Executing Strategy with New Cost and Performance Management Systems

Dr. Robert S. Kaplan
Baker Foundation Professor, Harvard Business School
Chairman, Professional Practice, The Palladium Group, Inc.
Hidden Profit and Hidden Cost Customers

<table>
<thead>
<tr>
<th>Revenues</th>
<th>Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apparent Profits</td>
<td>Hidden Costs</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Customer A</th>
<th>Customer B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Traditional Costing</td>
<td>Activity-Based Costing</td>
</tr>
</tbody>
</table>

Customer A

- Traditional Costing
  - Profits: [Green Bar]
  - Costs: [Blue Bar]

Customer B

- Activity-Based Costing
  - Profits: [Green Bar]
  - Costs: [Red Bar]

Hidden Profits

Hidden Costs
Hidden profits drive the opportunities from Time-Driven ABC

Operating Profit Profile

20% most profitable generate 180% of profits

20% least profitable lose 80% of net profits

Unrealized Profit Potential
Revealed By Acorn’s EPS

Actual Net Profit

Cumulative % of Units (Customers, Orders, Line Items, Products, Etc.)

Cumulative Net Operating Profit

0% 10% 20% 30% 40% 50% 60% 70% 80% 90% 100%

0% 10% 20% 30% 40% 50% 60% 70% 80% 90% 100%
But Traditional ABC Had Problems

Resource Intensive
Costly to interview and survey people for initial ABC model
Costly and difficult to maintain and update the ABC model as processes and resource spending change, and new activities added

Not Scalable
Can only handle relatively few activities; masks diversity and complexity of demands from individual orders, channels or customers

Inaccurate
Percentage allocations are subjective; difficult to validate estimates
Assumes resources are at 100% of capacity
The Time-Driven ABC innovation! First, calculate the cost per unit time of supplying capacity in processes or departments

<table>
<thead>
<tr>
<th>Unit Cost</th>
<th>=</th>
<th>Cost of capacity supplied</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Practical capacity of resources supplied</td>
</tr>
</tbody>
</table>

Total department (process) costs per quarter are $179,200.
28 customer service employees do the front-line work.
Employees work 20 days per month (after weekends, holidays, and vacation).
Average workday is 8 hours less 80 minutes for breaks, training, and other anticipated down time, so employees are available for productive work for about 400 minutes per day or 8,000 minutes per month.

The unit cost of supplying capacity:

\[
\text{Unit Cost} = \frac{\$179,200}{8,000 \times 28} = \frac{224,000}{8,000 \times 28} = \$0.80 \text{ per minute}
\]

Then, calculate the capacity used – typically unit times – by each transaction on each capacity resource

<table>
<thead>
<tr>
<th>Transaction Type</th>
<th>Time Required</th>
</tr>
</thead>
<tbody>
<tr>
<td>Process customer orders</td>
<td>8 minutes</td>
</tr>
<tr>
<td>Handle customer inquiries</td>
<td>44 minutes</td>
</tr>
<tr>
<td>Perform credit check</td>
<td>50 minutes</td>
</tr>
</tbody>
</table>
Time-Driven ABC combines unit cost and unit time estimates; it also reveals the quantity and cost of unused capacity each period.

1. **Estimate Costs of Resources Supplied**  
   $179,200

2. **Estimate Practical Capacity of Resources Supplied**  
   224,000 minutes

3. **Calculate Cost of Capacity Time**  
   $0.80 per minute

4. **Estimate Unit Times to Perform Each Activity**

5. **Calculate Capacity-Based Activity-Cost Driver Rates**

<table>
<thead>
<tr>
<th>Activity</th>
<th>Unit Time (minutes)</th>
<th>Activity Cost Driver Rate</th>
<th>Activity Cost Driver Quantity</th>
<th>Activity Time</th>
<th>Activity Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Process Customer Orders</td>
<td>8</td>
<td>$6.40 / Order</td>
<td>49,000</td>
<td>392,000</td>
<td>$313,600</td>
</tr>
<tr>
<td>Handle Customer Inquiries</td>
<td>44</td>
<td>$35.20 / Compliant</td>
<td>1,400</td>
<td>61,600</td>
<td>$49,280</td>
</tr>
<tr>
<td>Perform Credit Checks</td>
<td>50</td>
<td>$40.00 / Check</td>
<td>2,500</td>
<td>125,000</td>
<td>$100,000</td>
</tr>
<tr>
<td>Used Capacity</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unused Capacity (17.3%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td></td>
<td>700,000</td>
<td>$560,000</td>
</tr>
</tbody>
</table>
Actions to Transform Unprofitable Products or Customers

Process Improve

Deploy Menu-Based Pricing Based on Cost-to-Serve

Redefine Customer Relationship
Case Study: Kemps

Kemps Dairy is a manufacturer and distributor of ice cream and dairy products and part of HP Hood, the 2nd largest dairy group in the U.S.

Kemps faced growing industry and customer consolidation, increased competition, and greater demands from its customers for specialized products, services, and delivery.

Kemps’ new strategy – to be the best cost producer in the industry and the best branded food products company – required it to have much better insights about its cost of production, delivery, and service.

Kemps Foods: Time-Driven ABC Reveals an Unprofitable Customer

Kemps learned it had a medium-sized unprofitable customer: a chain of specialty ice cream shops with special recipes, small production runs and frequent direct store deliveries

- Revenue (3 months): $1,182,092
- Loss (3 months): ($95,510)
- High number of stores, 133 active ship-to locations, average under $9,000 revenue per store
- 39 locations were profitable; the remaining 94 locations lost money
- Profitable locations made $32,000; the unprofitable locations lost $127,000
- High degree of service (2 – 3 deliveries per week per location, partial cases, dumps, follow-up calls)
- Small order sizes
Kemps Foods: Change pricing or relationship to transform an unprofitable customer.

