It Pays to Have a Digitally Savvy Board

Having board members with experience in digital business is the new financial performance differentiator.
Boards of directors have many issues competing for their attention, but being digitally conversant in an era of digital transformation is quickly rising to the top of the list. Nearly all companies are looking for ways that technology can be used to improve their business models, customer experience, operational efficiency, and more — and boards must help them move forward at a sufficient pace, advocating for change by supporting and sometimes nudging their CEOs. Those that do are likely to see better financial results than those that don’t.

That’s what we discovered when we did a machine learning analysis of the digital know-how of all the boards of U.S.-listed businesses. (See “About the Research,” p. 43.) Our research shows that companies whose boards of directors have digital savvy outperform companies whose boards lack it. We define digital savvy as an understanding, developed through experience and education, of the impact that emerging technologies will have on businesses’ success over the next decade. We measured it by analyzing data from surveys, interviews, company communications, and the bios of 40,000 directors,

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**BY PETER WEILL, THOMAS APEL, STEPHANIE L. WOERNER, AND JENNIFER S. BANNER**

LEADING DIGITAL CHANGE: GOVERNANCE
extracting key words that signal exposure to digital ways of thinking and working.

Our discoveries are striking: We found that among companies with over $1 billion in revenues, 24% had digitally savvy boards, and those businesses significantly outperformed others on key metrics — such as revenue growth, return on assets, and market cap growth.

Doing business in the digital era entails risks ranging from cybersecurity breaches and privacy issues to business model disruptions and missed competitive opportunities. When a board lacks digital savvy, it can’t get a handle on important elements of strategy and oversight and thus can’t play its critical role of helping guide the company to a successful future. But companies can fix that by understanding what characteristics to look for in existing and new board members, managing board agendas differently, and cultivating new learning opportunities.

What Makes a Board Digitally Savvy

Our research suggests that three factors make a board digitally savvy: the backgrounds of individual members, the number of members with deep digital experience, and the way the board interacts with management on the strategic role of technology.

Individuals’ backgrounds matter. On a digitally savvy board, members have an enterprise-level understanding of current technology such as digital platforms, AI, big data, and mobile and digital processes that enable new business models, an improved customer experience, and more efficient operations. Being a digitally savvy director is often a consequence of one of two activities: time spent, either as a board member or a senior executive, in a high-clock-speed industry where business models change quickly, such as software or telecom, or having an executive role with a strong technology component, such as CIO, CTO, COO, chief data officer, or, more recently, chief marketing officer. Given their perspective, such board members have a sense of when to commit, when to experiment, and when to partner. They can also spot early indicators of both successes and challenges for new initiatives operating at enterprise scale.

It takes three to tango. We tested whether the number of digitally savvy directors would affect a company’s financial performance and found that it takes three members to have a statistically significant impact.1 We saw little difference in financial performance between companies with one or two digitally savvy directors and those with none. But companies with three or more digitally savvy directors had 17% higher profit margins than those with two or fewer, 38% higher revenue growth, 34% higher return on assets, and 34% higher market cap growth. Beyond three digitally savvy directors, the incremental differences in performance were small. As one director commented, “A single tech-savvy director in the boardroom risks feeling lonely and misunderstood. To effect change at the board level, there must be a critical mass of directors who truly understand.”

The effects of three digitally savvy board members were consistent across industries, although the percentage of such boards varied by industry. (See “Some Industries Are Savvier Than Others,” p. 45.) While on average, 57% of company boards in the information industries were digitally savvy, only 24% of company boards in retail, and less than 10% in transportation, construction, and mining, had this understanding.

It’s important to ask hard questions about technology and strategy. Several directors we spoke with observed that non-savvy companies and their boards tend to think about strategy quite traditionally, first asking, “What’s our strategy?” and then, “How do we marshal our resources, including technology, to achieve it?” Managers in these companies often turn
to technology when they’re ready to implement, not when they’re still setting direction. In contrast, digitally savvy companies and their boards ask themselves early on, “How can we use technology to delight customers and be more efficient?” Management takes a test-and-learn approach to strategic planning, experimenting to see what works and then scaling the successes. Digitally savvy boards will ask tough questions like, “Rather than speculate, how can we quickly test whether customers really like this new offer, learn, and adjust?” or “When we launch this new offer, how do we track usage and bottom-line impact?” By asking such questions and then engaging with executives, boards can help their companies learn what makes them great so that those traits or features — their “crown jewels” — can be digitized through internal innovation, external partnering, or both. Companies that make the most of their crown jewels in this way include Amazon (matching customer needs with providers), Schneider Electric (providing real-time energy management services), and BBVA (matching banking services like risk assessment to customer goals).

In other words, rather than focusing on the basics of the technology itself, digitally sophisticated board members use their insight about trends and transformation to help managers explore the bigger picture the business is facing competitively. As one of the directors we interviewed put it: “Digitally savvy directors change the risk conversation from evaluating the project risk of particular initiatives to the business model risk of not doing something new.”

