HOW Strategic Performance Management IS HELPING COMPANIES CREATE Business Value

THE ENTIRE ORGANIZATION MUST BE ALIGNED BEHIND THE GOAL OF TURNING THE STRATEGIC PLAN INTO EFFECTIVE ACTION.

BY OMAR AGUILAR

At most companies the business strategy is no sooner developed than it begins to lose steam. There's no mechanism to cascade and instill the strategy down through the organization and to ensure that it is actually implemented. This leaves divisions, business units, departments, and individuals to set their own priorities as best they can, whether or not these priorities are in alignment with overall strategic objectives.

To maximize their resources, managers need to know the game plan and their role in it. They also need frequent and accurate feedback telling them how they are doing, where they are falling short, and what they need to do to get back on track. Performance management is supposed to address these challenges, but in most companies it is pursuing its own goals—assessing performance in isolation without asking if that performance is actually helping the company achieve its strategies.

Six Obstacles to Good Planning

When asked what factors are causing their planning process to lack validity, CFOs cited these top six culprits:

Listed by percentage of CFOs citing that factor as a cause; multiple answers permitted.

Lack of a well-defined strategy	57%
Lack of a link between strategy and operational plan	53%
Lack of individual accountability for results	45%
Lack of meaningful performance measures	34%
Lack of pay for performance	21%
Lack of appropriate data	21%

Source: The Conference Board

To achieve the results promised by their business strategy, a number of business leaders are demanding that performance management bring the entire company into alignment behind that strategy. More important, they are defining a way to institutionalize business value creation. There are five critical dimensions of performance management that together can help companies maximize value.

1. Strategic Planning: Create a strategic business plan that can be cascaded down through the organization.

2. Performance Measurement: Establish key measures that tell management whether the objectives of the plan are being realized and, if not, where and by what degree they are falling short.

3. Integrated Business Planning: Design and integrate processes—operational planning, budgeting, and forecasting—that create value and align efforts rather than simply police and keep score.

4. Management Reporting: Provide concise, timely information that helps management see what needs to be done and how to do it.

5. Organizational Culture and Reward Systems: Create a culture that energizes employees and inspires them to work together to achieve the company's strategic goals.

The final and most important element isn't to plan, budget, forecast, report, or reward, but to act—to manufacture products, perform services, or serve customers; to create income; and to earn profits. All other functions and processes should exist to ensure that employees are carrying out the right activities and have the resources they need to succeed.

STRATEGIC PLANNING

In many companies the strategic plan is more of a mission statement than a road map. The real planning, as often as not, is driven by the budget process, which determines where resources will be allocated. Those allocations, in turn, shape the operational plan. The final operational plan often reflects how well executives compete for budget rather than what senior management actually hopes to accomplish.

To change this ineffective planning process, senior management must lead the change process and demand that the operational plans and budgets fully support the implementation of the strategic plan. In short, management must establish clear strategic goals that can be translated into specific actions.

Companies pursuing a workable strategic plan usually assign small teams of top executives to set their goals using a rigorous planning process. Typically these teams start with a thorough analysis of their industry, markets, customers, products and services, competitors, and internal strengths and weaknesses. Most use a top-down process, but some combine this with a bottom-up approach that enables middle management to bring their local knowledge into the process. Such a flexible approach helps build middle-manager ownership and motivation.

Once the planning team has developed actionable goals, they "cascade" these goals down through the company. At each level, the planning team works with operational management to determine specific actions and priorities. By bringing operational management into the planning process, the company's leadership gains buy-in and ensures that staff at all levels knows what must be done. Operational management gains a clear understanding of what success looks like and how it will be measured. Ultimately, everyone knows his or her goals and is accountable for achieving them.

To create a clear link between employee activities and the goals of the organization, Georgia-Pacific restructured its personnel management process and tied it much more closely to the strategic planning process. Now the company's strategic planning process generates goals and measures that are set in January and are cascaded to all levels of the organization. Performance management then links these corporate goals to individual performance targets, establishing a clear link between corporate objectives and daily employee activities.

PERFORMANCE MEASUREMENT

To effectively implement the strategic plan, management must know if the plan's goals are being achieved on time and with the allocated resources. Getting the right answers means having the right performance measurement framework. You can't begin to manage performance until you can accurately measure it.

At most companies, the problem isn't a lack of measures—most have too many—but a lack of *focused* *and effective measures*. The challenges in selecting the right measures include choosing the right leading and lagging indicators, benchmarking against competitors, balancing financial and nonfinancial measures, and using an appropriate number of measures.

Performance measures at best-practice companies tend to be few and focused and have clearly defined targets. Best-practice companies typically use eight to 12 measures companywide.