Kemps CEO offers customer the choice among three options:

Institute an 11 percent price increase to continue the status quo

Maintain existing pricing, but use Kemps-branded ice cream: standard recipes, large production runs, standard packaging, and weekly deliveries

Find another ice cream supplier
Summary: Time-Driven ABC provides multiple benefits.

**Fast and Easy to Implement**
- Can exploit standard industry and company templates

**Scalable**
- Easily scales to enterprise-wide models
- Handles millions of orders and transactions

**Accurate**
- Incorporates capacity explicitly in costing rates
- Captures specific features for particular orders, processes, suppliers, and customers
- Estimates can be validated through observation and work sampling

**Lower Cost to Maintain**
- Data driven, not based on time surveys
- Works from automatic data feeds from ERP and CRM systems

**Proven and Successful in Enterprise Models**
- Charles Schwab, Lowe’s, FedEx, TNT, Citigroup Technology, Coca Cola Belgium, Danisco, Kemps, Sysco, SuperValu, Deutsche Bank, American Express, Johnson & Johnson, Petco.com
The Balanced Scorecard: The Central Component in a New Strategy Execution Management System

Private Sector Organizations

**Financial Perspective**
"If we succeed, how will we look to our shareholders?"

**Customer Perspective**
"To achieve our vision, how must we look to our customers?"

**Process Perspective**
"To satisfy our customers and shareholders, at which processes must we excel?"

**Learning & Growth**
“How do we align our intangible assets to improve critical processes?"

Non Profit and Public Sector Organizations

**Mission (Customer) Perspective**
“How do we have a social impact with our citizens/constituents?"

**Support Perspective**
“How do we attract resources and authorization for our mission?"

**Process (Operational Capacity)**
“To have a social impact and to attract resources and support, at which processes must we excel?"

**Learning & Growth**
“How do we align our intangible assets to improve critical processes?"

**Financial**
“How should we manage and allocate our resources for maximum social impact?"
A Conference Board’s 2007 survey identifies *strategy execution* as CEO’s #1 and #3 issue

<table>
<thead>
<tr>
<th>Relative Ranking</th>
<th>Cite challenge as being of “greatest concern”</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Excellence in execution 38.4%</td>
</tr>
<tr>
<td>2</td>
<td>Sustained and steady top-line growth 36.8</td>
</tr>
<tr>
<td>3</td>
<td>Consistent execution of strategy by top management 31.8</td>
</tr>
<tr>
<td>4</td>
<td>Profit growth 28.4</td>
</tr>
<tr>
<td>5</td>
<td>Finding qualified managerial talent 27.2</td>
</tr>
<tr>
<td>6</td>
<td>Customer loyalty / retention 26.3</td>
</tr>
<tr>
<td>7</td>
<td>Speed, flexibility, adaptability to change 25.4</td>
</tr>
<tr>
<td>8</td>
<td>Corporate reputation 23.7</td>
</tr>
<tr>
<td>9</td>
<td>Stimulating innovation / creativity/ enabling entrepreneurship 18.7</td>
</tr>
<tr>
<td>10</td>
<td>Speed to market 18.2</td>
</tr>
</tbody>
</table>

N – 769. Weighted by regional representation in global GDP (Asia, 21.7 percent; Europe, 35.1 percent; the United States, 28 percent; and other, 15.2 percent). GDP data from the International Monetary Fund, World Economic Outlook Database, September 2006.
The Execution Premium: Companies around the world are using a strategy execution system, based on the Balanced Scorecard, to deliver breakthrough results.

- Revenue up 310%
- EPS up 305%
- Active clients rose from 293 to 500
- Big accounts ($20M+) up from 6 to 27
- Innovation (new product revenues) up 48%
- Ranked #1 employer in IT sector (Dataquest)
- Ranked India’s best managed company

Financial Perspective

Customer Perspective

Process Perspective

Learning & Growth Perspective
Balanced Scorecard Hall of Fame for Executing Strategy
By Industry 2000 – 2007

© 2007 Balanced Scorecard Collaborative/Palladium Group, Inc.
The Execution Premium: Successful strategy execution creates dramatic increases in shareholder value.

