

Irrational Digital Exuberance

Getting real about digital transformation and getting it right

An ISG Focus Paper

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Talking it through

At ISG we believe in dialogue. It's the basis of any good relationship. The best way to work through strategies, issues and objectives is to gain valuable insights that can make a difference to any organization.

We brought together five of our most experienced people to examine the idea that, perhaps, there's too much exuberance around digital right now. Could we call it 'irrational'? Is digital-optimism well placed, but just needs a reality check and some sober examination? Both are important questions.

This is the second in a series of Focus Papers, capturing the views of some of ISG's most experienced advisors. The participants are:



John Keppel
President EMEA & Asia



Lois Coatney
Partner & Head of
Strategy & Operations



Harald Wolf
Partner, ISG DACH



Owen Wheatley
Partner & Head of Banking,
Financial Services & Insurance



Steven Hall
Partner & Head of Digital
Advisory Services

Their views are personal but relevant and sometimes controversial. Feel free to agree or disagree. Let us know what you think.





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What is 'Irrational Exuberance'?

Exuberance drives markets. It's an essential element of innovation and change. It's what fosters creative risk-taking. But – and there's always a 'but' – it often goes too far. Bandwagons roll too fast, too many people try to jump on them and the inevitable crash happens.

The concept of 'irrational exuberance' is an old one. Go back to the South Sea Bubble and the Tulip Mania, and you'll find many examples of bad business practices (and downright dishonesty) that match anything we've seen over the last century or so.

The phrase hit the headlines when the then Chair of the US Federal Reserve Board, Alan Greenspan, used it during a statement on December 5th 1996. He was trying to explain the inexorable rise of global stock markets. Greenspan was worried that there was no basis to the Bull Market, so he delved into his economic history and uttered the phrase. Immediately, stock prices slumped: by 3% in Japan, 4% in London, and the Dow Jones slipped by 2.3%.

Greenspan proved the point. The markets were being powered by exuberance rather than underlying economic strengths within the global economy. The furor over his comments died down, the markets continued to be strong and were then boosted by the Dot-Com Bubble. Another example of 'irrational exuberance.' And a better one. The mere addition of a '.com' to a company name attracted investors who knew nothing about digital technology or the burgeoning Internet economy.

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Shiller focused his argument on how ideas become seen as fixed truths. For instance, the idea that stocks always go up after a crash.

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Nobel Prize winning economist, Robert J. Shiller, then wrote a best-selling book (unusual for a volume of economic theory) that cemented the phrase into popular folklore. In 'Irrational Exuberance'¹ Shiller defined the concept as a 'euphoria' and a 'madness':

A situation in which news of price increases spurs investor enthusiasm, which spreads by psychological contagion from person to person and, in the process, amplifies stories that might justify the price increases and brings in a larger and larger class of investors, who despite doubts about the real value of the investment, are drawn to it partly through envy of others' successes and partly through a gambler's excitement.

Shiller focused his argument on how ideas become seen as fixed truths. For instance, the idea that stocks always go up after a crash: "That is something people believe they have 'learned' from the past – and so it becomes a fact because everyone says it is true. But it is not a fact."²

And Shiller has the figures and charts to prove it. But, many people still believe it.





Irrational Digital Exuberance – really?

So, what has this to do with digital? Well, quite a lot. Every business believes that it is in danger of being 'disrupted' by a digital competitor.

A newly formed company (or one, like Amazon that seems to be able to shape-shift into any kind of provider of goods and services at will) unencumbered by legacy systems or any kind of physical infrastructure can take over a sector or – as Steven Hall puts it, 'Uberize the hell out of our business!'

That fear then drives optimism about how digital transformation can help protect long-standing companies from disruption. The very fact that the words 'digital' and 'transformation' are often paired together is, in itself, a form of optimism. You get digital – you achieve transformation. You become something shiny and new, totally agile and competitive.

We all feel as if we are in a new world and a new age. According to Shiller, that's an essential element of irrational exuberance: "It is the sense that we are all suddenly learning important facts, and have arrived at a new enlightenment."³ Shiller argues that the rise of this kind of certainty is a clear sign that a period of irrational exuberance has begun.

