CHAPTER 1

Strategy Gap

WHAT GAP?

We often come across companies that have set an ambitious long-term goal, perhaps to double revenue and profits over five years, or to dramatically increase the proportion of revenues coming from new businesses, but have devoted almost no intellectual effort to thinking through the medium-term capability-building program that is needed to support that goal. In too many companies there is a grand, and overly vague, long-term goal on one hand . . . and detailed short-term budgets and annual plans on the other hand . . . with nothing in between to link the two together. . . . There seems to be, in many companies, an implicit assumption that the short term and long term abut each other, rather than being dove-tailed together. But the long term doesn't start at year five of the current strategic plan. It starts right now![1]

—Gary Hamel and C.K. Prahalad,
Competing for the Future

Long-term goals and detailed, short-term budgets, with nothing to link the two together. Does this organization sound familiar?

Whatever the answer, most business professionals understand that achieving a long-term goal requires a series of logical, achievable, sequential steps. Organizations cannot rely on chance or luck. Yet the steps that lead from where a business is today to where it wants to be—its objectives—often are missing.

The "strategy gap," as this group of missing steps is called in this book, is real and exists within most organizations. Often unseen, the gap is a threat to the future performance—and even survival—of an organization and is guaranteed to impact the efficiency and effectiveness of senior executives and their management team.

Imagine for a moment that you are early in your chosen career and the thought of retiring is many, many years away. However, your objective is to retire early, perhaps at 55. To achieve this objective, you have to start planning and executing the plan today. It is no use waiting until you are in your 40s to start executing the plan; it will be too late and you will need to push that retirement date out much farther than desired.

Or consider an oil tanker navigating its way into a port. Newton's law says that a body in motion tends to stay in motion unless something changes it. An oil tanker weighing 500,000 tons requires over an hour and six miles just to slow down from 15 knots. This means that the plan to stop has to be executed well in advance of the intended result.

It is the same in business. Organizations must plan and start executing that plan today if they expect to achieve their objectives some time in the future. Yet surveys indicate that this just is not happening. Despite the increased spending on systems and the technological advances in recent years, only 33 percent of executives take advantage of electronic decision support tools that could help them in managing performance.[2]

The failure of organizations to manage the transition from where they are to where they want to be is one of the most critical management challenges facing senior executives today. Consider that in 2001, more than 250 U.S. organizations—with a combined asset value exceeding $255 billion—failed. As this book is being written, companies are on track to match that figure in 2002. More than 25 percent of the top 100 U.S. companies that survived in 2001 lost at least 66 percent of their market capitalization.[3] Without the ability to achieve objectives, executives and managers become mere bystanders in an organization where performance—or nonperformance—"just happens."

So what is going wrong? What is it about the strategic planning process and its execution that fails? Why do systems so frequently fail to live up to management's expectations? These are crucial questions that need to be answered if the strategy gap is to be avoided.

FAILURE OF STRATEGIC PLANS

According to the dictionary, strategy is "a plan," "an approach," and "a line of attack." There are many different types of strategy, which will be discussed in the next chapter. For now, consider strategy to be "the art of guiding, forming, or carrying out an action plan." When applied to business, strategic planning is about deciding where an organization wants to go and how it is going to get there.

Strategic planning is still the most widely used tool for managing the performance of an organization. In Bain & Company's annual survey of senior executives from around the world, 76 percent of these executives said they look to strategic planning as the top management tool to improve long-term performance and to strengthen integration across an organization. Despite the appearance of many other tools, the report states that senior management trusts familiar tools during difficult times.[4]

Strategic plans typically have a structure that makes them easy to follow. Most start by stating the purpose of the organization, which is usually followed by documenting the long- and short-term goals and the plans for achieving these goals. However, the terminology contained within these plans often varies between organizations, and the words have different meanings. In the context of this book, these definitions will be used:

- *Mission.* A concise statement of the organization's reason for existing
- *Objectives.* Broad statements describing the targeted direction
- *Goals.* Quantifications of objectives for a designated period of time
- *Strategies.* Statements of how objectives will be achieved and the major methods to be used
- *Tactics.* Specific action steps that map out how each strategy will be implemented
- *Key Performance Indicators (KPIs).* Measures of performance that show progress of each tactic in reaching the goals

For its Apollo space program, for example, NASA's strategic plan may have looked something like this:

Mission: Lead all other nations in the race for space.
Objective: Send a man to the moon and bring him back alive.

Goals:	Be the first to do it. Do it by the end of the decade.
Strategy 1:	Investigate and select safe landing sites for manned missions.
Tactic 1:	Create and launch a series of unmanned spacecrafts to take and transmit high-quality pictures of the moon back to Earth for scientific study.
KPI 1:	Launch moon reconnaissance spacecraft by the middle of year 2 of the plan and analyze photos by the end of that year.

For a manufacturer of consumer electronics today, the strategic plan may look like this:

Mission:	Be the premier global provider of consumer electronics.
Objective:	Expand the cellular phone product line.
Goals:	Cellular sales for all regions will be 35 percent of total revenue with an overall increase in revenue of 5 percent.
Strategy 1:	Target a new market segment—senior citizens.
Tactic 1a:	Launch a new cell phone with larger pushbuttons and a “panic” button that connects the user immediately with the local emergency response unit, coupled with a special senior citizen discount rate.
KPI 1a:	Produce 1,000 units by May.
Tactic 1b:	Partner with existing national senior citizen organizations for additional user benefits and marketing opportunities.
KPI 1b:	Sign two partnerships by April.

