ISSUE 129

BOARD PERSPECTIVES: Risk Oversight

IS YOUR BOARD DIGITALLY SAVVY?

As global markets continue to address the COVID-19 pandemic, practical digital know-how is becoming more than a desirable attribute that directors aspire to embrace. A compelling study asserts that companies could be falling behind if they lack a digitally savvy board.

Boards and business leaders are well aware of the digital revolution taking place across the globe and how digital leaders were able to navigate the choppy COVID-19 seas much more effectively than their less resilient peers. But what's being done to advance their organizations' digital capabilities? Specifically, does the board possess the digital savviness needed to support the CEO's efforts to continuously improve the company's business model, customer experience, decision-making processes, and operational efficiency and effectiveness?

Key Considerations

A study indicates there is a financial performance payback from a digitally savvy board. The research defined "digitally savvy" as "an understanding, developed through experience and education, of the impact that emerging technologies will have on businesses' success over the next decade." It analyzed the boards of U.S.-listed companies and determined that organizations with boards that have at least three digitally savvy members outperform other enterprises in their respective industry. These companies reported 17% higher profit margins, 38% higher revenue growth, 34% higher return on assets and 34% higher market capitalization.[1]

Based on machine analysis of the various boards' digital capabilities, the research analyzed data from surveys, interviews, company communications and the bios of 40,000 directors, extracting keywords indicating the ability to think and act

[1] "Without a Digitally Savvy Board, Your Company Is Falling Behind," by Peter Weill and Stephanie Woerner, The Hill, March 20, 2019: https://thehill.com/opinion/finance/434788-without-a-digitally-savvy-board-your-company-is-falling-behind.

digitally. According to the research, digitally savvy directors possess the following attributes:[2]

- Firsthand knowledge of how technologies will impact the way companies can thrive in the next 10 years.
- An enterprise-level comprehension of innovative technologies, such as artificial intelligence, big data, the Internet of Things, scalable digital platforms and digital processes that enable new business models, improve customer experiences and drive operational efficiencies.
- An understanding of when to undertake new digital initiatives and the early indicators of when those initiatives are either struggling or succeeding.
- The instinctive ability to integrate digital thinking into the early stages of the strategy-setting process.

The researchers found that every industry studied had digitally savvy boards, though the concentration of these boards was higher in some industries compared to others. For example, the top three industries with digitally savvy boards were information (57%), professional services (39%) and manufacturing (29%). The bottom three were mining, transportation and construction (less than 10% each). Interestingly, across all industries, only 24% of companies with over $1 billion in revenues had digitally savvy boards.[3]

The takeaway: To be successful in the digital age, companies need leadership from their boards to help them advance their digital maturity and support their CEOs in thinking and acting digitally. Digital savviness is about much more than leadership; it is also about ensuring that the business has a relevant vision and that necessary changes are being implemented as the company pushes that vision forward.

So, the question arises: How does a board gain that next-generation knowledge? Here are some suggestions:

Three may be the magic number. There was little difference in financial performance between companies with one or two digitally adept directors. However, companies with three or more such directors saw statistically meaningful improvements in performance. Accordingly, boards should look at the extent to which digital savviness is present in their oversight processes. When screening new director candidates, consideration should be given to the pool of seasoned executives who have served in senior roles in fast-paced industries where business models change rapidly. Such executives might include those with both a digital and an operational background who helped their companies innovate and/or undertake a major change initiative or who served in roles requiring strong technology acumen (such as chief information officer or chief technology officer, both hereinafter referenced as the CIO).

Merge institutional knowledge and digital perspectives. Directors who grew up in the analog age experiencing business downturns and developing a deep understanding of cultural and operational aspects of the business offer valuable institutional knowledge going forward. To remain relevant, they can elevate their digital savviness through engaging external experts as advisers, participating in self-directed digital training, and visiting "born digital" companies or companies that have consummated significant transformation activities. Combined, these directors and directors who are technologically savvy can pool their expertise and experience to understand how digital trends and disruption can affect the organization's business model, value proposition and industry, and advise executive management as they transform the company.

[2] "Why a Digitally-Savvy Board Will Increase Your Revenue," by Alison DeNisco Rayome, TechRepublic, May 30, 2019: www.techrepublic.com/article/why-a-digitally-savvy-board-will-increase-your-revenue/.

[3] "It Pays to Have a Digitally Savvy Board," by Peter Weill, Thomas Apel, Stephanie L. Woerner and Jennifer S. Banner, *MIT Sloan Management Review*, March 12, 2019: https://sloanreview.mit.edu/article/it-pays-to-have-a-digitally-savvy-board/.