<table>
<thead>
<tr>
<th>Marriott Vacation Club (USA)</th>
<th>Key Corp (USA)</th>
<th>Bank of Tokyo Mitsubishi UFJ (Japan)</th>
<th>Thai Carbon Black (Thailand)</th>
<th>LG Philips (Korea)</th>
<th>InfoSys (India)</th>
<th>Minera los Pelambros (Chile)</th>
<th>SOHO (Indonesia)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Perspective</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Revenue up 65%</td>
</tr>
<tr>
<td></td>
<td>Op profit rose by 80%</td>
<td>Share price up 230%</td>
<td>Net profit up 117%</td>
<td>Profit margin 13% higher than nearest competitor</td>
<td>Revenue up 500%</td>
<td>Revenue up 310%</td>
<td>Leading company in Latin America in return on assets for 2 consecutive yrs (America Economic Survey)</td>
</tr>
<tr>
<td>Customer Perspective</td>
<td></td>
<td></td>
<td>Net income up 24%</td>
<td>ROE more than doubled (to 27%)</td>
<td>EPS up 305%</td>
<td></td>
<td>Market share doubled</td>
</tr>
<tr>
<td></td>
<td># Customers rating MVCI &quot;easy to do business with&quot; rose 70%</td>
<td>Retail client retention rates up 5% (3 years)</td>
<td>Ranked #1 brand among Japanese financial institutions</td>
<td>Market share #1 (22%)</td>
<td>Customer satisfaction awards (4 consecutive years)</td>
<td>Big accounts ($20M+) up from 6 to 27</td>
<td>Percent of satisfied customers doubled (40% to 80%)</td>
</tr>
<tr>
<td>Process Perspective</td>
<td></td>
<td></td>
<td>Non-performing loans decreased for 11 consecutive months</td>
<td>COSO-based self-assessment methodology (linked to BSC) achieved high marks from regulators</td>
<td>Overall plant effectiveness = 98.7%</td>
<td>First to produce in 4th/5th generation factories</td>
<td>Top brand award</td>
</tr>
<tr>
<td></td>
<td>BSC integrated with process reengineering to create measurable improvements in all areas</td>
<td>COSO-based self-assessment methodology (linked to BSC) achieved high marks from regulators</td>
<td>Overall plant effectiveness = 98.7%</td>
<td>First to produce in 4th/5th generation factories</td>
<td>Sixth generation factory is world’s largest</td>
<td>Innovation (new product revenues) up 48%</td>
<td>Production lead time on key product reduced (25 days to 2 days)</td>
</tr>
<tr>
<td>Learning &amp; Growth Perspective</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Market share doubled</td>
</tr>
<tr>
<td></td>
<td>% Employees who understood the strategy rose (74% to 86%)</td>
<td>Employees ‘willingness to go the extra mile’ increased from 3.8 to 4.3</td>
<td>Employee satisfaction rose (20% to 89%)</td>
<td>Best employer in IT sector (Datquest)</td>
<td>Ranked #1 employer in Chile (Hewitt)</td>
<td>Ranked india’s best managed company</td>
<td>Percent of satisfied customers doubled (40% to 80%)</td>
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<td>Rated “Best Employer in Chile” (Hewitt)</td>
<td></td>
<td>Top brand award</td>
</tr>
<tr>
<td></td>
<td>Best employer / manufacturing (Hay Group)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Percent of satisfied customers doubled (40% to 80%)</td>
</tr>
</tbody>
</table>
Five Strategy Execution Principles

I. MOBILIZE CHANGE THROUGH EXECUTIVE LEADERSHIP

II. TRANSLATE STRATEGY TO OPERATIONAL TERMS

III. ALIGN THE ORGANIZATION TO THE STRATEGY

IV. MOTIVATE TO MAKE STRATEGY EVERYONE’S JOB

V. GOVERN TO MAKE STRATEGY A CONTINUAL PROCESS
A gap often exists between a Leader’s description of mission, vision, and strategy and the understanding by front-line employees and middle managers.

LEADERSHIP
Why we exist

VALUES
What’s important to us

VISION
What we want to be

STRATEGY
Our game plan

LEAN – SIX SIGMA – TQM – TQC – etc.
   Improve local processes

EMPOWERMENT / PERSONAL OBJECTIVES / GRID
   Motivate employees
Strategy Maps and the Balanced Scorecard bridge the strategy implementation gap: They link leadership at the top to management of initiatives, process improvements and employees’ everyday actions.
Strategy-Focused Organization Best Practices Framework

I. MOBILIZE CHANGE THROUGH EXECUTIVE LEADERSHIP

II. TRANSLATE STRATEGY TO OPERATIONAL TERMS
   2.1 Strategy translated in strategy map
   2.2 Strategy described in Balanced Scorecard
   2.3 Targets identified for all measures
   2.4 Strategic initiatives rationalized
   2.5 Executives accountable for initiatives

III. ALIGN THE ORGANIZATION TO THE STRATEGY

IV. MOTIVATE TO MAKE STRATEGY EVERYONE’S JOB

V. GOVERN TO MAKE STRATEGY A CONTINUAL PROCESS
A Strategy Map Describes How the Enterprise Creates Value for Shareholders and Customers

#1. **Financial** performance, a lag indicator, measures the tangible outcomes from the strategy.

#2. The **customer** value proposition defines the source of value.

#3. Strategic **processes** create value for customers and shareholders.

#4. Aligned **intangible** assets drive improvement in the strategic processes.
Electric Utility, Inc.—Strategy Map

Financial
- Maximize return on assets
- Leverage asset base
- Profitable growth
- Manage operation costs

Customer
- Residential, Commercial, Industrial
  - Innovative solutions
  - Reliable energy supply
  - Socially responsible energy sources
  - Supplier stability
  - Competitive price
- Ensure market-driven skill development
- Industry leading employee satisfaction
- World-class leadership effectiveness

Process
- Optimize Core Business
  - Optimize asset utilization
  - Max Returns on resource allocation
  - Enterprise-wide risk management
  - Continued cost management

- Continued Public Support
  - Proactively build & manage relationships
  - Ensure reliable service
  - Communication and education programs
  - Seamless cross-group delivery of services

- Customer Service Excellence
  - Understand drivers of customer value
  - Effective customer service processes

Learning & Growth
- Business Growth
  - Capitalize on deregulation opportunities
  - Use alliances & joint-ventures
  - Cross-group R&D
  - Trading opportunities
  - Develop innovative service offerings
### BSC Terminology

**Strategic Theme:**
*Diagram of the cause and effect relationships between strategic objectives*

<table>
<thead>
<tr>
<th>Strategic Theme: Customer Service Excellence</th>
<th>Objectives</th>
<th>Measures</th>
<th>Targets</th>
<th>Initiatives</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial</td>
<td>Max. Return on Assets</td>
<td>Statement of what strategy must achieve and what’s critical to its success</td>
<td>Promised Delivery %</td>
<td>Service Dispatch Automation</td>
</tr>
<tr>
<td>Customer</td>
<td>Profitable Growth</td>
<td>How success in achieving the strategy will be measured and tracked</td>
<td>97% (first time)</td>
<td></td>
</tr>
<tr>
<td>Internal</td>
<td>Industry Leading Customer Loyalty</td>
<td>The level of performance or rate of improvement needed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Learning &amp; Growth</td>
<td>Seamless Cross-Group Delivery of Services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Understand Drivers of Customer Value</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Effective Customer Service Processes</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Objectives Statement of what strategy must achieve and what’s critical to its success**