Certainly these examples are simplistic. They are used only to demonstrate the intended meanings of words used in this book. Also for the purposes of this book, it is assumed that organizations know how to prepare a good plan. A typical organization, for example, would have several objectives, each with a set of goals. Each goal could have several strategies, which in turn would have tactics and associated KPIs. Tactics must have measurable KPIs in order to gauge their success. Without these KPIs, an organization has no way of knowing whether a particular strategy worked. Without successful strategies, the organization will not achieve its goals and objectives.

Strategic planning as a management tool has existed for decades. Lack of planning is not causing the strategy gap. According to Hackett Best Practices, a division of Answerthink, companies spend on average nearly five months each year on strategic planning; a little over four months are spent on annual financial planning.[5] This leaves just three months a year when a typical company is not actively planning. A joint report by Cranfield University School of Management and Accenture indicates that planning and budgeting consume an astonishing 25,000 person-days annually at a typical $1 billion company. The same report also suggests that 80 percent of companies are dissatisfied with their planning and budgeting processes.[6]

Failure to implement the strategic plan can be disastrous. At best, an organization might achieve acceptable performance based on luck and quick tactical thinking. At worst, the organization may cease to exist. Today's corporate world is littered with the remnants of organizations that failed to implement their strategic plan. An article investigating the reason for the spectacular failure of dot-com companies found that, in most cases, the failures had nothing to do with the strategic plans themselves. The failures resulted from a lack of executing those plans.[7]

So the questions remain: What causes the gap between vision and execution? What can be done to close it? What role should systems play? Based on existing research and experience, the main causes of the strategy gap can be grouped into three areas, each of which interacts with the others:

1. The way management acts to implement strategic initiatives
2. Traditional processes (e.g., budgeting, forecasting, reporting) used to implement strategy
3. Technology systems used to support those processes

MANAGEMENT-INDUCED GAPS

Management can cause a gap between strategy and execution through both action and inaction. Four main ways management causes this gap include failure to secure support for the plan, failure to communicate the strategy, failure to adhere to the plan, and failure to adapt to significant changes.

Failure to Secure Plan Support

The senior management team must develop a strategic plan with objectives, goals, strategies, and tactics that everyone supports. If people do not accept and support the plan, they are unlikely to put in the right amount of effort to make it succeed. Their allocation of resources may be counterproductive to implementing strategic initiatives, while their management time is diverted into seeking out factors that will justify their position. This misplaced time and effort will lead to a gap, which could prevent the execution of the plan.

To achieve buy-in, management must create a corporate culture and a set of values that support the vision and guide employees' decisions and behavior. Employees must have the opportunity to provide feedback regarding their ability to implement strategy. Not listening to their views, not addressing—and resolving—conflicts and major differences of opinion, and not building a learning culture—one that tracks and learns from its own successes, failures, and mistakes—will result in strategies that are unrealistic and cannot be implemented. This situation leads to the strategy gap.

Failure to Communicate the Strategy

Operational managers and their employees are typically the people within an organization who implement strategy. They need to know how the strategy impacts them. Yet according to research by Kaplan and Norton, creators of the Balanced Scorecard, "less than 5 percent of the typical workforce understands their organization's strategy."[8] Without a clear idea of what the strategy, vision, and direction of the organization are, they are unlikely to act in ways that will result in effective implementation of the corporate plan.

Communication of strategy is vital in all management processes. When budgeting, employees need to see the tactical plans and related targets that affect them so they can modify their behavior accordingly. During the year, they need to assess how well they are carrying out those tactics and the progress they are making toward strategic goals. When forecasting, employees need to know when their activities are unlikely to achieve their KPIs and, hence, their strategic goals so they can act early to bring the tactical plan back on target. Technology clearly has a role to play in facilitating this communication. Failure to effectively communicate strategy and how well or poorly it is being implemented will result in the strategy gap.

Failure to Adhere to the Plan

As the year progresses, many organizations make decisions reactively rather than strategically. Often the cause is the reporting of results based on a purely financial view of the organization, such as on the chart of accounts by cost center, rather than by a strategic and tactical view. As a result, operational managers focus on financial variances that do not relate to the specific strategic initiatives outlined in the plan. To put things back on track, the accounts become the target of any decision rather than the agreed-on action plans, which may have long been forgotten.

Test this for yourself. In your current reporting pack, how many of the reports tie actual and forecast results back to the strategies outlined in the strategic plan? The reports may monitor the goals, but how many of them actually monitor KPIs by tactic? Without this link, organizations are likely to act and react in ways that are divorced from the strategic plan, which results in the strategy gap.

Failure to Adapt to Significant Changes

The reality of today's business environment is that it continually changes. Strategic plans are built on a set of assumptions, such as market growth, production capability, and competitor actions. If these assumptions change, it is unlikely that the plan will still hold true. Following the attacks of September 11, 2001, for example, most organizations found themselves in an economy that was substantially different from the one that existed when they planned earlier in the year. Continuing to follow a plan when the basic assumptions on which it was founded have changed makes no sense. Unless plans are modified to reflect changes to these assumptions, the result will be the strategy gap.

