Best Practices *Bob Gunn, Editor*

Measuring Up...Consistently

AS WARREN BUFFETT FAMOUSLY SAID, THERE is no more powerful force in nature than the power of compounding returns. For example, a 10% return on a $10,000 investment for 10 years will create nearly $26,000 in value. Increasing the return to just 12% raises the value by more than $5,000! Similarly, small performance differences by employees will multiply over time to yield spectacularly different outcomes.

But how can managers predict which small points will provide big leverage? In other words, how do we know where to focus?

Consider the experience of the executive vice president of HR for one of the mega-retailers (more than 900 stores). He was sitting in a leadership team meeting when the CEO smacked the table and exclaimed, "I just don't get why we have a handful of stores that consistently outperform the others! What are they doing? Frustrates the hell out of me—if we could only bottle the magic we would be well on our way to beating our 5% margin goal!"

Good question!

No doubt, the truism "fortune favors the prepared mind" speaks accurately. But as the CEO of this retailer understood, luck is not a reliable partner—at least not something to be counted on long term. Sustained results are possible only when the collective energy of people is flowing, working toward an inspiring goal. That's the "magic in the bottle."

ILLUSTRATION: ARTDISC ILLUSTRATION INC.

Taking seriously the CEO's challenge to find the link to store performance, the EVP created an elegant framework for assessing performance. He started with a simple but easily taken for granted premise: Customers were more likely to continue to shop where they had a good experience. Then he gathered data that allowed him to correlate store profitability with *customer satisfaction*. His results proved that every five points of measured customer satisfaction resulted in a 1% increase in store profitability.

But he didn't stop there. He asked, "What factors caused high customer satisfaction?" Not surprisingly, the data showed a correlation with high levels of *employee* satisfaction. Again, proving the obvious, but the research had a big impact on the leaders of this American institution—as it proved what they had long suspected.

"What factors resulted in high employee satisfaction?" was the next question to be researched. The correlation was with *store manager effectiveness*.

Finally! The EVP had an answer that hung together. He expressed it in this formula: Profits = customer satisfaction × employee satisfaction × leader effectiveness.

Leader effectiveness was determined by 12 simple questions:

- Does your manager ask your opinion on how a task should be accomplished?
- Does your manager treat the employees with respect?
- Do you enjoy your work?
- Does your manager help you when you need it? Does your manager understand your job?
- Are issues/problems dealt with promptly and fairly?
- Does your manager say what he/she means and do what he/she says?
- Can you have a conversation with your boss that will be kept confidential?
- Does your manager enjoy his/her job?
- Does your manager resolve conflicts well?
- Do you feel part of the manager's team?
- Do you believe your manager has your best interests at heart?

Nothing complicated, just the basic questions about behaviors that good store managers exhibit—as defined by the employees. But notice that they point to respect—acknowledgement of the fundamental precept that each of us is doing the best we can, based on our current thinking.

The CEO and his team spent the next three years focusing actions on this information, and the company's performance steadily improved. Return on sales increased from 2.1% to 5.8%, and the stock price improved by nearly 100%.

Measuring the power of focus

Focus became the crux of measurement by a mega bank in the U.S. One of its key management processes is based on the Hoshin planning system—a methodology used by such Japanese companies as Toyota as part of ongoing quality efforts. First, the CEO articulates his top goals and describes the broad actions to achieve them. Then each business unit and functional manager uses the framework to nest her own objectives and actions so that the link between the focus of every department and that of the company is crystal clear. Goals, objectives, and actions cascade right from the top.

Adding teeth to the process, each action has a metric—sometimes quantitative, other times qualitative—so progress can be tracked. Quarterly, managers take the Hoshin framework and describe the actions taken and progress made for each principal objective. They describe their own initiatives and deeds during the period, categorizing them into four buckets—essential, beneficial, neutral, or negligible. Once each manager has produced a draft based on his own perceptions, he shares this with his staff. Some people feel more comfortable doing this in a face-to-face setting; others ask for feedback in an e-mail; still others facilitate communication with greater anonymity.

