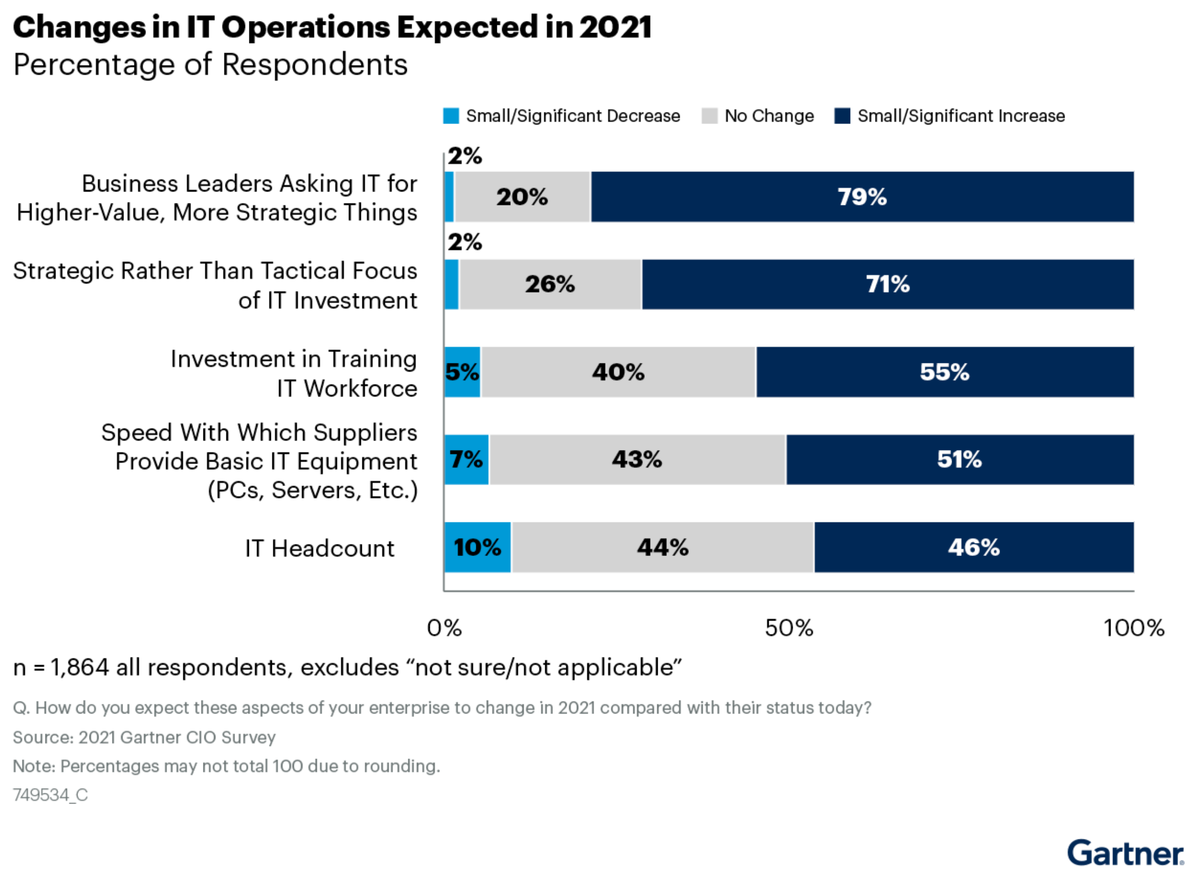
[2] Tool: CFO Presentation Template for CIOs (see Figure 5)

Figure 5: Failure Points in IT-Finance Collaboration



[3] The 2021 Gartner CIO Survey was conducted from 14 July 2020 through 14 August 2020. A total of 1,877 respondents participated. The respondents were members of Gartner Executive Programs and other IT leaders, primarily chief information officers (see Figure 6).

Figure 6: Shifts in IT Posture



Note 1: IT Costs

Formal IT costs are defined by Gartner in IT Key Metrics Data 2021: Industry Measures — Framework Definitions as "IT spending that the IT department is accountable for. The IT department is answerable for the provision of these IT assets and services."

Note 2: Six Pillars of IT Financial Transparency

See 6 Pillars of IT Financial Transparency Drive Business Value. These six pillars drive financial transparency and form the foundation for demonstrating the value in IT's spend. Competency in these six pillars forms the basis of the CIO's financial credibility to take on responsibility for more investment and partner effectively with the business to deliver the outcomes of digital transformation.

Recommended by the Authors

Some documents may not be available as part of your current Gartner subscription.

6 Pillars of IT Financial Transparency Drive Business Value

Expert Insight Video: IT Finance Training — Strategic Cost Optimization

Key Concepts in IT Financial Management: Budgeting, Transparency, Allocation and Funding

Expert Insight Video: The 2021 CIO Agenda: Seize This Opportunity for Digital Business Acceleration

Business-Led IT Spend Reaches a Tipping Point — CIOs Must Lead

The 9 Rules for Demonstrating the Business Value of IT

From Partner to Trusted Ally — How to Stay Relevant as a CIO

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