PROCESS-INDUCED GAPS

The traditional processes an organization uses to implement and monitor strategy are the second set of strategy gap causes. Once a strategic plan has been researched and created, what happens next? How is the plan translated into action? How are the organization's assets allocated to the various strategic initiatives? How is progress monitored and the success or failure of tactics measured? For most organizations, the key tool used to implement strategy is the annual budget, while the processes of actual reporting and forecasting are used to monitor achievement. But the way in which these processes are approached can lead to the strategy gap.

Lack of Strategic Focus

The objective of any process will determine what gets measured, by whom, and how far in the future. It may seem obvious that the budget should support the implementation of strategy. After all, the purpose of this tool is to control how resources are allocated, which in turn affects what an organization accomplishes. It also may seem obvious that one of the roles of reporting would be to monitor strategic progress. Unfortunately, there is very little evidence to support that these processes actually achieve this. In the report "Driving Value Through Strategic Planning and Budgeting," the authors cite a lack of strategic focus as one of the criticisms of traditional planning and budgeting. Instead of being focused on long-term business health, traditional planning and budgeting are internally driven and focused on current-year profits.[9]

In a survey conducted by Comshare, Incorporated, participants said that there is typically a gap between the strategic plan and the budget created to support it.[10] The budget tends to be financially focused with emphasis on the chart of accounts by cost center, while the strategic plan tends to be behaviorally focused on strategies and tactics. The result is that budget holders, operational managers, and senior executives are often unaware of how strategic initiatives impact the operating plan or whether resources have even been allocated. Without this linkage, the budget becomes a pure numbers exercise, allowing the strategy gap to emerge. As a result, the budgeting and planning processes actually become barriers to strategy deployment.

The same is also true when it comes to reporting actual results and forecasting future performance. For many organizations, reporting of actuals takes the form of a simple income and expense statement by department, based on the chart of accounts. The reason reporting takes this form is mainly because the general ledger holds income and expense items, and these systems are used to generate the reports.

However, strategic plans, which are typically action based and measure activity, do not fit easily within the rigid account and cost center structure of a general ledger, and so the focus is lost. As a result, there is no direction or logical connection in the budgeting and reporting processes for budget holders to adapt their behavior to achieving strategic goals.

Calendar Based

For most organizations, budgeting is an annual process that follows the strategic plan, and it is a process that just takes too long. Hackett Best Practices reports that a typical organization takes over four months to complete a budget cycle.[11] Organizations with an annual budget must try to predict events that are 16 months away, which is unrealistic and leads to the strategy gap. According to Hackett, in today's fast-paced business environment, planning should be treated as a continuous exercise in operational decision making, resource allocation, and performance management. Yet nearly half of organizations treat planning and budgeting as a strictly fiscal and annual exercise that leaves them unprepared to deal with sudden change. Similarly, Hackett found that 74 percent of organizations wait until the end of the month to issue reports.[12] Doing so delays the opportunity to deal with important emerging trends, which could be vital to the effective implementation of strategy. Interestingly, most organizations have the data; it is their processes and tools that let them down. What is required is a planning, budgeting, and reporting process that is triggered by change, not by the date on a calendar.

Financially Focused

An organization's financial results are the outcome of its strategy implementation or lack of strategy implementation. Although some financial measures, such as investments and expenses, will be used in implementing a tactical plan, many of the measures will be nonfinancial. Indeed, the long-term viability of an organization may well rest on the success of nonfinancial measures such as product reliability, customer satisfaction, organizational learning, and the efficiency of the internal processes. The adoption of methodologies like the Balanced Scorecard can ensure that organizations achieve the correct balance of measures that will be needed to achieve corporate objectives. The general ledger by itself will not be able to supply all the data required. As already mentioned, the chart of accounts is a transactional view of an organization. The reliance on this view cannot support the planning and monitoring of strategy and will lead to the strategy gap.

Internally Focused

Consider an organization that sets and achieves a revenue budget that reflects a growth of 10 percent year on year. Is this achievement a good result? Is it a good result if the general ledger confirms that the goal was achieved while staying within the cost budget? What if the goal was built on the assumption that the market was due to grow at 5 percent, when, if fact, it grew at 15 percent? In this case market share was lost rather than gained.

In most organizations today, reports compare the performance of the organization with the budget, not with competitors and the market. Strategy is nearly always based on a combined internal and external view that includes market and competitor assumptions. To ensure that strategy is being implemented, actual reporting needs to compare performance by strategic initiative and to check that any external assumptions made while planning still hold true. Without this strategic external view, decisions will be based on a view of performance that is too narrowly focused, and the strategy gap will develop.