Technology is a strategic driver rather than a strategic enabler. The study noted through interviews with directors that boards lacking digital savviness are likely to start with the question, "What is our strategy?" Then they ask, "What resources, including technology, do we need to execute that strategy?" But boards possessing that quality focus strategically on enhancing the customer experience, improving operations and securing the company's positioning within the value chain. For example, they might inquire about how to use technology to improve customer satisfaction and operations. They might encourage a test-and-learn approach to strategy to conduct experiments and scale successes. And they are more apt to ask the tough questions about what is really happening in the company and industry. In effect, they think differently — in approaching strategy, allocating board agenda time, organizing director education and viewing the role of technology in the business.[4]

Resist falling back on the CIO. If the board does not have the financial means to either add a board seat or attract top talent, it can consider hiring advisers with the requisite depth of experience. If the focus is on individuals with strong technical acumen, some boards might be tempted to leverage the CIO currently functioning within the company. We do not recommend that approach. Effective board oversight needs an independent view. Even solid CIOs need to be challenged on occasion, and boards must be capable of assessing the CIO's capabilities and performance in light of changing markets.

CEOs must be digitally capable, too. Digitally capable boards seek CEOs with a compelling vision on how the company can use technology to sustain competitiveness in the digital economy during the years ahead. The board needs confidence that the CEO can think and act digitally in managing the business, leverage evolving markets, and build digital ecosystems centered around teams with the requisite knowledge of digital business concepts and the ability to scale digital platforms that can facilitate rapid growth. With the right CEO and team in place, the board's role then is to support the CEO in setting strategy, monitoring strategic execution, aligning corporate culture and managing risk.

It's all about disruptive innovation. Understanding whether the company desires to be a digital leader or an agile digital follower — or something in between — is important, as it provides context for the board's oversight of the company's innovation strategy and culture and encourages open discussion around direction and progress. The digitally savvy board insists on appropriate innovation-specific metrics that tell the full story. Directors can help to do so by asking management, for example: How is the innovation and growth strategy performing relative to competitors and the targeted return on investment? Is management getting feedback on the customer experience? How effective is the company's innovation culture and capabilities in empowering and rewarding employees to test new ideas and take appropriate risks to make those ideas a reality?

No company is immune to digital disruption. That is why boards should appraise their digital savviness with regard to supporting the CEO in a rapidly changing digital economy, particularly as companies emerge from the COVID-19 lockdown. Gaps noted should be addressed sooner than later, so that the board is positioned to ask the right questions as the CEO assesses the broader capabilities of the business, identifies changes that need to happen and monitors whether those changes are taking place.

[4] "Without a Digitally Savvy Board, Your Company Is Falling Behind," by Peter Weill and Stephanie Woerner.

Questions for Boards

Following are some suggested questions that boards of directors may consider, based on the risks inherent in the entity's operations:

- Have we assessed our board's practical digital knowledge and ability to advise management on digital strategy? If there are gaps, is there a plan in place to close them soon? Do we have enough digitally savvy individuals serving on the board? If not, should we plan to onboard more to better recognize digital opportunities, to know when to experiment and when to partner, and to identify warning signs of trouble?
- Do we have an eye on the technological trends affecting the opportunities and risks expected to disrupt our industry in the foreseeable future? Wherever we are on the digital maturity continuum (e.g., skeptic, beginner, follower, advanced or leader), are we capable of advising and encouraging management to think and act digitally in advancing the company's digital maturity consistent with the company's strategy?
- Is the organization's culture enabling it to advance its digital capability, or is it a barrier to advancement? As a board, would we know the difference?

How Protiviti Can Help

Protiviti has worked with 60% of Fortune 1000, 35% of Fortune Global 500 and smaller companies, such as fast-growing pre- and post-IPO organizations. We have a proven track record of bringing innovative solutions to help companies solve some of their most difficult business problems. Our digitalization offerings focus on:

- **Customer engagement —** Exploring new ways to build strong relationships with customers.
- **Digitizing products and services —** Launching new, enhanced products and exploring new business models.
- **Better informed decisions —** Enhancing information available to enable timely and effective data-driven decision-making and improve digital propositions.
- **Operational performance —** Creatively using technology to improve processes and underlying performance.

Our online, proprietary digital assessment tool (https://landing.protiviti.com/digital) is designed to help companies identify issues that may undermine their digital strategy, focus on the decisions they need to address to advance their digital maturity and measure their progress over time.

Protiviti partners with the National Association of Corporate Directors (NACD) to publish articles of interest to boardroom executives related to effective or emerging practices on the many aspects of risk oversight. As of January 2013, NACD has been publishing online contributed articles from Protiviti, with the content featured on https://blog.nacdonline.org/authors/42/. Twice per year, the six most recent issues of *Board Perspectives: Risk Oversight* are consolidated into a printed booklet that is co-branded with NACD. Protiviti also posts these articles at protiviti.com.