

Beyond
Budgeting

Towards the 'adaptive' organization

How to create
a better model

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'Beyond Budgeting' Summit
8-9 June 2005 - Frankfurt am Main

'Budgeting' is NOT the big issue

Issue 1

Yesterday's management model
is in conflict with
today's competitive success factors

Issue 2

The change required is transformational

$$f(D \times V \times S) > R$$

Agenda

- 1. Problems with yesterday's model**
2. The 'beyond budgeting' vision
3. How to make the change
4. An implementation case

'In search of excellence' principles

1. A Bias for Action.
2. Close to the Customer
3. Autonomy and Empowerment
4. Productivity Through Simplicity
5. Hands-On Management
6. Stick to the Basics
7. Simple Structures and Staff
8. Simultaneous Loose-Tight Properties

Decentralization
and Autonomy
Tom Peters, 1990

In Search of Excellence, Tom Peters and Robert H Waterman jr., 1982

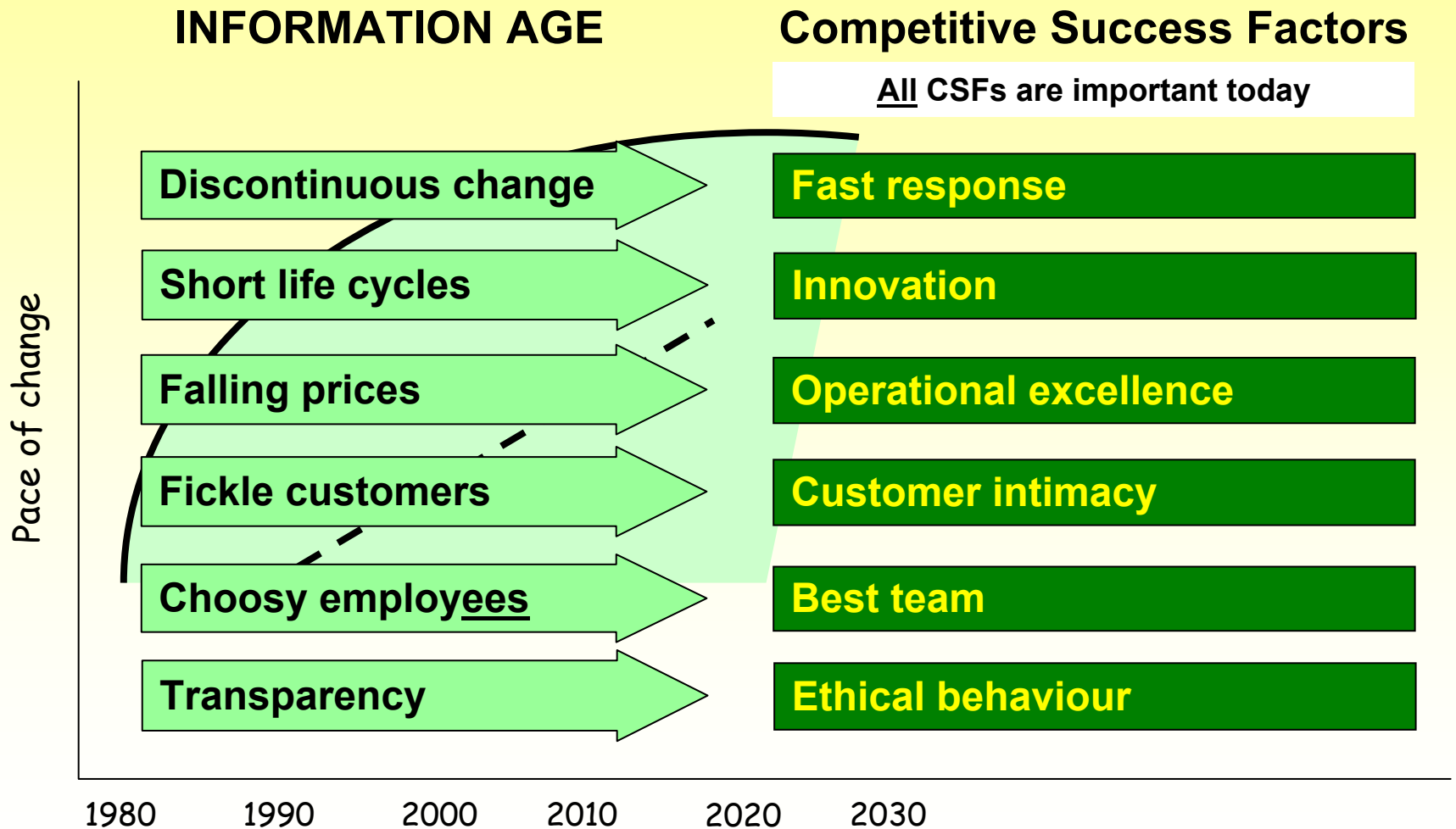
Tom Peters' extra principles

“*Search* was about people, customers, and action. Twenty years later, it's about ideas, liberation, and speed.”

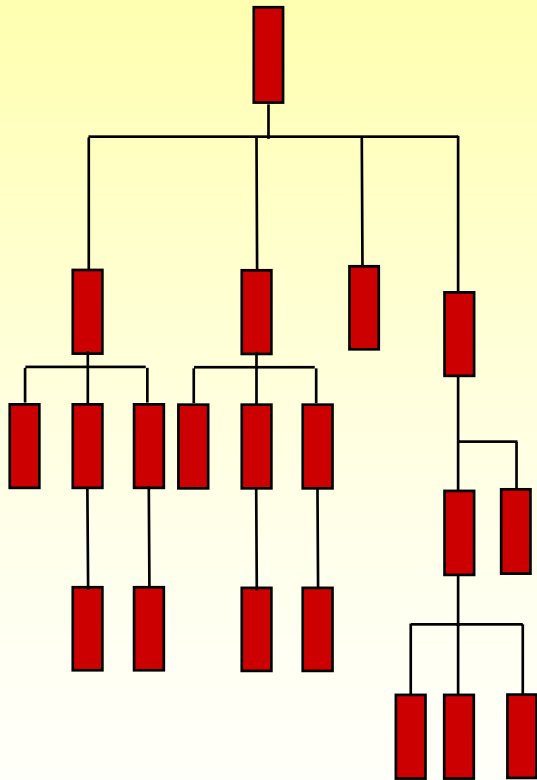
- **Principle 9** - GAK! Which stands for God alone knows! (i.e. Unpredictability).
- **Principle 10** - SAV. Which stands for screw around vigorously. (i.e. Speed of learning).

Tom Peters' True Confessions, Fast Company Magazine, Issue 53, December 2001, Alan M. Webber

Today's CSFs require 'liberation'

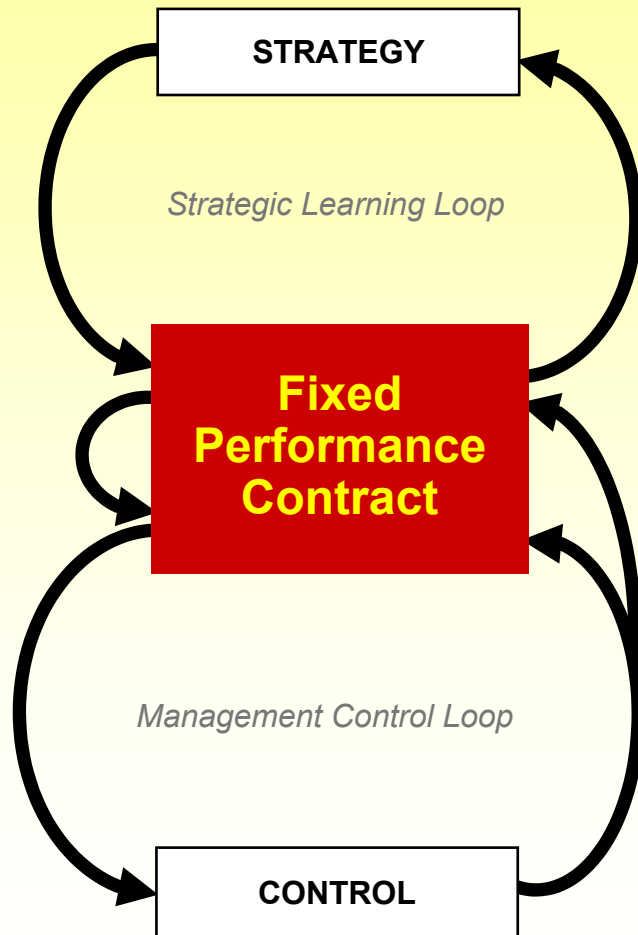


Our organizations are 'prisons'