Lack of Realistic Forecasting

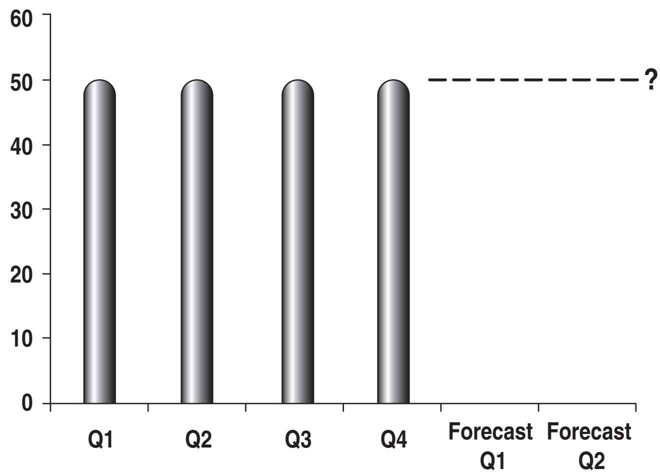
Although business conditions can change rapidly, many surprises that affect organizational performance can be predicted using available data and technologies. By predicting future performance from plans based on the current and perceived business environment, contingencies drawn up in advance can be selected or corrections to the existing plan can be made to avoid or exploit the impact of any variances. The ability to recognize and exploit changing business conditions is the driving force behind rolling forecasts—which also deliver the benefit of reducing or eliminating the annual budget process. According to Hackett Best Practices research, however, only 23 percent of organizations make use of this proven best practice.[13]

When forecasting, many organizations once again focus solely on financial results, such as how much revenue will be generated and what the associated costs will be. As with planning, effective forecasting requires modifying and developing plans to achieve strategic goals. In some circumstances, such as when assumptions have changed, strategic goals may have to be reset. Forecasting involves two steps:

1. Predicting the likely future performance based on current knowledge
2. Evaluating or selecting alternative plans to change the predicted outcome

To predict future performance, the natural life cycle of an organization's products and services should be taken into account. This consideration must take place bottom up; that is, each product and service must be analyzed individually. Consider the forecast depicted in Exhibit 1.1.

Exhibit 1.1 According to this forecast, performance is neither improving nor worsening.



Most people viewing this trend would predict that the forecast would remain level. Now consider the charts in Exhibits 1.2 and 1.3.

Exhibit 1.2 reflects a product that is dying. The forecast suggests that future performance is likely to remain near zero. Exhibit 1.3 represents a product that is growing and whose future performance is likely to reflect a typical life cycle.

Exhibit 1.2 A dying product line.

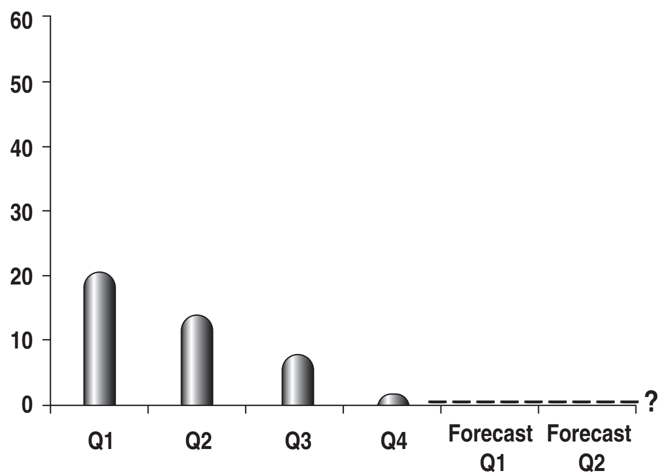
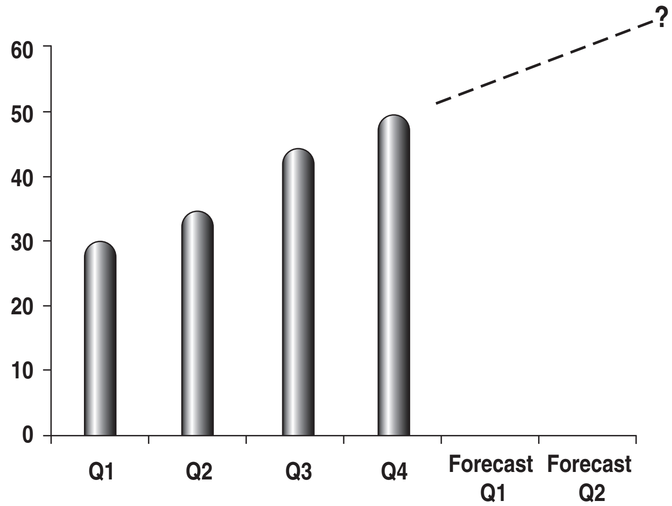
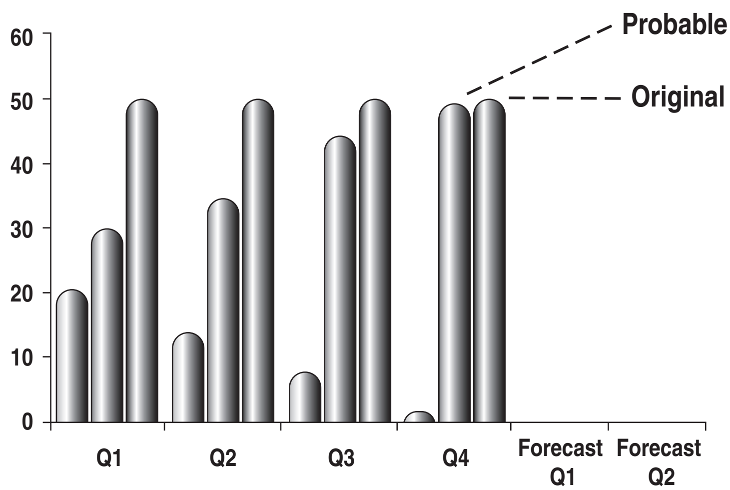


Exhibit 1.3 A growing product line.