For these reasons, digitally savvy boards can keep management honest. For example, one or two Netflix board members attend key monthly and quarterly management meetings as observers to become better informed and share insights with fellow directors afterward. “Management can lose their sense of accountability to a board on these matters,” a director at another company told us. “They think they can put anything up to the board and the board will say, ‘Oh, yes, OK.’ Digitally savvy boards push back and ask hard questions. One of the most important and hardest things for a board is to have a real line of sight into what’s going on in the company. It sounds so obvious, but it’s not easy.”

Building Your Own Savvy Board

When we identified key word indicators of digital savviness, we found that those directors had one distinctive indicator such as virtual reality or chief information officer, or multiple less-distinctive indicators such as technology companies, diversified technology, and skills and technology. Words such as software, digital media, chief technology officer, e-commerce, cloud, AI, and data were common signals that directors had the right background to assist in their companies’ digital transformation. (See “How Digitally Savvy Directors Are Described,” p. 44.)

Once organizations know what indicators to look for, how can they make their boards more digitally savvy? By strategically adding new members, altering board agendas, and encouraging educational opportunities for current members.

Add new directors. For most boards, having three digitally savvy directors would mean adding at least one new board member. Several directors told us that they are seeing first-time public company board members, often much younger than the average board member, invited to join because of their digital experience.

Based on our analysis of key words and our work with boards, we found there are several places
to search for digitally savvy directors. Directors or former senior executives of companies that operate in industries where technology changes the product offerings every two or three years are typically digitally savvy. So, too, are directors or former executives of companies that have developed platform-based businesses.

Alter the board agenda. Along with adding new members, boards can increase the digital savviness of the existing team. Many boards have tech committees or similar groups steering them on digital issues, and often those committees engage nondirectors and external experts as advisers (several banks we spoke with have done this). Such committees can offset gaps in knowledge, which is a good place to start. But within a few years, the whole board must get up to speed on digital issues.

The most effective approach we observed was visiting other organizations to learn from their experiences — one director described this as “digital tourism.” This took the form of confidential, in-person discussions with leaders of born-digital companies such as Amazon, Tencent, Google, and LinkedIn. Directors who made these trips often commented on how the born-digital companies behaved differently — in particular, how they used evidence-based decision-making, reused digital platforms, applied test-and-learn techniques rather than big bang implementations, and got everybody involved in innovation.

Visits to noncompeting companies that have made significant progress in digital transformation in similar industries were also valuable. Downtime during these meetings was especially useful: One director said that important conversations between directors occurred during meals, debriefings, and travel. It was at those times that the visitors had an opportunity to really debate the issues privately and honestly (and off the record), comparing what they’d seen with what happens in their companies. As one director summed up the value of these conversations, “If you don’t step outside and see what ‘better’ can look like, you can actually think you’re doing pretty well.”

Several directors also mentioned annual, or more frequent, strategy retreats as critical for improving the board’s digital savviness. Having a significant amount of dedicated time — often one or two uninterrupted days — to focus on digital issues is crucial.

Boards can learn a lot by visiting born-digital companies. As one director pointed out, “If you don’t step outside and see what ‘better’ can look like, you can actually think you’re doing pretty well.”
threats and opportunities is a starting point. Other retreat activities can include engaging with provocative external speakers, debating presentations from company executives on their views of the future, and doing hands-on exercises like case studies of learning opportunities (formally known as “failures”). These meetings are most effective when all the directors and executive managers are present and when they include small-group exercises or discussions with clear direction on what will become of the insights after the retreat is over.

Encourage self-directed learning. Of course, there is no substitute for curious and committed directors who understand the areas where they need to develop. Some board members told us they invested in becoming digitally savvy when they didn’t have previous digital experience, taking online and in-person courses, reading research reports and case studies, attending technology conferences, and finding reverse mentors — “digital-native” colleagues — to learn from. Others volunteered for roles where they’d learn on the job: As one director reflected, “When the opportunity came up to join either the IT committee or the remuneration committee, I jumped at the IT committee.”

To be clear, we’re not advocating that boards set digital strategy — that’s the role of management. Instead, boards must encourage, push for change and progress, see the big picture, review, and question. Just about every company today is grappling with digital transformation in some way. Although there is no proven playbook yet, the active involvement of a savvy board can give companies a performance edge over competitors that are facing similar challenges.

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### SOME INDUSTRIES ARE SAVVIER THAN OTHERS

The percentage of digitally savvy boards varies widely across sectors.

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<th>Industry</th>
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<tr>
<td>INFORMATION</td>
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Source: MIT CISR analysis of 1,233 publicly traded companies with revenues over $1 billion

### REFERENCES

1. Several female directors commented that three was also a magic number when it came to reaping benefits of gender diversity on boards. This perspective is highlighted in the research of V.W. Kramer, A.M. Konrad, and S. Erkut, “Critical Mass on Corporate Boards: Why Three or More Women Enhance Governance” (Wellesley, Massachusetts: Wellesley Centers for Women, 2006).
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