Many companies focus almost entirely on financial measures, but that approach results in a one-dimensional view of performance. To gain a more complete picture, best-practice companies use a variety of measures, including people measures (*How do we motivate and retain people?*), customer measures (*How do we build customer satisfaction and loyalty?*), and operations measures (*In which processes must we excel?*).

Once appropriate measures are in place, managers can receive the specific information they need in electronic form in a concise format. If they want more information about a particular measure, they can simply drill down for greater detail. Agreed-upon measures help managers take actions that are directly related to achieving the company's strategies. Such measures also show senior management where the best results are coming from so that success can be recognized and rewarded.

Are Rolling Forecasts a Panacea?

MYTH OR REALITY?

- Fewer than 20% of multinationals use them in some form
- Although about 65% of CFOs view rolling forecasts as very valuable, less than 15% use them extensively
- Of companies using rolling forecasts, five- or six-quarter forecasts are more prevalent than four-quarter ones

WHAT'S NEEDED TO MAKE IT WORK?

- A focus on fewer data elements and less information
- Cascading of firm top-down targets
- Effective and timely management reporting—typically, technology enabled
- Philosophical change on how to manage, view, and compensate performance

IS IT RIGHT FOR YOUR COMPANY?

- Unless planning, budgeting, and forecasting are already integrated, rolling forecasts may be more difficult to implement than a traditional process
- If a culture demands more information and is slow to react, rolling forecasts may not work
- A company faced with a highly dynamic external environment may be well suited for rolling forecasts

Source: Gunn Partners

INTEGRATED BUSINESS PLANNING

Integrated business planning comprises three elements: operational planning, budgeting, and forecasting.

Operational planning takes the company's strategies and translates them into specific tactical steps, or actions, starting with broad, general actions and then breaking them down into increasingly specific ones. Much of this happens as the strategic and operational plans are cascaded down through the organization. By bringing all levels of management into the operational planning process and giving individuals a chance to help shape the plan, the company wins management alignment and buy-in. Having bought into the plan, individual managers become accountable for achieving its goals. They are also energized by the realization that their compensation and other rewards will be governed by their success at achieving their goals.

At many companies, budgeting drives operational planning when the process should actually operate in reverse. When companies try to use the budget process to drive and control operations, budgeting typically becomes enormously time-consuming, with managers competing for the largest allocations irrespective of actual need. In best-practice companies, budgeting is a relatively simple process that translates operational goals into the resources needed to accomplish them.

The focus of integrated business planning at Texas Instruments is on improving the bottom line while minimizing iterations and processing time. The result is a deeper understanding of key mileposts that show where each business is headed and what it needs to get there. Detail is reduced; overall strategy is encouraged. The first year of this long-range planning provides a baseline for the annual budgeting process. Budget iterations are minimized because the operating units are encouraged to get "smarter" during the budget process.

Similarly, Hewlett-Packard emphasizes analysis and strategic reviews rather than "numbers" while at the same time focusing on process excellence. Although Hewlett-Packard uses performance-based compensation and a modified Economic Value Added (EVA) model, the success of its planning and budgeting rests largely on the excellence of its processes. Strategic guidelines drive

Best Practices of the Building Blocks of an Integrated Business Planning Process

PLANNING → BUDGETING → FORECASTING → REPORTING

PLANNING
- Focused on analysis
- External focus
- Small teams making decisions
- Top-down
- Results clearly communicated
- Results in balanced scorecard

BUDGETING
- Plans and budgets linked
- One- to two-month cycle time
- Firm financial targets
- Reduce detail (fewer than 100 lines)
- Reduce iterations (no more than two)
- Simplify and reduce allocations

FORECASTING
- Use of ranges to account for input accuracy
- Linked to operational plans to close performance gaps
- Use of quantitative and qualitative methodologies
- Process in place to track accuracy

REPORTING
- Timely
- Integrated
- Accurate and relevant
- Qualitative and quantitative
- Focused
- Drill-down capability

strategic plans that, in turn, drive annual plans with periodic annual updates. Moreover, the company continuously strives to improve planning effectiveness by focusing on cycle time, relevance, systems and technology, predictive accuracy, process accountability, and linkage to product cycle life.

FORECASTING ACCURATELY

Poor planning and budgeting make it almost impossible for companies to accurately forecast their quarterly earnings. Industry analysts would have you think that investors should applaud positive earnings surprises and deplore negative ones. Yet all earnings surprises, positive or negative, are signs that a company's planning and budgeting processes are malfunctioning. Of course, there are times when a company's earnings are pushed up or down by unanticipated economic events, but those should be the exceptions.