Now consider that Exhibit 1.1 was a summary of the two products shown in Exhibits 1.2 and 1.3. Knowing this, the true forecast is going to be far different from what one might have expected before looking at the individual products (see Exhibit 1.4). Forecasting has to take place from the bottom up to avoid creating misleading results.

Exhibit 1.4 A forecast that considers each product line independently reflects different results from one that summarizes and averages all results.



Once a forecast has been generated, it can be used as the basis for "what if" analysis, the process of evaluating alternative scenarios. The aim is to evaluate what changes are required to the tactical plan to achieve the strategic goals. As with budgeting, this evaluation needs to be done by strategic initiative. The result will be the predicted income statement.

Organizations that reduce the forecasting process to a simple extrapolation into the future will reap unrealistic and misleading predictions. They will be unable to modify behavior effectively to achieve strategic goals, which will result in the strategy gap.

Other Factors

Two other factors that can contribute to the strategy gap are more attributable to organizational behavior than to the processes themselves; nevertheless, they need to be taken into account when designing a solution. The first factor is a lack of accountability and commitment to the budgeting process. Budgeting is often a game in which budget holders inflate costs and suppress revenues because they expect senior management to demand reduced costs and increased revenues during a second budget pass. In addition, when a budget is handed down to budget holders without giving them a chance for input, budget holders feel free to miss their targets. After all, it was not their budget. This game playing produces unrealistic budgets, an absence of accountability, and a lack of commitment to the final plan. The result will be the strategy gap.

The second factor is wrongly focused incentive plans. Budget holders and management often are paid on their ability to meet or beat the budget. This fact will affect their decisions when it comes to planning and reporting their performance and does little to help with the implementation of strategy. In some cases it will actively work against the implementation of strategy. Hackett found that when management motivation was linked to strategy rather than to the annual plan, budgeting cycles were reduced and managers were less afraid of taking risks.[14]

TECHNOLOGY SYSTEM-INDUCED GAPS

The third area that causes the strategy gap involves the traditional systems used to support the planning, budgeting, forecasting, and reporting processes. Issues include fragmented systems and misplaced dependence on enterprise resource planning (ERP).

Fragmented Systems

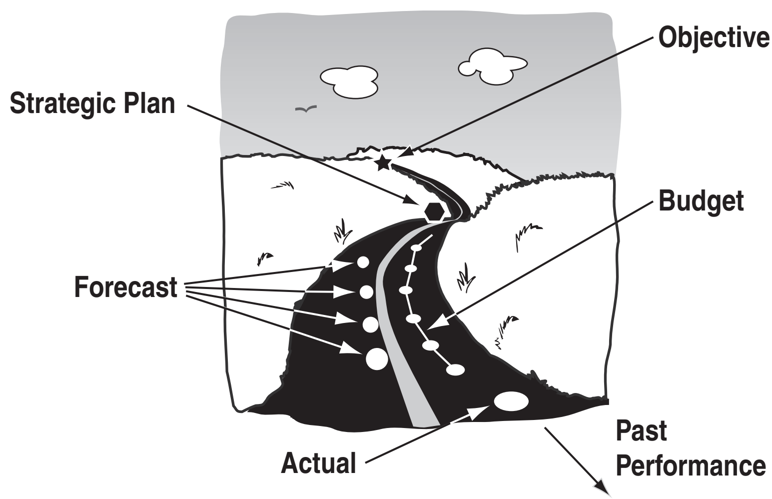
In most organizations, planning, budgeting, forecasting, and reporting are treated as separate, disconnected processes and supported by different technology solutions. In fact, these processes are all part of the much larger process of strategy implementation. The following analogy illustrates why this separation does not make sense.

The journey that a business takes over time is like traveling down a road (see Exhibit 1.5). The road curves and changes direction, and its exact route often is hidden from view. In the same way, business direction continually varies because of changing customer requirements, competitors' actions, or other occurrences in the business environment.

On this journey, the business objective rests on the horizon. This objective, based on current circumstances and assumptions, is the planned destination for the organization. It serves as a beacon, guiding the organization's actions and decisions. The journey is divided into a number of shorter segments, each of which the organization will arrive at over time, allowing the organization to gauge its progress.

To reach the point on the horizon, the traveler outlines a route. This plan identifies the main roads to be traveled and the major cities the traveler will pass through en route to the final destination. In the same way, strategic plans outline the route an organization will travel to reach

Exhibit 1.5 A successful business journey requires knowledge of the starting point, final destination, possible routes, and roadblocks.



its objective. The journey may take months or years to complete. The key roads are analogous to the strategic plan's tactics that must be performed to achieve the objective. Cities are analogous to key performance indicators that will tell the organization if the tactics have been completed and if it is on target for success.

Continuing, the traveler may plan in greater detail the portions of the journey to be attempted in the near future. The plan may include the names of townships, descriptions of landmarks, and locations of road junctions. These are vital indicators. Without them, the traveler may go in the wrong direction without realizing it until much later. The budget is like that detailed plan outlining the organization's immediate route. It is very much linked to the strategic plan but contains far more detail. With the budget, the business assigns money, people, and assets to the initiatives that will keep the organization on course to reach its objective.