**Measures How success in achieving the strategy will be measured and tracked**

**Targets The level of performance or rate of improvement needed**

**Initiatives Key action programs required to achieve objectives**
## Electric Utility, Inc.—Measures, Targets, & Initiatives

<table>
<thead>
<tr>
<th>Objectives</th>
<th>Measures (D=Drivers)</th>
<th>Targets</th>
<th>Initiatives</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Financial</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Maximize returns</td>
<td>• ROCE</td>
<td>Yr 1</td>
<td>Yr 2</td>
</tr>
<tr>
<td>• Profitable growth</td>
<td>• Revenue growth</td>
<td>14%</td>
<td>14.5%</td>
</tr>
<tr>
<td>• Leverage asset base</td>
<td>• Asset utilization rate</td>
<td>6%</td>
<td>8%</td>
</tr>
<tr>
<td>• Industry leading customer loyalty</td>
<td>• Customer satisfaction rating</td>
<td>80%</td>
<td>85%</td>
</tr>
<tr>
<td><strong>Customer Process</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Optimize core utilization</td>
<td>• % revenue from deregulated products/services</td>
<td>5%</td>
<td>7%</td>
</tr>
<tr>
<td>• Max. return on resource allocation</td>
<td>• % trading revenue</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td>• Continued cost management</td>
<td>• Revenue from new services</td>
<td>$500M</td>
<td>$550M</td>
</tr>
<tr>
<td>• Enterprise-wide risk management</td>
<td>• % customers served through alliances and joint ventures</td>
<td>10%</td>
<td>20%</td>
</tr>
<tr>
<td>• Continued Public Support</td>
<td>• NPV product/service pipeline</td>
<td>$500M</td>
<td>$550M</td>
</tr>
<tr>
<td>• Proactively manage relationships</td>
<td>• % R&amp;D projects meeting protocol gates (D)</td>
<td>90%</td>
<td>95%</td>
</tr>
<tr>
<td>• Ensure reliable service</td>
<td>• Customer/partner satisfaction (5 point scale)</td>
<td>4.0</td>
<td>4.5</td>
</tr>
<tr>
<td>• Communicate/educate customers</td>
<td>• Reliability index</td>
<td>90/100</td>
<td>92/100</td>
</tr>
<tr>
<td>• Customer Service Excellence</td>
<td>• Communication/education coverage (%)</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>• Seamless cross-group delivery</td>
<td>• % communication/education plans executed (D)</td>
<td>80%</td>
<td>85%</td>
</tr>
<tr>
<td>• Understand customer drivers</td>
<td>• Promised delivery %</td>
<td>90%</td>
<td>95%</td>
</tr>
<tr>
<td>• Effective customer services</td>
<td>• New product uptake rate</td>
<td>20%</td>
<td>25%</td>
</tr>
<tr>
<td>• On-time market research projects (D)</td>
<td>90%</td>
<td>95%</td>
<td>100%</td>
</tr>
<tr>
<td><strong>Business Growth</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Capitalize on deregulation opportunities</td>
<td>• Customer satisfaction rating – C.S. Center (see above)</td>
<td>85%</td>
<td>89%</td>
</tr>
<tr>
<td>• Optimize trading opportunities</td>
<td>• Problem resolution cycle time – Customer Service Center (D)</td>
<td>6hr</td>
<td>4hr</td>
</tr>
<tr>
<td>• Develop innovative services</td>
<td>• % rated capacity attained</td>
<td>80%</td>
<td>85%</td>
</tr>
<tr>
<td>• Use alliances and joint ventures</td>
<td>• Employee productivity improvement</td>
<td>2%</td>
<td>3%</td>
</tr>
<tr>
<td>• Leverage cross-group R&amp;D</td>
<td>• % cost reduction</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Learning &amp; Growth</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Ensure market-driven skill</td>
<td>• Strategic skill coverage ratio</td>
<td>65%</td>
<td>75%</td>
</tr>
<tr>
<td>• Industry leading employee satisfaction</td>
<td>• Hours in strategic skills training (D)</td>
<td>10</td>
<td>12</td>
</tr>
<tr>
<td>• World-class leadership effectiveness</td>
<td>• Employee satisfaction rating (5 point scale)</td>
<td>3.0</td>
<td>4.0</td>
</tr>
<tr>
<td>• Leadership effectiveness rating (upward appraisal—5 point scale)</td>
<td>4.0</td>
<td>4.5</td>
<td>4.5</td>
</tr>
</tbody>
</table>

- **Initiatives**:
  - Customer loyalty program
  - Telecom infrastructure development
  - Trading risk assessment (work support)
  - Research alliance program
  - Preventive maintenance
  - Community outreach program
  - Cross-selling marketing program
  - Service dispatch automation
  - CIS upgrade
  - Call center software integration
  - Fossil maintenance benchmark
  - Competency profiling
  - Performance compensation link
  - Leadership training program
Vision: Setting the standard worldwide.

Mission: Luxfer Gas Cylinders will respond to customers’ needs by providing the most innovative products and services in the gas containment marketplace.

F1. Generate an ROS of x% on a sales revenue of £yM per year through innovative organic growth by 2010.

**PRODUCT LEADERSHIP**

- PL1. Grow our global SCUBA business to £xM pa.
- PL2. Grow lightweight medical cylinder revenue to £xM pa.
- PL3. “Provide me a differentiated SCBA cylinder wherever I am.”
- PL4. “Provide me a medical product that enhances my profitability.”
- PL5. Deliver innovative SCBA products.