The real goals of forecasting are to predict revenues and expenses over a period of time, update plans, and provide management with a vision of the future. So, accuracy is crucial. A company whose earnings are on target quarter after quarter may not be as exciting as one whose earnings yo-yo, but common sense tells us that companies that can forecast their earnings accurately are likely very well managed. Such companies typically keep a close watch on their forecasts; if results start to deviate beyond a specified threshold, they take prompt action.

MANAGEMENT REPORTING

In many companies, managers are inundated with voluminous reports that fail to give them the precise information they need to assess what's happening and take appropriate action. In addition, it's almost impossible for management to reward good performance if it can't "see" where that performance is coming from.

To create an effective management reporting system, a company must first establish its strategic and operational goals, measures, targets, budgets, and forecasts. Once these are in place, it can accurately determine what information must be reported, in what detail, and how often.

Because managers at different levels require different information, the company must ensure that managers get the specific information they need to guide them in planning actions, with top management getting primarily strategic reports and operational management getting tactical data. In short, good management reports are concise and provide information that can be acted upon. They are also consistent throughout the company in the sense that they offer one version of the truth.

At NationsBank, now integrated with Bank of America, performance measures and reporting requirements were defined first; then the appropriate recipients for different levels and types of information were determined. Now the performance measurement process gathers relevant information from throughout the organization and transmits it electronically to managers in concise reports, typically two or three pages. For more detail about a particular measure, managers can drill down by double-clicking on that measure's line in the electronic report. As a result, managers at every level can readily see if targeted objectives are being met, can tell where the best performance is coming from, and reward those responsible.

In best-practice companies, technology plays a major role in management reporting by integrating the reporting process into other systems so that managers can access useful information online and then drill down for additional details. For example, at Knight Ridder the reporting system also enables senior management to ask what-if questions and investigate alternative scenarios.

ORGANIZATIONAL CULTURE AND REWARD SYSTEMS

In most companies, the energy level is high at the top and fades as it moves down through the organization. One of the goals of performance management is to energize employees, first by making performance more visible and then by recognizing and rewarding good performance.

Design of an effective reward system parallels the integrated planning cycle. General reward objectives are identified—during the creation of performance measures—and performance is rewarded during results reporting and assessment. Implementing a new reward system, especially one that alters the performance culture, usually takes several review cycles to have its full impact on individual behavior. In most companies this means that the entire journey may take several years.

With their superior planning, measuring, and forecasting, best-practice companies can readily identify the divisions, units, departments, and individuals that are getting the best results and reward them accordingly. In such companies, individuals know their goals and priorities. They are empowered to achieve these goals and are held accountable for the results.

Three years ago, Georgia-Pacific recognized that its processes for reviewing and managing performance were cumbersome and, more important, did not always provide a clear link between employee activities and the goals of the organization. To restructure its performance management systems, the company designed a database, accessible to salaried management online and in real time, that defines a standard competency set applicable to all employees. The Georgia-Pacific strategic planning process generates company goals and measures that are set in January and then cascaded to all levels of the organization. The new performance management process then links these organizational objectives to individual performance targets, establishing a clear link between objectives and daily employee activities.

IBM, with some 300,000 employees worldwide, uses its Personal Business Commitment (PBC) performance management system to clearly link employee activities to corporate objectives. The idea is to first gain alignment throughout the organization and then to align the company's objectives with the activities of individual employees. By providing access to a competency database that reflects and then ties compensation targets to performance, PBC helps the organization understand each individual's unique contribution to achieving the corporate objectives and reward employees accordingly. Managers can clearly see what is expected of their staff, how to measure those activities, and how to tie them to the company's objectives. This kind of empowerment and accountability motivates people not just to do their best but also to focus their energies on doing what is best for the company.

TAKING ACTION

The final step in developing an integrated performance management plan—taking action—sounds like an anticlimax, but it isn't. It is the organization's ultimate goal, and all of the organization's other functions and processes exist to ensure that employees are performing the right activities and have the necessary resources. These activities—manufacturing products, performing services, serving customers—are the core of the company. They are why it exists.

A key purpose of performance management is to align the entire organization behind the goal of turning the strategic plan into effective action. Most companies have processes in place for planning, budgeting, and other critical management activities, but all too often these processes are not linked together or integrated throughout the organization. To a great extent, developing more effective performance management means identifying the disconnects and then creating linkages to bring the processes—and the organization—together.

Throughout this change process, it is critical that senior management lead the effort and make it clear that the changes will be implemented and that obstacles to change will be removed. It is also critical that management communicate its determination down through the entire organization. Communications should serve to inform employees, to involve them in the process, and ultimately to empower them to implement change—and to keep implementing change on an ongoing basis. ■

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Author's note: Corporate experiences cited in this article are derived from *Gunn Partners Performance Management Process Forums* and *Gunn Partners Best Practice Forums.*