Monitoring progress relative to the detailed plan is a vital activity because it shows the organization whether it is on target. Past performance is of interest, but it actually does little to help the business navigate the road ahead. On the journey, organizations will come up against unexpected diversions, such as construction (activities that are not yet implemented), accidents (activities that are having an adverse impact on performance), and heavy traffic (intense competition for the same customers). These diversions will cause delays and can even lead to dead ends unless the organization can avoid them. Similarly, organizations may come across new roads (new business opportunities) that were not on the map when the journey started. They may discover that taking advantage of these roads can enable them to reach their destination sooner than anticipated.

Finally, like directional signs and mile markers, the forecast tells an organization whether it is heading in the intended direction and where it will end up unless it takes immediate action. The enterprise must monitor position and make adjustments constantly. Occasionally it may need to make a major detour—sometimes even heading in what seems to be the wrong direction—to achieve its final objective. By taking note of the signs—the projected forecasts—and using judgment based on experience, business leaders can make intelligent adjustments to the plan. These adjustments will not be just a once-a-year activity. They may become necessary at any time to keep on track toward the intended destination.

Strategic planning, budgeting, forecasting, and monitoring actuals are all part of the same process—moving an organization toward its objective. Together, they are essential components in the implementation and execution of strategy. When performed in isolation, however, they provide little value.

Quite often, managers are asked to budget using systems that do not allow them to see the strategic plan or latest forecast. It is like asking someone to drive down the road with only partial sight, no map, and no idea of the final destination. To drive performance, the company needs to see the whole travel plan: objective, strategic plan, forecast, actuals, and budget. These elements are all part of the same process.

This journey, or performance management process, is continuous. Markets and competitors do not remain motionless to accommodate an organization's annual planning process. Traveling down this road smoothly and staying on course, like driving a car, requires regular, small adjustments.

Unfortunately, the traditional systems that support planning, budgeting, forecasting, and reporting are inflexible. Each component is isolated from the others. In addition, often each piece of the process is supported by a different technology than the others, causing integration problems. For example, the strategic plan may be presented as a text document; the budget may be prepared in a spreadsheet; actual results may be reported in the general ledger; and analyses may be performed using an online analytical processing (OLAP) tool. These systems are completely disjointed, manually intensive, and error-prone. As a result, they help create the strategy gap. In addition, these systems tend to suffer from other problems that also create gaps:

- *Difficult to change.* Most existing management systems do not allow changes to be made easily. Altering structures, accounts, and basic assumptions so that management can quickly see the impact of change is complex and time consuming. Sadly, most systems are nothing short of glorified adding machines—and they do not even do this very well.
- *Reporting problems.* Systems tend to report from one perspective—usually accounts down the page, and time and version across the page, with each page representing a cost center. Viewing data by product, turnover, geography, or any other business perspective—such as strategy and tactic—is extremely difficult. In addition, many systems require a great deal of effort to disseminate actuals, the latest forecast, and strategy information throughout the organization. These difficulties prevent the detailed analysis of budgets, forecasts, and actual results in context and can result in the approval of unrealistic plans.

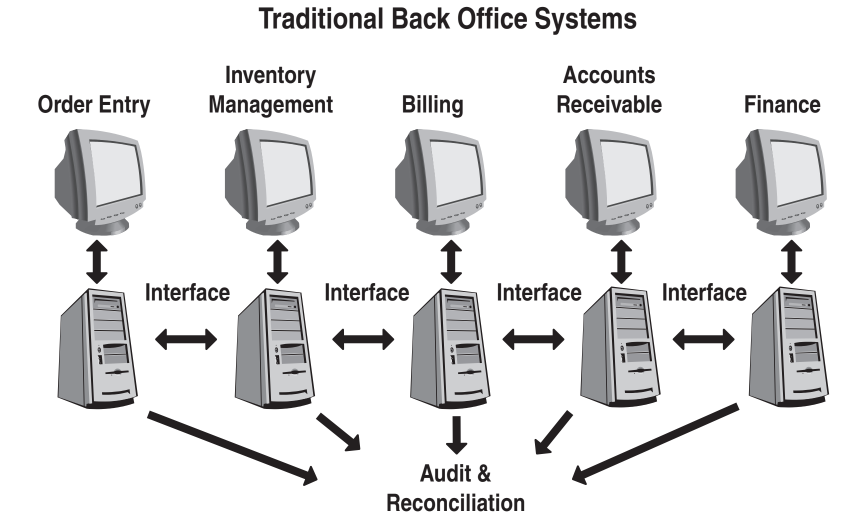
- *File management issues.* Many organizations still rely on spreadsheets for preparing budgets and reporting results. While spreadsheets are great personal productivity tools, they are a nightmare when used as a corporate planning and reporting system. In addition to flexibility and reporting problems already discussed, spreadsheets and many other file-based systems also incur version control and other problems because multiple files have to be maintained, relinked, and then redistributed. Apart from the time and error-prone nature of this task, you can never be sure that users are now using the right version.

Misplaced Dependence on Enterprise Resource Planning

A second system-induced gap can be caused by the reliance some organizations have placed on their enterprise resource planning (ERP) systems to implement strategy. At first glance, such reliance seems logical.