They
conflict
with our
CSFs

Our processes are 'straightjackets'



They
conflict
with our
CSFs

Our whole model is 'constrained'

CSFs

- **Fast response**
- **Innovation**
- **Operational excellence**
- **Customer intimacy**
- **Best team**
- **Ethical behaviour**

- **Financial performance**

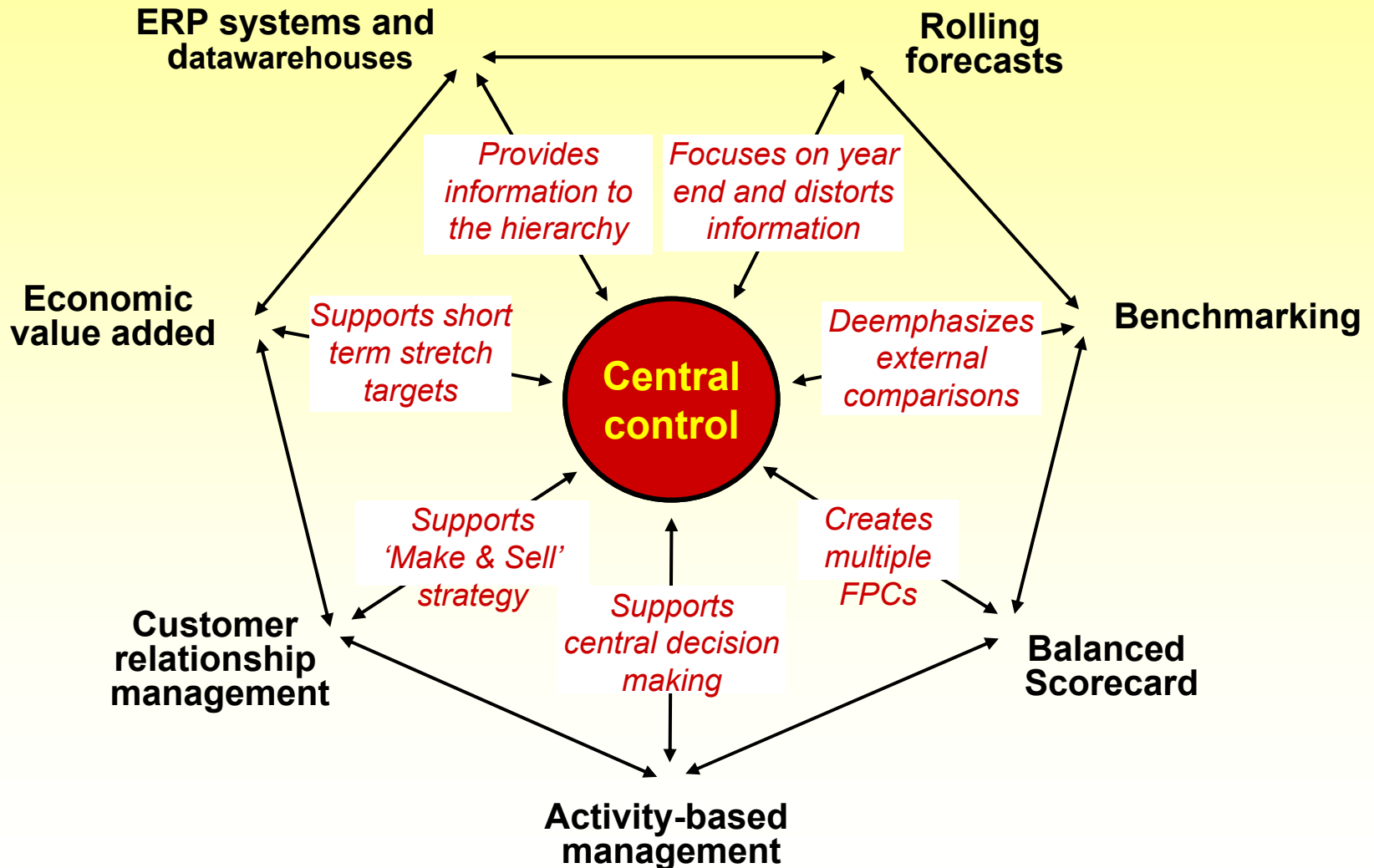
Misalignment examples

- Retarded by annual planning process
- Stifled by centralized bureaucracy
- *'Spend it or lose it'* budget mentality
- Incentives drive short term behaviour
- Motivation is extrinsic, not intrinsic
- Individualism leads to dysfunctional, even unethical behaviour