**CUSTOMER FOCUS**

- CF1. Grow AF sales revenue to £xM pa.
- CF2. Maximize profit from our existing revenue base.
- CF3. “Provide me an AF system that meets my platform requirements.”
- CF4. “Provide me with products and services that I value.”
- CF5. Introduce Type I, II, III & IV AF cylinders.
- CF6. Build close relationships & secure contracts with key target customers.

**OPERATIONAL EXCELLENCE**

- F2. Take advantage of any strategically complementary acquisitions.
- OE1. Improve manufacturing effectiveness at all plants.
- OE2. Reduce costs to improve ROS to x%.
- OE3. Protect volume and margin in high-volume segments.
- OE4. “Provide me with a safe, low-cost product, when I want it, that meets my quality needs.”
- OE5. Drive to World Class Manufacturing through implementation of LPS.
- OE6. Drive cost improvement through capital investment.
- OE7. Excel at supply chain management.
- OE8. Innovate process improvement.

**PROCESS**

- ML1. Identify & fulfill priority requirements providing profitable solutions on time.
- ML2. Build & exploit brand preference for Luxfer.
- ML3. Make it easy to do business with Luxfer.
- ML4. Ensure that we have the right structure populated with the right people in the right positions at the right time.

**BE A MARKET-LED ORGANIZATION**

- L1. Share and implement best practice across the division.
- L2. Create an environment that demands everyone focus on our customers, our markets and our strategy.
- L3. Align organisation structure, skills, and performance objectives to the strategy.
- L4. Ensure that we have the right structure populated with the right people in the right positions at the right time.
- L5. Live our values and build pride in Luxfer.

**Key Growth Markets**

- PL3. “Provide me a differentiated SCBA cylinder wherever I am.”
- PL4. “Provide me a medical product that enhances my profitability.”
- PL5. Deliver innovative SCBA products.

**Other Markets**

- CF3. “Provide me an AF system that meets my platform requirements.”
- CF4. “Provide me with products and services that I value.”
- CF5. Introduce Type I, II, III & IV AF cylinders.
- CF6. Build close relationships & secure contracts with key target customers.

**High Volume Markets**

- OE4. “Provide me with a safe, low-cost product, when I want it, that meets my quality needs.”
- OE5. Drive to World Class Manufacturing through implementation of LPS.
- OE6. Drive cost improvement through capital investment.
- OE7. Excel at supply chain management.
- OE8. Innovate process improvement.
Case from Turkey: ÇimSA’s Strategy Map

“Most Valuable Concrete & Cement Organization of Turkey”

“High-performance Culture for Profitable Growth”

Profitable Growth
- Achieve Outstanding Business Results
- Increase generated value
- Develop new production capacities in strategic regions/markets
- Cost leadership
- Optimize capital structure

High Performance Culture
- “Increase Value to customer”
- Personalized Customer Relationships
- Exceed Customer Expectations

Internal Processes
- Segment Management
  - Optimize sales mix (customer/product/region)
- Operational Efficiency
  - Adapt operational best practices
  - Optimize production costs and energy usage

Enterprise Risk Management (ERM)
- Improve raw materials & cementitious materials/resources management
- Improve logistics

Supply Chain Management
- Improve logistics

“High Performance Processes”

“Çimsa DNA”

Information Capital
- Implement a strategic performance management model
- Harmonize & Unify the information platforms

Human Capital
- Ensure implementation of effective HR management system and framework
- Develop leadership & management capabilities

Organizational Capital
- Achieve organizational alignment/improvement
- Create value through organizational synergies

Our Values: Reliable – Customer-focused – Collaborative
Principle 3: Align the Organization to the Strategy

I. MOBILIZE CHANGE THROUGH EXECUTIVE LEADERSHIP

II. TRANSLATE STRATEGY TO OPERATIONAL TERMS

III. ALIGN THE ORGANIZATION TO THE STRATEGY
   3.1 Corporate contribution to strategy defined
   3.2 Enterprise scorecard guides business units
   3.3 Enterprise scorecard guides support units
   3.4 Scorecards align suppliers and/or customers
   3.5 Scorecard reports to board and/or shareholders

IV. MOTIVATE TO MAKE STRATEGY EVERYONE’S JOB

V. GOVERN TO MAKE STRATEGY A CONTINUAL PROCESS
Alignment in Action
Linked Strategy Maps and Scorecards Assist Vertical and Horizontal Alignment
Shared Objectives Example

Global Corporate Banking Unit (GCBU) Strategy Map

Bankwide identical objective:
- (Corporate and Units)

Objective unique to GCBU:
- (Between Units)

Shared objective:

**Financial Perspective**
- Increase net income:
  - Increase fee income
  - Maximize income from core customers
  - Minimize credit costs
  - Enhance cost efficiency

**Customer Perspective**
- Grow Revenues:
  - Be #1 foreign wholesale bank in the Americas
- Manage Risk:
  - Be a reliable source of credit
  - Provide global network banking
  - Provide speedy and accurate service

**Internal Process Perspective**
- Grow Revenues:
  - Strategically focus on opportunities in Asia
  - Ensure collaboration - Relationship & Purchasing Managers
  - Segmentation and tier up
- Manage Risk:
  - Proactive risk management and compliance
  - Enhance risk management in Latin America
  - Enhance disaster recovery/business continuity plan
- Improve Productivity:
  - Execute major technology and efficiency projects
  - Enhance collaboration throughout supply chain
  - Streamline credit approval process

**Human Capital Perspective**
- Develop succession plan
- Provide training on credit and product
- Competitive environment: teamwork, safe and fair
- Competitive compensation
Strategy-Focused Organizations Use a Best Practices Framework