Before ERP, the processes that made up the supply chain—order entry, inventory management, billing, accounts receivable, and others—were separate functions supported by multiple stand-alone systems, often running on multiple technologies (see Exhibit 1.6). Each part of

Exhibit 1.6 Prior to ERP, the supply chain consisted of multiple processes, technologies, and links.



the process could be owned by a different department or operating unit. The problems these systems generated are similar to those encountered with today's planning, budgeting, and reporting systems:

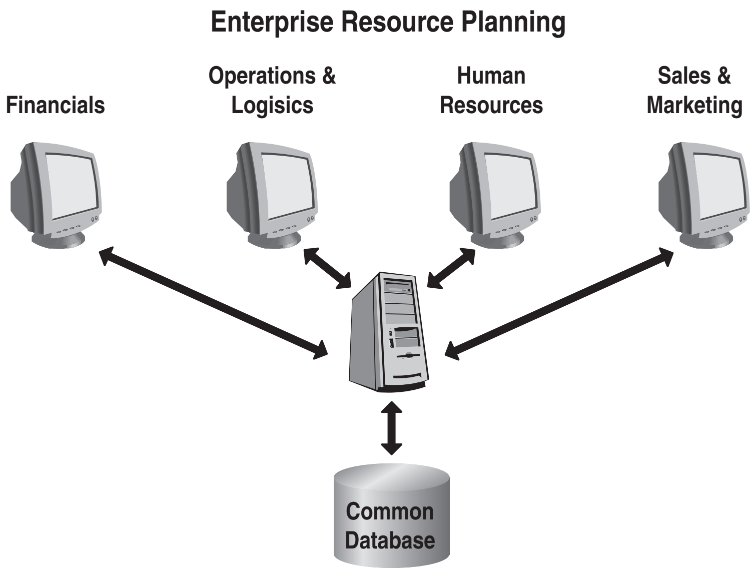
- Expensive in terms of both time (maintenance) and money (hardware and software, personnel). Software had to be maintained on individual desktops. Information technology (IT) staff had to learn multiple technologies. If the system had been created inhouse by a person who then left the company, the organization had a big problem.
- Data integrity and version control issues. Changes in one system were not automatically reflected in other systems, data often had to be rekeyed, and data were shared by transferring files. Many departments multiplied by many files equaled trouble. Organizations could never be certain that the information they were basing decisions on was accurate and up to date.
- Organizations could not easily see what was happening across the enterprise, making it difficult to implement corporate strategy, measure its success, and make informed decisions.

Enterprise resource planning was hailed as the solution because it integrated the supply chain processes and supporting systems (see Exhibit 1.7). The ERP systems increased the efficiency and speed of these operations.

Because ERP systems appear to hold most of the actual data in a centralized database, organizations today are looking to these systems to solve their planning, budgeting, and reporting problems. Many organizations are also trying to leverage their huge investments in ERP implementations to get a return. Given that many ERP vendors are now offering "integrated" planning, budgeting, and reporting applications on top of ERP, this initially seems an attractive solution.

The problem, however, is that ERP is the wrong vehicle for implementing strategic plans just as a farm tractor is the wrong vehicle for taking a family on vacation. Gartner, the Stamford, Connecticut–based research firm, reports that "[a]lthough ERP systems have largely addressed the needs of transactional users, they have not been able to address the needs of strategic and operational users."[15] The main reasons given are the complexity of these systems for users and their closed architectures, which make it difficult to integrate non-ERP data. All enterprise resource planning systems are focused on transactions, not on strategy. This very issue is the reason why today's traditional planning, budgeting, forecasting, and reporting systems fail.

Exhibit 1.7 ERP integrated supply chain processes and technologies.



Implementing a strategic plan requires the dissemination of goals, objectives, strategies, and tactics. Planners must be able to evaluate the impact of economic drivers, forecast trends, and predict the impact of competitors. Senior management needs the ability to analyze alternative operating structures, investments, and divestments. Enterprise resource planning was not designed to deliver these capabilities. It is focused on operational efficiency. Implementing strategy is about management effectiveness. The two are different and require different tools and processes.

ROLE OF THE CHIEF FINANCIAL OFFICER

In the past, the role of the chief financial officer (CFO) was to oversee the transactional systems and to report operational performance to investors and management. That role has evolved dramatically in recent years. Today's CFOs are increasingly seen as true business partners in developing and managing the business.

Being a business partner means that CFOs have to increase the value of the finance department by providing leadership in the areas of planning, reporting, and analysis. Today's executives are overwhelmed by the amount of data that technology allows organizations to generate. When this information overflow is combined with dramatically shortened business cycles, increased competitive activity, and a volatile business climate, operations managers and senior executives cannot keep up, are frustrated, and may become ineffective. The finance department, often the custodian of corporate information, must step up to the challenge by providing new business processes and management methodologies and leverage information technology to help enhance organizational effectiveness.

What could be more important and add more value to the business than to help it execute and adjust its plans, avoiding the strategy gap? Chief financial officers and their teams must provide systems and processes that allow organizations to implement strategy. They must provide business methodologies and systems infrastructures to support collaborative strategic planning, budgeting, forecasting, reporting, and analysis that is focused on the execution of strategy. They must provide systems that can disseminate information to those who need it, when they need it, in a form that makes sense to the business user.