- Inferior financial results

When pressure is applied, the problems get worse

It undermines our 'modern' tools



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Best cases are the most 'liberated'

- **Ahlseil**, Sweden, Distribution

- **Aldi**, Germany, Retail

- **Borealis**, Denmark, Petrochemicals
- **Ciba Vision**, USA, Eye care
- **Coors**, USA (UK division), Brewing
- **Deutsche Bank**, Germany, Banking
- **Fortis**, Belgium (US division), Insurance
- **Groupe Bull**, France, Computers
- **Guardian Industries**, USA, Glass mfg
- **IKEA**, Sweden, Furniture mfg and retailing
- **Leyland Trucks**, UK, Truck manufacturing
- **Norsk Hydro**, Norway, Energy
- **Omgeo**, USA, Finance
- **Philips**, Netherlands, Diversified

- **Rhodia**, France, Specialty chemicals
- **Ricoh (UK)**, UK, Printers, cameras
- **Schneider Electric**, France, Engineering
- **SKF**, Sweden, Ball bearings
- **Sight Savers Int'l**, UK, Charity

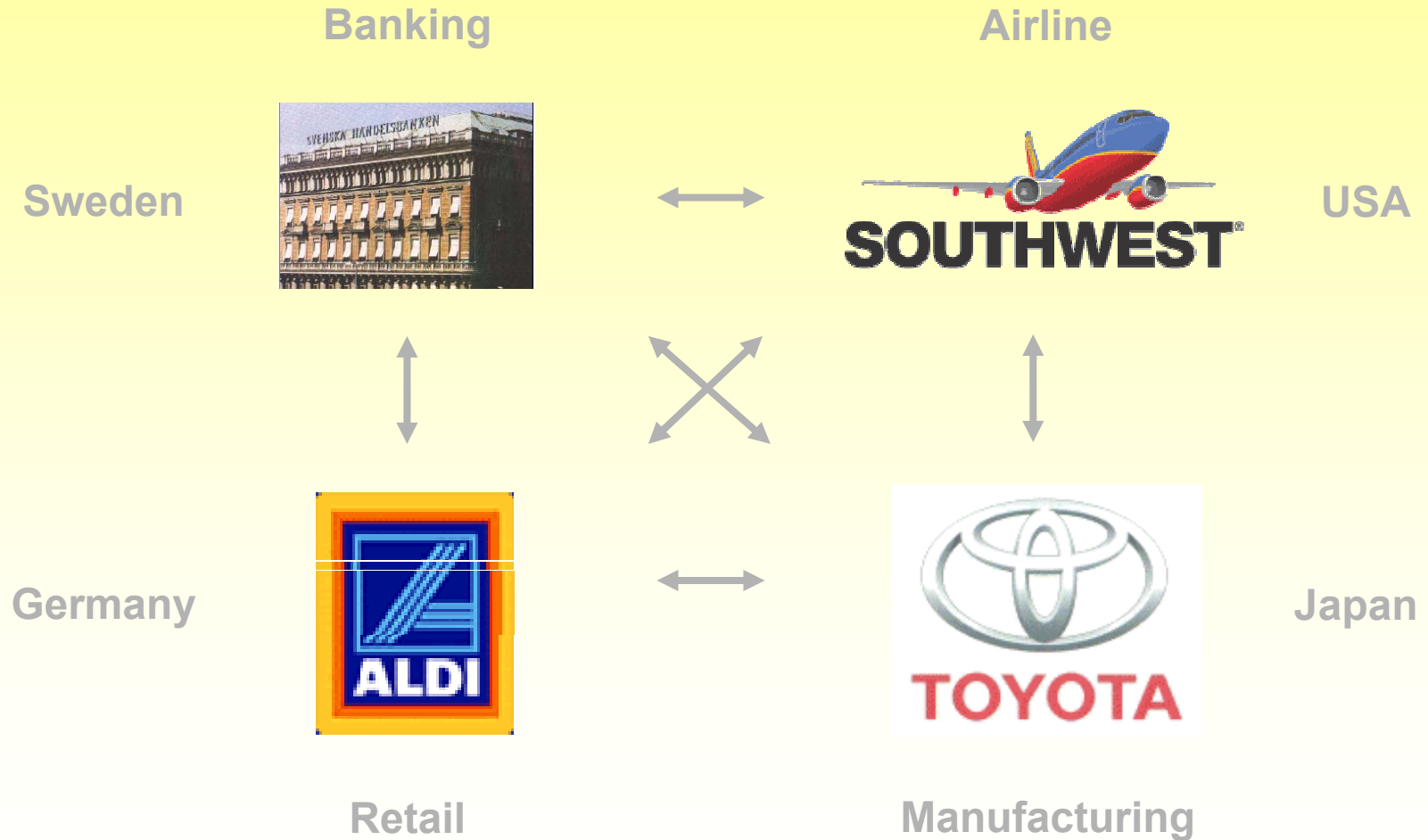
- **Southwest Airlines**, Texas, USA

- **Svenska Handelsbanken**, Sweden, Banking

- **Toyota**, Automotive

- **UBS**, Switzerland, Banking
- **Unilever**, UK/Netherlands, Consumer products
- **Volvo Cars**, Sweden, Car manufacturing

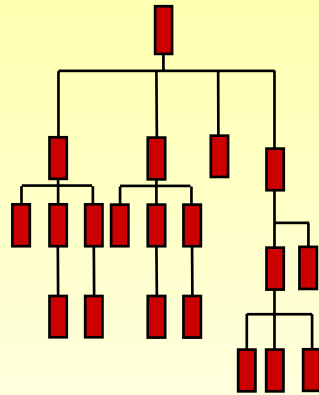
What do they have in common?



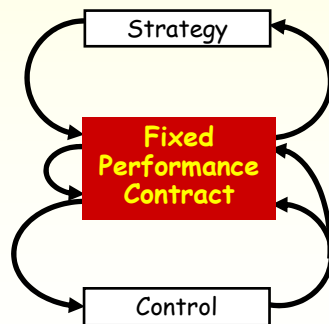
They're decentralized and adaptive

Constrained

'Hierarchical control'

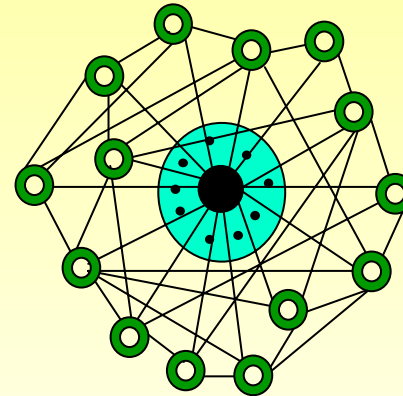


'Fixed process'

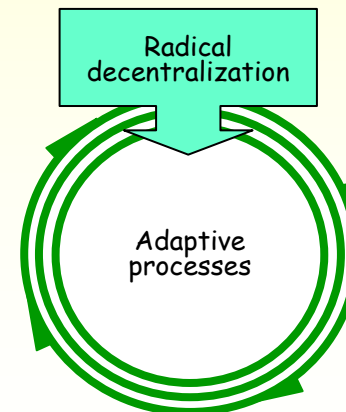


Liberated

'Decentralized network'



'Adaptive processes'