Shiller's conclusion is simple: "We have to consider what we as individuals and as a society should be doing to offset some of the ill effects of this exuberance."⁴

And this is where the ISG team comes in; do they think we're living in an era of Irrational Digital Exuberance?

There's a big difference between exuberant optimism and pragmatic optimism



Let's be clear what we're talking about.

"None of us are pessimists," says John Keppel. "We are all optimists." Steven agrees and then claims the mantle of being 'the most optimistic guy at ISG' – "Digital is transformative. It is a big deal."

"We need to step back a little," says Harald Wolf, "And realize that we are in the typical 'hype-phase' that all new eras go through. The exuberance about digital is based on hype from, well, the people who sell the digital tools."

Lois Coatney agrees that the optimism around digital has a firm basis in fact, but she sees it from a slightly different perspective: "People out there are anxious about disruption. They keep hearing stories about

companies like Kodak that didn't understand digital, and made the wrong choices. So, they're in a rush. They're anxious. Very anxious!"

Owen Wheatley is more skeptical about the idea of 'exuberance'; "I'd prefer to call it 'naive optimism', he says. "People look at what their peers are doing – or say they're doing – and they tell their IT people, 'I want one of those,' but without really working out why they want to go digital. The point is to start with a business strategy, and then match the technology to the outcomes you're after."

John is eager to make it clear that there is no doubt about the impact of digital technology on every sector of the economy; "This is not a fad. Sure, there's hype, but it's fading. That's a good thing. Optimism isn't fueled by hype, it's underpinned by how our lives are changing day-to-day, and digital tools are changing our lives – each and every day."

Owen agrees, "It's definitely not a fad. It's going to be here tomorrow – and much more of it. The problem is that suppliers are crawling all over clients trying to sell them new solutions and some companies are buying things they don't really need."

Lois agrees, "That's exactly right. But it's also because the people we speak to everyday, the people who have to run well-established organizations, use digital tools when they're outside the office that they know could help their companies do more. It's easy to get impatient. 'Why can't we just transform our business and get ahead of the curve?' Problem is, that's the hard part."

"That's where the need for pragmatism comes in," says Steven, "And that lack of pragmatism is what makes some companies' exuberance about digital irrational: they want the technology but don't know what business problem they're solving or what new business they should enter based on the evolving technologies."

“You need a strategy and you need a way of executing it properly,” says Steven.

“I think you can use the whole cloud euphoria we experienced recently,” points out Owen. Steven nods in agreement, “Definitely.” Owen continues his point: “People decided that they had to put everything into the cloud, and they rushed into service agreements that turned out to be totally unsuitable. There was no real understanding of how to leverage the cloud - or more particularly, which type of cloud - for the specific business needs.”

“Yeah, they drank the cloud Kool-Aid’,” adds Steven, “And quite quickly, the bills start to come in, and the regulatory people start to ask questions, and it turns out the strategy was not thought through properly, and instead of saving money and boosting efficiency, it’s doing the opposite.”

“Steven is a big optimistic pragmatist,” says John, “Just as we all are.” He pauses, then gets serious: “You’ve got to look at the reality of our world right now. It’s a fact that the IT services industry and IT skills and capabilities are now at the very forefront of most industries and business ambitions. For many years, computer systems were about plumbing - helping out in the back office -

and for most organizations they didn’t really have any impact on revenues. Even in retail, which is a sector that’s really worked hard to exploit digital: really, it’s just another shop front, with revenues moving from one channel to another. But now you have organizations that really haven’t embraced digital before and now believe that digital is the way they can engage with customers, connect with revenue streams, and open opportunities to capture entirely new revenue opportunities. That’s why they’re so eager to jump on the bandwagon.”

So, it’s ok to be optimistic, just not exuberantly so?

“Yes, but it’s hard to cut through the hype,” says Lois, “And it’s important to do just that. The hype creates anxiety. People don’t want to be left out in the cold. This affects their strategic vision and their decision making. They start to think in big leaps, but you don’t have to do that. Big change causes anxiety. You need to step back and figure out the key areas in your business where digital can have an impact. And start there. We need to remove the stressful feeling that you’re way behind and that you need to jump on the bandwagon. Take the time to look at your own business - find one or two areas to start your transformation in... and chill.”