I. MOBILIZE CHANGE THROUGH EXECUTIVE LEADERSHIP

II. TRANSLATE STRATEGY TO OPERATIONAL TERMS

III. ALIGN THE ORGANIZATION TO THE STRATEGY

IV. MOTIVATE TO MAKE STRATEGY EVERYONE’S JOB
   4.1 Strategic awareness created
   4.2 Personal goals aligned
   4.3 Personal incentives aligned
   4.4 Competency development aligned

V. GOVERN TO MAKE STRATEGY A CONTINUAL PROCESS
Align Employees to Make Strategy Everyone’s Job

Create Strategic awareness: “Communicate seven times seven different ways”

Personal relevance (WIIFM) brings the strategy to life

Sustained communication uses different channels to get the message across

- Leadership meetings
- CEO random visits to employees
- Dear Colleague Quarterly Letter in Mellon News
- Learning lunches & informal discussions
- Intranet
- Working groups facilitated by HR
- Staff briefings

Source: Presented by Jack Klinck, Vice Chairman, Mellon Europe at BSCol European Summit, June 2005
Royal Canadian Mounted Police V Division – Iqaluit (Baffin Island)
Creating a Line of Sight And Making Strategy Everyone’s Job

Customer Example
- Customer Satisfaction
- Customer Retention
- On Time Delivery
- First Pass Yield
- Schedule Adherence
- Line Availability
- Schedule Adherence
- Attendance
- Machine Utilization

Financial Example
- Operating Margin
- Variable Costs
- Period Expenses
- Variable Costs
- Mfg Overhead
- Scrap rate
- Labor/Unit
- Scrap rate

Individual Strategic Objectives and Measures Should Support Higher Levels in the Organization

I. MOBILIZE CHANGE THROUGH EXECUTIVE LEADERSHIP

II. TRANSLATE STRATEGY TO OPERATIONAL TERMS

III. ALIGN THE ORGANIZATION TO THE STRATEGY

IV. MOTIVATE TO MAKE STRATEGY EVERYONE’S JOB

V. GOVERN TO MAKE STRATEGY A CONTINUAL PROCESS

A. RESOURCE MANAGEMENT
   5.1 Budget is driven by strategy
   5.2 Planning linked to strategy
   5.3 Portfolio of strategic initiatives aligned to themes

B. KEY PROCESS MANAGEMENT
   5.4 Process improvement aligned to strategy
   5.5 Best practice sharing in place

C. LEARNING & CONTROL
   5.6 Review and adapt strategy
   5.7 Data and analytics guide strategy
A New Six Stage Management System Links Strategic Planning and Operational Execution

Successful strategy execution has two basic rules: understand the management cycle that links strategy and operations, and know what tools to apply at each stage of the cycle.

Mastering the Management System

Harvard Business Review
January 2008

Harvard Business Review

The Execution Premium

June 2008
The Management System for Strategy Execution Links Strategic Planning and Operational Excellence

1. DEVELOP THE STRATEGY
   - Mission, Values, Vision
   - Strategic Analysis
   - Strategy Formulation

2. TRANSLATE THE STRATEGY
   - Strategy Map / Themes
   - Measures / Targets
   - Initiative Portfolios
   - Funding / Stratex

3. ALIGN THE ORGANIZATION
   - Business Units
   - Support Units
   - Employees

4. PLAN OPERATIONS
   - Key process improvement
   - Sales planning
   - Resource capacity plan
   - Budgeting

5. MONITOR & LEARN
   - Strategy Reviews
   - Operating Reviews

6. TEST & ADAPT
   - Profitability Analysis
   - Strategy Correlations
   - Emerging Strategies

Strategic Plan
- Strategy Map
- Balanced Scorecard
- Stratex

Operating Plan
- Sales Forecast
- Resource Requirements
- Dashboards
- Budgets

results

performance measures

EXECUTION
Process
Initiative
Stage 4 of the Management System: Plan Operations

**Stage 1: Develop the Strategy**
- Mission, Values, Vision
- Strategic Analysis
- Strategy Formulation

**Stage 2: Translate the Strategy**
- Strategy Map / Themes
- Measures / Targets
- Initiative Portfolios
- Funding / Stratex

**Stage 3: Align the Organization**
- Business Units
- Support Units
- Employees

**Stage 4: Plan Operations**
- Key process improvement
- Sales planning
- Resource capacity plan
- Budgeting

**Stage 5: Monitor & Learn**
- Strategy Reviews
- Operating Reviews

**Stage 6: Test & Adapt**
- Profitability Analysis
- Strategy Correlations
- Emerging Strategies

**Execution**
- Process
- Initiative

**Performance Measures**
- Strategic Plan
- Operating Plan
Using the Balanced Scorecard with the Catchball Process

**Catchball Process**

**Leadership team**

- Develop strategy map
- Select measures and targets for Balanced Scorecard process objectives
- Communicate process objectives, measures, and targets down through the organization

**Flow Chart**

1. **Review with next level**
   - Yes → **Pass the ball to the next level**
     - Are targets attainable?
       - Yes → **Commitments reviewed with leadership team**
         - **Implement**, measure results, and report
       - No → **Address and resolve barriers**
         - Yes → **Targets attainable or new targets agreed to?**
           - Yes → **Commitments reviewed with leadership team**
             - **Implement**, measure results, and report
           - No → **Address and resolve barriers**
         - No → **Address and resolve barriers**

2. **Pass the ball to the next level**
   - Are targets attainable?
     - Yes → **Commitments reviewed with leadership team**
       - **Implement**, measure results, and report
     - No → **Address and resolve barriers**
Example of Catchball Process

Balanced Scorecard Customer Objective:
  • *Reduce order to delivery lead time*

Catchball Objectives for Mobile Phone Manufacturing Plant:
  • *Improve on-time delivery*
  • *Reduce order lead times*

Purchasing Department Catchball Objective:
  • *Reduce replenishment time for critical components*
Using the BSC and Quality Assessment Models (Baldrige, EFQM) Together

**Business Processes**

- **Strategic** (Competitive Advantage)
- **Balanced Scorecard**
  - **Vital** (‘Hygiene’)

### Quality Assessment Model

- **Weak**
  - Improve to minimum acceptable quality levels
  - Improve to levels of quality excellence
- **Strong**
  - Maintain high quality levels
  - Potential to cut back current investment
Linking Process Management to BSC Strategic Processes

To achieve this strategic process objective, how must we improve?