Table 1: Tracking a Manager's Effectiveness

Actions	Adjustments
ESSENTIAL	
Coached sales teams in 65% of the opportunities won	Account managers should become accountable for coaching sales teams, not just me
BENEFICIAL	
Worked with account managers to proactively think through risk mitigation tactics and opportunity action plans	Account managers need to learn from each other by working risks and opportunities together, not solo
NECESSARY	
Asked account managers to develop incentive scenarios based on revenue recognition policies	Need to develop revenue recognition scenarios with sales staffs and explore implications
NEGLIGIBLE	
Required sales teams to develop target account lists	Seems like we do this a couple of times a year and never use the results—process should be left to discretion of account managers

Whatever procedure is used, the managers usually end up with something similar to Table 1. It clearly depicts the manager's effectiveness based on her actions during the quarter, and it expresses the adjustments she can make that may have a positive result in the next period.

As seems obvious from reading the results from the manager depicted in Table 1, the true power comes from the process used to identify and categorize fruitful actions and then explore the adjustments going forward. Essentially, the process allows the manager to see where she is having impact—and where she needs to concentrate her efforts in the near future.

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Safran had this to say about his role as an MFP: "…. with the Managerial Finance Professional or MFP, I finally had a perfect description of what I am and what I do. It fit me perfectly, as it fits most of the members of IMA. I added MFP to my résumé and business card. It may be a coincidence, but within a month I had two interviews, and I started my new job last week as a Controller."

Finally, from you, my fellow members, I have seen a renewed interest and have received so much feedback, information, and support that I really do feel a new enthusiasm and pride sparking in our ranks. Keep up that spirit for Larry White and his team as they continue IMA's quest to reclaim the domain of the management accounting profession.

To say "Thank you" is not enough to express what an honor and privilege it has been to serve you this year. But thank you all for helping to "Rekindle the Spirit of IMA."

See you in Chicago June 26-30. As always, keep in touch. I can be reached at kwallin@imanet.org. ■

[TAXES] *cont'd from p. 14*

taxpayer and thus must be recognized. The key to recognition or deferral is an unrestricted present right of the taxpayer to control the disposition of the income. If substantial limitations or restrictions hinder the taxpayer's right of access to income, then recognition can be deferred. Taxpayers who seek to defer income recognition must avoid an unqualified right to control that income. ■

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For this company, the effect of *focus* has been galvanizing, like opening the doors during spring cleaning and allowing fresh air to blow in. Managers are learning what actions actually make a difference as seen by people throughout the organization.

One key lesson is that by keeping the attention on results and allowing employees to assess actions using an effectiveness scale, managers have specific information necessary to see where their actions correlate to constructive outcome and where they are having virtually no impact.

When focus is approached from deep feelings, the results are particularly sweet. Southwest Airlines' logo, for example, celebrates "The Luv Connection." Sentimental? Corny? Perhaps. But with it, Southwest has achieved 31 years of unbroken profitability in an industry that consistently bleeds red jet fuel.

In a January 22, 2004, press release, Southwest noted it "was included in *Global Finance* magazine's January 2004 'Expert's List of the World's Most Socially Responsible Companies' and recently recognized as the 'Best Domestic Airline of the Year' by *Travel Weekly* magazine." The release went on to say, "We commend our *caring and altruistic Employees* for these honors" (emphasis added).

Southwest's results show what can happen when leaders focus on liberating people's passion to engage fully in the enterprise's mission—to unreservedly give it their best effort. Unfettered energy and enthusiasm provide an edge for superior accomplishment; they facilitate clear decisions in a "tough-minded but soft-hearted" framework.

Such results are achieved not by the *doing* but by the *being* of leadership: focusing on the things that really matter. ■

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