Harald agrees, “Hype makes you want to go too quickly, that’s exactly right,” he says. “I worked with a major

brand which had been sold on the idea of Big Data. Everyone was telling them that it would transform the way they made their products and how they would also collect so much data that they could monetize it. So, they rushed out and created a Big Data Lab. They spent a lot of money on it. Now, two years later, it’s yielded nothing valuable... not yet, anyway. The decision was made too fast.”

“It’s our job to use our unique view of the market and the technological landscape, to temper enthusiasm and optimism with practical reality,” concludes Owen, “The objective is to help clients achieve the future they need - quickly but properly.”

Pragmatism can generate optimism, but it’s also important to be clear about where you want to go, and where you are now. And you may not be where you think you are.



Striving for 2020 but still working in 1999

Step back, understand where you are, and where you need to go.

“People get frustrated; I get that. It’s natural,” says Lois. “They’re being sold digital transformation but they’re working with legacy systems that seem so slow to change. It’s like they wish they could deliver 2020 right now – but they feel like they’re still working in 1999. It’s hard to get perspective.”

“You are where you are,” says John, “You need someone to tell you that. To help you step back and gain the perspective you need to make the right decisions about digital. That’s what I always hope to do for clients.”

“You have to get past what I call ‘The Barron Effect’ – the fact that most of the C-Suite are reading these great stories about what their peers are doing, and they feel left out,” says Steven. “The pace at which tech has moved,

especially over last 10 years, means that many business leaders believe that they can create completely new biz models. So, boards are looking at that prospect, fearing that they could be ‘Uberized’. Which is an irrational fear in my opinion. It’s completely over-played. Of course, there are some businesses that could be, but the threat is being used as a call to arms to sow fear, uncertainty and doubt. But I think, honestly, the threats will come from competitors within your own industry rather than from totally new entities.”

John agrees, “That’s another aspect of how we’re living in 1999 instead of in the present. Back then the Dot-Com boom led too many people to make bad decisions. Because most companies don’t have digital competency in-house, they have to build a wider ecosystem of partners. That means that, all of a sudden, they become integrated with partners in terms of what their future business model looks like, rather than just working with them as suppliers.”

“Now, they don’t have the same control as they used to, so they need to learn how they’re going to drive the new operating model that they are creating for a digital environment. That’s a huge challenge,” says John.

“It’s not just about choosing the right people; it’s about being able to converse with new partners as part of your business ecosystem. You have to be able to have relationships and run them so you get the best out of each of them for your own organization.”

The point is to step back and get the broad perspective needed to make the right decisions before committing to specific technologies and tools or suppliers.

“You’ve got to link the strategies together coherently; business vision to digital strategy to IT strategy to sourcing and implementation strategies. That’s a lot of strategies, but if they work seamlessly, they deliver results,” says Owen.

“To me the biggest hurdle is understanding how you actually incorporate the vision you want to achieve into the way a company operates,” adds Lois, “It’s the reality of implementing digital inside the business, with all the

different platforms, the new governance implications, the myriad of impacts on the way people work.

I mean, all of a sudden it opens up the need for a lot of work-arounds and changes that need to take place to really get the whole effect of digital. And, so often, it all gets diluted. You need to be specific. And definite. Understand where you want to be and then work out exactly how you want to get there. Make the investment that needs to be made. If you don’t then people end up being disappointed, and that’s the ‘gotcha’ moment you want to avoid.”

“Which is why they need someone to help them,” says John. Wise leaders have always employed advisors willing to question the current wisdom, and challenge the optimists. They also must be brave enough to tell the truth about the real state of affairs within a kingdom – or, of course, an enterprise. That’s the way you can winnow out the distractions and base your vision on how your company is actually working right now.