- CUSTOMER MGMT
  16. HAVE A STRONG PRESENCE AT EXTERNAL MARKET
  17. SEARCH LONG TERM RELATIONSHIPS ALONG WITH TARGET CUSTOMERS

- APPLIED DEVELOPMENT
  18. BE AGILE AND EFFECTIVE ON THE DEVELOPMENT OF CUSTOMER-ORIENTED SOLUTIONS

- CRITICAL SUCCESS FACTORS
  21. SUPPLY INFORMATION TECHNOLOGY THAT SUPPORTS BUSINESS REQUIREMENTS
  22. EMPOWER PEOPLE AND FORTIFY VALUE-ORIENTED MANAGEMENT
  23. DEVELOP STRATEGIC COMPETENCIES
18. BE AGILE AND EFFECTIVE ON THE DEVELOPMENT OF CUSTOMER-ORIENTED SOLUTIONS

- RDEI - R&D Effectiveness Index
- Time-to-Market

Strategic Objective and Metrics

Critical Success Factors

- BE CONTINUOUSLY INNOVATIVE ON OUR PRODUCT LINES
- HAVE AN IN-DEPTH UNDERSTANDING ABOUT OUR MARKETS AND THEIR TARGET-SEGMENTS
- HAVE A CONTINUOUS MONITORING PROCESS RELATED TO OUR PRODUCTS PERFORMANCE

Business Processes Metrics

- # of Protected Ideas
- # of Co-created Proposals
- % Performance-Controlled Products

New Products

- NEW PRODUCTS PLAN AND STRATEGY DEVELOPMENT
- ESTABLISH PRIORITIES AND PROTECT NEW PRODUCT IDEAS
- IDEA TESTING
- PROPOSALS DEVELOPMENT
- SCHEDULING, BUDGETING AND PRIORITIES ESTABLISHING
- SALES AND NEW PRODUCTS DEVELOPMENT EVALUATION
Dashboards articulate the critical link between strategy management and operations management.

- Identify operational processes key to executing strategy and manage those processes using analytical models rather than instincts
- Analytical models identify drivers to the process and display these drivers on a dashboard accessible to managers that can make an impact
Stage 5 of the Management System: Monitor and Learn

1. DEVELOP THE STRATEGY
   - Mission, Values, Vision
   - Strategic Analysis
   - Strategy Formulation

2. TRANSLATE THE STRATEGY
   - Strategy Map / Themes
   - Measures / Targets
   - Initiative Portfolios
   - Funding / Stratex

3. ALIGN THE ORGANIZATION
   - Business Units
   - Support Units
   - Employees

4. PLAN OPERATIONS
   - Key process improvement
   - Sales planning
   - Resource capacity plan
   - Budgeting

5. MONITOR & LEARN
   - Strategy Reviews
   - Operating Reviews
   - Sales Forecast
   - Resource Requirements
   - Dashboards
   - Budgets

6. TEST & ADAPT
   - Profitability Analysis
   - Strategy Correlations
   - Emerging Strategies

**Performance Measures**

**Results**

**Execution Process Initiative**
Companies use strategy scorecards and operational dashboards to inform their different management meetings.

Operational Review Meetings: Role for **KPI Dashboards**
- Frequent (daily, twice weekly, weekly)
- Departmental and functional personnel
- Identify and solve operational problems (late deliveries, equipment downtime, supplier problems)
- Promote continuous improvement (better, faster, cheaper)

Strategy Review Meetings: Role for **Balanced Scorecard**
- Monthly
- Management team; cross functional, multiple business units
- Discuss and solve problems with strategy implementation
- Manage product and customer profitability
The leadership team uses the BSC to review performance, examine strategic initiatives, make informed decisions, and assign accountability.

Use of a BSC Report in Strategy Review Meetings

1. Focus on the performance of objectives NOT measures.

2. What are the measures telling us? Are the measures driving change and adding focus?

3. What are the root causes of what’s occurring? What are the expectations for the future? And, are current initiatives sufficient to close the performance gap?

4. Are initiatives on track to deliver expected value? If not, why and what can be done to remedy issues?

5. What action steps – including additional or different initiatives - are required to improve performance going forward?

Take Action:

6. Discuss and agree on how to remedy issues.

7. Assign accountability to ensure decisions are implemented.

Identify Performance Issues:

- Focus on the performance of objectives NOT measures.

Analyze Objective Performance:

- What are the measures telling us? Are the measures driving change and adding focus?
- What are the root causes of what’s occurring? What are the expectations for the future? And, are current initiatives sufficient to close the performance gap?
- Are initiatives on track to deliver expected value? If not, why and what can be done to remedy issues?
- What action steps – including additional or different initiatives - are required to improve performance going forward?

Take Action:

- Discuss and agree on how to remedy issues.
- Assign accountability to ensure decisions are implemented.