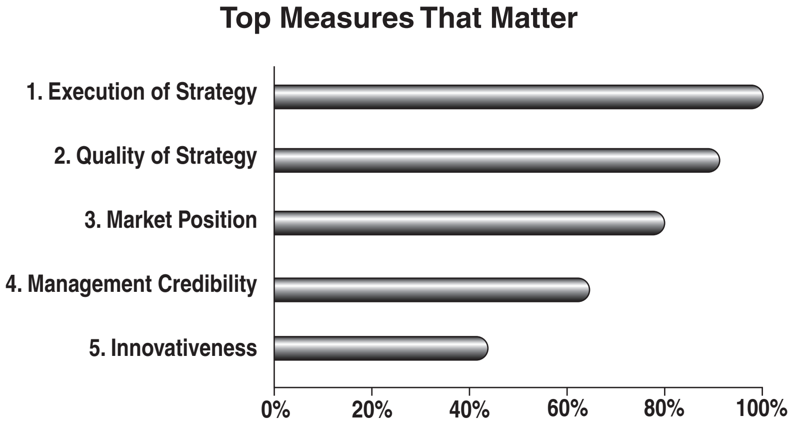
Even though IT will enable this environment, Gartner says that IT-driven initiatives in the area of corporate performance management (CPM) will fail.[16] Finance, not IT, must drive any initiative focused on successfully implementing business strategy. Sadly, many finance organizations today are struggling to provide the expected value, particularly when it comes to managing effective budgeting and reporting cycles and giving timely access to results, analyses, and information.

CORPORATE PERFORMANCE MANAGEMENT

Just when executives, buffeted by continually and dramatically changing business conditions, want to throw up their hands and yell, Why bother with planning?, investors and analysts want proof that companies can execute on the promises they make—their mission, objectives, goals, and strategies. In fact, some investors and analysts feel that execution is more important than the strategy itself (see Exhibit 1.8).[17]

It is against this backdrop of execution failure that a new approach to the implementation of strategy is taking shape. "Corporate performance management" is a term coined by Gartner. They describe CPM as "an umbrella term that describes the methodologies, metrics, processes and systems used to monitor and manage the business performance of an enterprise."[18] The concept of CPM has been around for many years but has been identified by many names. For example, Comshare, Incorporated has used the term "management planning and control" (MPC)

Exhibit 1.8 Investors want proof that corporations can execute strategies.



Source: Ernst & Young, Measures That Matter™

since 1998 to describe the integration of methodologies and processes, while IDC refers to the same concept as "business performance management" (BPM). Whatever term is used, they all refer to the same basic concept of successfully implementing and monitoring strategy.

In the context of CPM, methodologies are the different management techniques and approaches for implementing and monitoring corporate performance. Although many methodologies exist, such as scorecards, activity-based costing, and Stern Stewart's Economic Value Added (EVA), Gartner believes that no single methodology exists for corporate performance management. Organizations will have to blend a number of methodologies together to manage the performance of the enterprise.[19]

Metrics are the specific measures that are used to both manage and monitor the performance of the organization. Some of these metrics will be dictated by the methodology used but will include both financial and nonfinancial measures and will be grouped into both leading and lagging indicators.

Processes are the procedures that an organization follows to implement and monitor corporate performance. Although these can vary widely between organizations, certain key processes are common to all, such as planning, budgeting, forecasting, and reporting.

Systems are the technology solutions that are developed to support the processes that incorporate the chosen methodology(s). They also report on the specific metrics.

All CPM systems leverage technology and best business practices to enable senior executives to confidently and knowledgeably answer questions that help them formulate strategy on an ongoing and real-time basis (see Exhibit 1.9). This is a closed-loop process that starts with understanding where the organization is today, where it wants to go to, what actions have to occur, what goals should be set, and how resources will be allocated to achieve those goals. As plans are implemented, CPM monitors performance of strategies and tactics, highlights exceptions, and provides insight as to why they occurred. From this, CPM systems support the evaluation of alternatives from which decisions can be made—which then leads back to deciding where the organization wants to go.

The technology systems that support CPM must:

- Integrate planning, budgeting, forecasting, consolidation, reporting, analysis, and other processes. A technology system must treat these processes as a continuous course of action, triggered by events rather than by an arbitrary calendar.
- Support methodologies for linking strategy to the allocation of assets (financial and nonfinancial) in support of strategies that can be transformed into action.

Exhibit 1.9 CPM systems help organizations answer questions and formulate strategy.

- Enable executives to communicate and drive strategy down throughout the entire organization in a way that enables people to act and make decisions that support the strategic goals.
- Focus members of the organization on key issues and critical facts rather than overloading them with data from every aspect of the organization. CPM systems must deliver the right information to the right people at the right time and in the right context.

SUMMARY

In the early days of the race for space, President Kennedy outlined the anticipated rewards of establishing space travel leadership. These included such things as new tools and computers for industry, medicine, and the home as well as new techniques for learning, mapping, and observation. Similarly, business is in the early days of corporate performance management. According to Gartner, there will be rewards for those pioneers who understand and implement CPM first. Gartner predicts, "Enterprises that effectively deploy CPM solutions will outperform their industry peers." They also predict that 40 percent of enterprises will implement a CPM solution by 2005.[20]

Effective CPM will eliminate the strategy gap. The following chapters will explore the design and implementation of effective CPM solutions and how to assess the return on a CPM investment. As Gartner recommends, enterprises should understand the implications of CPM and immediately start building their strategy for deployment.

Where are you on the road to CPM?

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