Take advantage of the new but keep the old going as long as it needs to go

“You know you need to change, you want to be optimistic and you want to get on this journey – organizations have to do it, but at the same time you have to be balanced. Do you go all the way or do you focus digital on key areas?” asks Steven, rhetorically.

Lois answers the question simply: “It comes back to Owen’s point, what’s the business outcome you’re after? You don’t have to transform everything, that would be a huge and risky undertaking. Look at the new technologies and see where they can be best used to achieve your specific business goals.”

Owen likes the way the conversation is going: “This is a crucial point, and it’s important that clients understand that ‘digital transformation’ isn’t an ‘all-or-nothing’ concept. It’s something you can do incrementally.”

“Take advantage of the new, but keep the old going as long as it needs to go,” says Lois.

“Exactly. For me it’s the manifestation of a Bi-Modal IT approach – or Two-Speed IT,” says Owen, “It’s not a negative concept, but a very positive – and pragmatic one. It’s based on being honest that your legacy platforms and applications constitute a whole spaghetti of complexity.”

“It might be too costly and risky to transform all of it, so in terms of improving customer experience, spend on digital is often better invested in the front-end. In the banking sector that’s been done by creating online and mobile banking apps, for instance. I mean, when was the last time any of you actually wrote a check or went into a branch to deposit one?”

There’s a pause, everyone nods. It’s a rare occurrence now. “But the branches are still there. The incumbent banks are cutting their numbers, but they can’t do away with them. The new wave of digital banks don’t have that legacy to worry about, but they also don’t have the depth of brand awareness and the backing that the big banks have. So, the incumbents can continue to use their legacy systems and slowly transform them. But they can also do interesting things with their branches.”

“Barclays is doing just that. They have teamed up with Amazon to put in click-and-collect lockers in their branches. That brings people in to the heart of the brand even when they do all their banking online. So, it’s using the digital realm to create new selling opportunities – once the customer is into the bank... there’s a chance they might open an ISA or think about moving their mortgage. Clever.”

Clever and entirely pragmatic.



Pragmatism underpins digital optimism

The joys of realism.

Steven is eager to turn that pragmatism into practical steps, and he does so: “For me, there are three components you need to think about: your digital backbone, your digital insight strategy, and your omni-channel approach. You’ve got to look at it all holistically, and have all the information you need. And that means realizing that, working in isolation, you don’t. You need someone who has that market perspective.”

Owen adds, “It’s not just about the disruptive competitors – the digital start-ups in your market. It’s about your traditional competitors too. They might be ahead of you. That’s more dangerous, in my opinion.”

“Yes, this isn’t fantasy land anymore – this is happening now,” stresses Steven, “The points I mentioned are the things you must think through thoroughly to make your digital future real.”

Harald offers an intriguing image; “We need to be the stern uncle who asks the hard questions. Set up a group – a lab – and let your people play with digital so they can find out what can be done, but don’t expect instant results, or try to change the fundamental processes too quickly. Be the stern uncle.”

Everyone is relieved, they thought he meant that ISG had to take on the avuncular role. “No, we help the CIO or the CEO to do that. The uncle needs the right information!” Harald explains that each ‘lab’ or group has to be given targets and a point needs to be set where measurable outcomes should be obvious. “You need to build a structure to do that,” he says, “And ISG helps clients do so and, in parallel, ensure the management function works smoothly. That’s what a lot of clients don’t do. They’re too focused on playing with digital. You need to manage the way you play. Sorry, but the stern uncle has to keep a close eye on what’s going on!”

John says, “To build on Harald’s idea, it’s about approaching this in a grown-up way. I don’t mean that in any patronizing sense. What an organization has to do is stand back and look at the whole thing holistically.”

“Create a picture of the operating model of the future. And by that I mean, the digital operating model for your organization as compared to the one you have now. You might have digital now, for sure. But if we want to operate more digitally, you need to specify what attributes you need, what organizations you need to partner with, and how you support those partnerships.

You also have to be explicit about the cultural attributes and skills you need. And investigate what your current weaknesses are and the existing areas that you want to change. In short, you need to do the essential blocking and tackling work,” says John.