**ILLUSTRATIVE**
The BSC Review Meeting can be used for strategic learning by asking the right questions.

<table>
<thead>
<tr>
<th>Questions</th>
<th>Answers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Did you execute the plan?</td>
<td>Administrative</td>
</tr>
<tr>
<td>What happened?</td>
<td>Descriptive</td>
</tr>
<tr>
<td>Why do you think that happened?</td>
<td>Diagnostic</td>
</tr>
<tr>
<td>What alternatives are there?</td>
<td>Creative</td>
</tr>
<tr>
<td>What do you think would happen?</td>
<td>Predictive</td>
</tr>
<tr>
<td>Which is the best choice?</td>
<td>Evaluative</td>
</tr>
</tbody>
</table>
Stage 6 of The Management System: Test and Adapt

1. Develop the Strategy
   - Mission, Values, Vision
   - Strategic Analysis
   - Strategy Formulation

2. Translate the Strategy
   - Strategy Map / Themes
   - Measures / Targets
   - Initiative Portfolios
   - Funding / Stratex

3. Align the Organization
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   - Budgeting

5. Monitor & Learn
   - Strategy Reviews
   - Operating Reviews

6. Test & Adapt
   - Profitability Analysis
   - Strategy Correlations
   - Emerging Strategies

Execution

Process

Initiative

Strategic Plan
- Strategy Map
- Balanced Scorecard
- Stratex

Operating Plan
- Sales Forecast
- Resource Requirements
- Dashboards
- Budgets

Performance Measures

Results
Stage 6: Strategy Testing and Adapting Meetings

Analyze External, Competitive Information and Internal Information (Balanced Scorecard, ABC)

- Annually (perhaps quarterly for fast-moving industries)
- Senior management team; functional and planning specialists
- Test and adapt strategy based on causal analytics (Store24) and product-line and channel profitability (role for ABC)
- Establish strategic and operational plans, authorize resource spending, targets, and initiatives
### Summary of Three Types of Management Review Meetings

<table>
<thead>
<tr>
<th>MEETING TYPE</th>
<th>Operational review</th>
<th>Strategy review</th>
<th>Strategy testing and adapting</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Information requirements</strong></td>
<td>Dashboards for key performance indicators; weekly and monthly financial summaries</td>
<td>Strategy map and Balanced Scorecard reports</td>
<td>Strategy map, BSC, ABC profitability, analytic studies of strategic hypotheses, external analyses, emergent strategies</td>
</tr>
<tr>
<td><strong>Frequency</strong></td>
<td>Daily, twice weekly, weekly, or monthly, depending on business cycle</td>
<td>Monthly</td>
<td>Annually (perhaps quarterly for fast-moving industries)</td>
</tr>
<tr>
<td><strong>Attendees</strong></td>
<td>Departmental and functional personnel; senior management for financial reviews</td>
<td>Senior management team, strategic theme owners, strategy management officer</td>
<td>Senior management team, strategic theme owners, functional and planning specialists, business unit heads</td>
</tr>
<tr>
<td><strong>Focus</strong></td>
<td>Identify and solve operational problems</td>
<td>Issues in strategy implementation, progress of strategic initiatives</td>
<td>Test and adapt strategy based on causal analytics</td>
</tr>
<tr>
<td><strong>Goal</strong></td>
<td>Respond to short-term problems and promote continuous improvements</td>
<td>Fine-tune strategy; make midcourse adaptations</td>
<td>Improve or transform strategy</td>
</tr>
</tbody>
</table>
Case From Turkey: Strategy is reviewed systematically in Borusan Holding with a defined calendar & assigned responsibilities

Five years Strategic Planning period at Borusan Group anchors long term horizon to be achieved.

A well defined operation and strategic reporting calendar supports the governance process with clear responsibility set.

BSC reporting is made on monthly, quarterly and annual basis in Borusan. All group companies uses the same framework in Board Meetings to highlight overall strategic highlights feeding the budgeting process.
A Strategy Management Officer Coordinates the Six Stage Management System that Links Strategy and Operations

Plan the Strategy: Develop, Translate and Align (Stages 1-3)

Execute the Strategy: Link to Operations, Monitor, Learn and Test (Stages 4-6)
The Office of Strategy Management is the process owner for several strategy execution processes.

Define, develop and oversee execution of close-loop processes required to manage the strategy.

**Develop the Strategy:** Help the CEO and Executive Team to formulate and adopt the strategy.

**Translate the Strategy:** Design the Strategy Map and Balanced Scorecard. Manage the reporting system.

**Align the Organization:** Ensure that all business and support units have strategy maps and scorecards aligned with the strategy.

**Plan & Fund the Initiatives:** Link financial, HR, IT, and marketing plans to the strategy.

**Review the Strategy:** Shape the agenda for strategy review and learning meetings.
The Office of Strategy Management coordinates with other functions to ensure their processes are aligned to the strategy.

Insure that operational processes owned and run by other functional executives are linked to the strategy.

- **Human Capital:** Ensure that all employee’s goals, incentives and development plans link to the strategy.

- **Financial Resources:** Insure that the expected impact of strategic investments are reflected in operating plans.

- **IT Resources:** Insure that IT plans for applications and infrastructure are aligned with the strategy.

- **Key Business Processes:** Insure that the design of key business processes reflects the strategic priorities and intent.

- **Quality Programs:** Insure that quality management / six sigma programs focus on strategic objectives.

- **Strategy Communications:** Communicate and educate employees about the strategy.

- **Initiative Management:** Identify and oversee the management of strategic initiatives.

- **Best Practice Sharing:** Facilitate a process to identify and share best practices.
Why do organizations fail to get results from their Balanced Scorecard programs?

1. No Executive Leadership and Ownership
   (done by middle management team only; long development process)

2. Scorecard Not Linked to Strategy
   (no strategy map - just KPIs in 4 perspectives; mostly financial measures; done as a systems or a compensation project)

3. Scorecard Not Communicated to Employees

4. Scorecard Not Linked to Management Processes
   - SFO Principles: Mobilize, Translate, Align, Motivate, Govern
   - The 6-stage Closed-Loop Management System
   - Office of Strategy Management
Executing Strategy with new performance and cost management systems

QUESTIONS?