But wouldn’t that slow everything down? “Well, you’re free to go fast and fail,” answers John. “That’s an oft followed business practice. Plenty of people do that. No one really wants to go fast and fail. It’s either go fast, fail and fix it. Or it’s stop, think and move at a sensible and steady pace that’s right for your organization. A pragmatic one, that’s informed by the learnings that exist around you, rather than ignoring everyone else and charging straight into the unknown.”

After a pause, everyone thanks ‘Uncle John.’



In 'digital-land' is in-house pragmatism enough?

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But today, you have a lot of SaaS and cloud providers, so the barriers to entry are much lower suddenly, and there are lots more options. That compounds the difficulty our clients have.

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The challenge for the modern CIO, CTO and CDO.

Owen is clear that it isn't. "In-house expertise is just that, in-house. It's great for the organization as it stands, but sometimes clients require a broader perspective, across your sector, across different markets, and across all suppliers and their technologies. You just can't do that in-house."

"The market is moving so quickly that it's almost impossible for the C-Suite to keep up. IT departments are focused on BAU, and so the digital vision has to be worked on in conjunction with consultants who can bring in that wider view," says Steven. "Our research capabilities combined with our practical experience – well, it gives them what they can't get elsewhere."

"CIOs don't have the time to look at lots of vendors," Lois says, "They need someone who knows more than you can get from a McKinsey article or a Gartner Magic Quadrant. They need someone who sees it all and has the practical experience. Someone who can connect them with that market and can get them the expertise they need in a practical, operational way. Simply put, they don't know what's out there. How could they?"

Steven amplifies the point: "In 'digital-land' the ecosystem is changing rapidly. For instance, if I was an established ERP provider it used to be that the barriers of entry into my marketplace were high – so you had few suppliers – in ERP it was Oracle and SAP right? So, not a lot of options. But today, you have a lot of SaaS and cloud providers, so the barriers to entry are much lower suddenly, and there are lots more options. That compounds the difficulty our clients have."

“There are so many different things to consider. Each has to be examined from the point of view of the business case or Total Cost of Ownership, and so on. A lot of work! That’s what we can do – and that’s very valuable,” says Steven.

“Because of speed of development in ‘digital-land’, as you call it, the nature of the role that the CIO has to do has changed. It’s not a failing of the CIO, it’s just the nature of the world we’re in. It’s a different world and this is how we have to work,” says Owen. “That’s why you’re seeing more and more Chief Digital Officers. They’re responsible for the vision and then they have to work with the CIO and CTO to make it happen.”

“That’s more people, but they still need help,” stresses Lois. “‘Digital-land’ is a hyper-agile, hyper scaled environment, where there are just so many options. They change weekly almost. If you look at any of the technology magazines the number of new solutions you have to keep up with can be mind boggling, even for consultants. But you have to keep up. A lot of CIOs need help to do that.”

“It’s their ‘secret sauce’ that needs to be protected,” says John. “The essential components they want to keep in-house and they need help to do that. We get in the middle, and help clients find the right partners to work with, and the right models so that they can exploit what those partners offer fully.”

In the end, it doesn’t matter where the wisdom comes from, so long as there’s enough wisdom to avoid mistakes, and move forward with decisive confidence.



It's time to industrialize digital

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If you look at a Google datacenter, everything is streamlined and standardized: the reason is simple – it's the only way to manage this amount of IT with an acceptable level of effort.

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Standardize without compromise.

This is Harald's big idea. So, he waxes lyrical.

“It's important to create a permanent, efficient, structure that works into the future. That overcomes what is, in my opinion a big challenge: current IT is still not really industrialized. I believe that IT is between the 'craft' phase and the 'industrial' phase, and we need to move it forward so it becomes far more standardized and repeatable.

“It's like the car industry. When it started it was a craft – workshops that made elegant carriages, unit by unit, building the technology as they went. Then it was brought into the era of the production line, and production was refined and refined until now when it is a totally repeatable production process that has many standard components.”

“This is what we need to do with IT and with digital. If we don't, then the complexity of IT will increase to a level where you will not be able to manage it all if you have non-industrialized IT behind it.”

“Without introducing a much higher level of discipline, standardization, and process driven organization – you won't be able to manage IT digitization. If you look at a Google datacenter, everything is streamlined and standardized: the reason is simple – it's the only way to manage this amount of IT with an acceptable level of effort.”

Owen thinks Harald has a point and adds, “When digital delivers business as usual (BAU), then you know it's standardized.”



Live forwards, understand backwards

Don't stress – you have time to be digital.

So where does the conversation leave us? How does an enterprise understand the future, when the future is still speculative and full of unknowns?

The Danish philosopher, Soren Kierkegaard famously pointed out that, 'Life must be understood backwards... but must be lived forwards.'⁵ You have to make choices based on experience, but without any real certainty. That dilemma is even more challenging in the digital world (Steven's 'digital-land') where everything moves at lightning speed.

"In the face of rapid change you have to be collegiate," says Steven. "Get advice, broaden your perspective and don't try to go it alone. You will still get CIOs who say there is no way we can do this, we don't have the systems and the people to do this. You can't just say

replace it all. So, at ISG we help them create a roadmap – and lay out, for instance, the five things they need to get started with today. That relieves a lot of stress".

"When you think you're being left behind, or you're not sure if you're missing out on the best technology, you get stressed," Lois says. "I say, there's time. It's not a sprint, it's a marathon. Maybe a half-marathon. But there is time. Be pragmatic. Be collegiate. Create an ecosystem of suppliers and partners that provide the firm foundations for your journey. Then you can be confident... and as speedy as you need to be."

"My clients in the banking sector are realizing that there is time," says Owen, "And they're also realizing that the threat of digital up-starts might actually be an opportunity. I mean, we're talking to clients about partnering with new banks... or even acquiring them. That's a strategic play. By working with ISG, we give them the time and breathing space to think more deeply and broadly."

⁵ Soren Kierkegaard – A Kierkegaard Reader. eds Roger Poole & Henrik Stangerup (1989)

“The trick is to see through the hoopla, all the hype and create that roadmap and base it on your business needs. So, you need good information,” says Lois. “That’s dynamic pragmatism.”

John sums up: “We don’t only pitch ISG as the pragmatic choice. We try to be more excited than that. But we do pitch ISG as the knowledgeable, experienced and objective partner enterprises need in the digital age. Those are the adjectives I always associate with us. That’s because we help clients select the right partners. We have been doing so for a very long time. We know old style outsourcing and we’ve mastered new style digital sourcing.

“We have a huge amount of experience in what has gone very well and not so well. We have developed a huge amount of learning in the kind of attributes that have contributed to success. Some of those things are quite small, what I call the blocking and tackling, and the skills and personal attributes of the people involved. But we’re also good at the business processes that create a sound ecosystem of relationships which are necessary to make an enterprise operating model successful. Simply put, you don’t have to figure it all out on your own.”

So, ‘pragmatic optimism’ in a time of digital euphoria means:

- Take a step back, be realistic
- Understand where you are and where you want to be
- Realize that you’re not there yet and you need to transform your organization
- Create a structure to get the right information
- Balance in-house knowledge with external wisdom and expertise
- Industrialize digital by creating standardized repeatable processes that work every time
- Achieve a broad perspective to create a sound roadmap
- Be optimistic not euphoric

At ISG our role is to partner you as you address the issues and changes you need to make. We bring our experience and expertise to the table, and help you cut through the exuberance, irrational or otherwise.

We work with you to energize your organization and focus on the issues that matter to your business and your people. We’re honest, down-to-earth, and speak plainly. When all around you are being irrationally exuberant, we help you tread carefully, but swiftly. We help you go forward, with confidence.



You don't have to figure it all out on your own

ISG can help you go digital
at the right pace.

Why not talk to ISG and see how we can help.

If you would like to discuss the issues raised in this ISG Focus Paper then give us a call on **+44 (0)1737 371523**, or send an email to **denise.colgan@isg-one.com**, and we'll set up a meeting.

Our next ISG Focus Paper will examine the subject of Robotic Process Automation. Email **denise.colgan@isg-one.com** to register for your copy now.