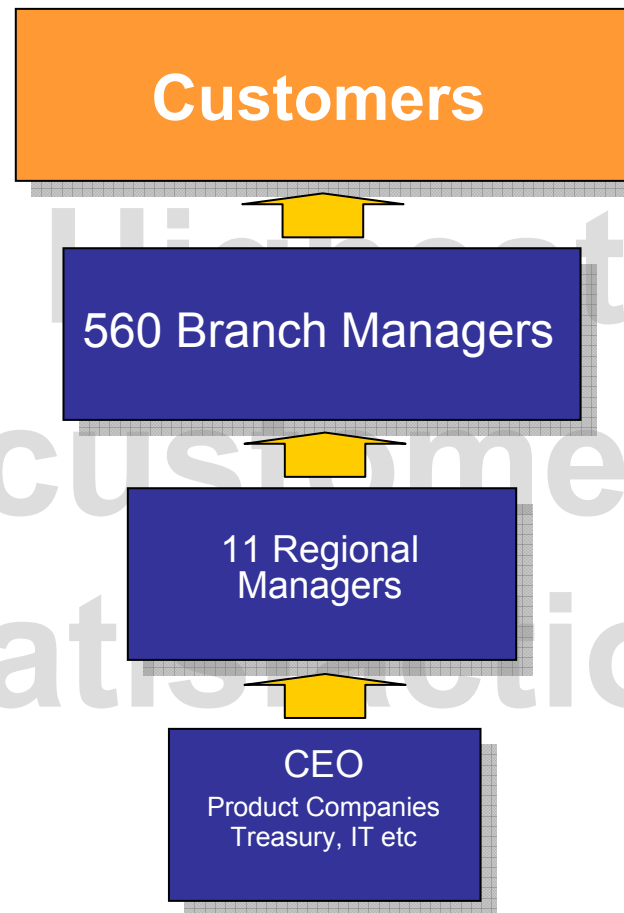
SHB's 'decentralized' network

Principles

Customer responsiveness

Freedom and capability to act

Governance and transparency



SHB's 'adaptive' processes

Principles

Relative goals
and rewards

Continuous planning
and controls

Resources as
needed and dynamic
coordination

Bank to banks

(RoE)

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.
- 8.
- 9.
- 10.

Region to regions

(RoE)

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.
- 8.
- 9.
- 10.

Branch to branches

(Cost/Income etc.)

1.	Branch C	28%
2.	Branch H	32%
3.	Branch A	37%
4.	Branch D	39%
5.	Branch F	41%
6.	Branch E	45%
7.	Branch J	54%
8.	Branch B	65%
9.	Branch I	72%
10.	Branch G	87%

SHB's 'virtuous circle'

Better to do business with

- 4. Customer intimacy** – Highest (independent) customer satisfaction scores in sector year-after-year; lowest customer complaints.
- 3. Operational excellence** – Lowest costs of any bank in Europe; lowest bad debts; cost reduction culture; flat organization (half a head office person per branch versus five for rivals); internal market exerts constant pressure on central services.
- 2. Innovation** – Competitive products and solutions are fed back from branches to product development.

Better for society

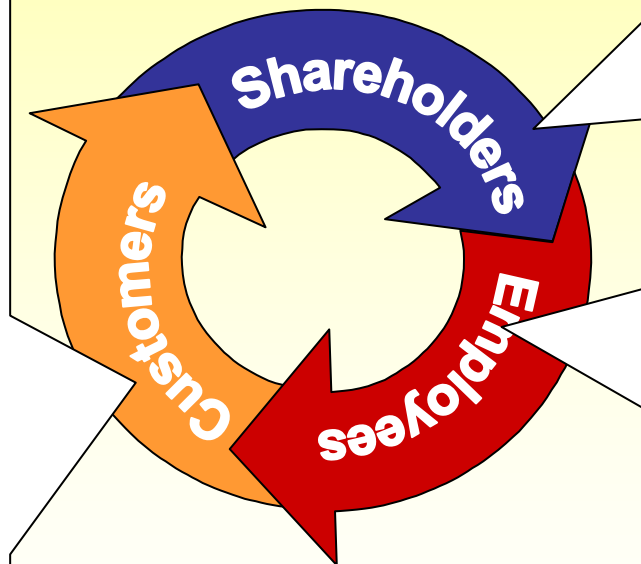
- 5. Ethical & social standards** – Support the long term interests of the bank and society.

Better to invest in

- 6. Sustainable value** – Beats peer group most years on ROE and cost-to-income ratio; highest total shareholder return in sector; devolved adaptive organization is key driver of success.

Better to work for

- 1. Best people** – SHB is first choice financial services company in Sweden for graduates; employee turnover is lowest in sector; challenge, personal responsibility and freedom to run their part of the business; group-wide profit sharing scheme.



Virtuous circle

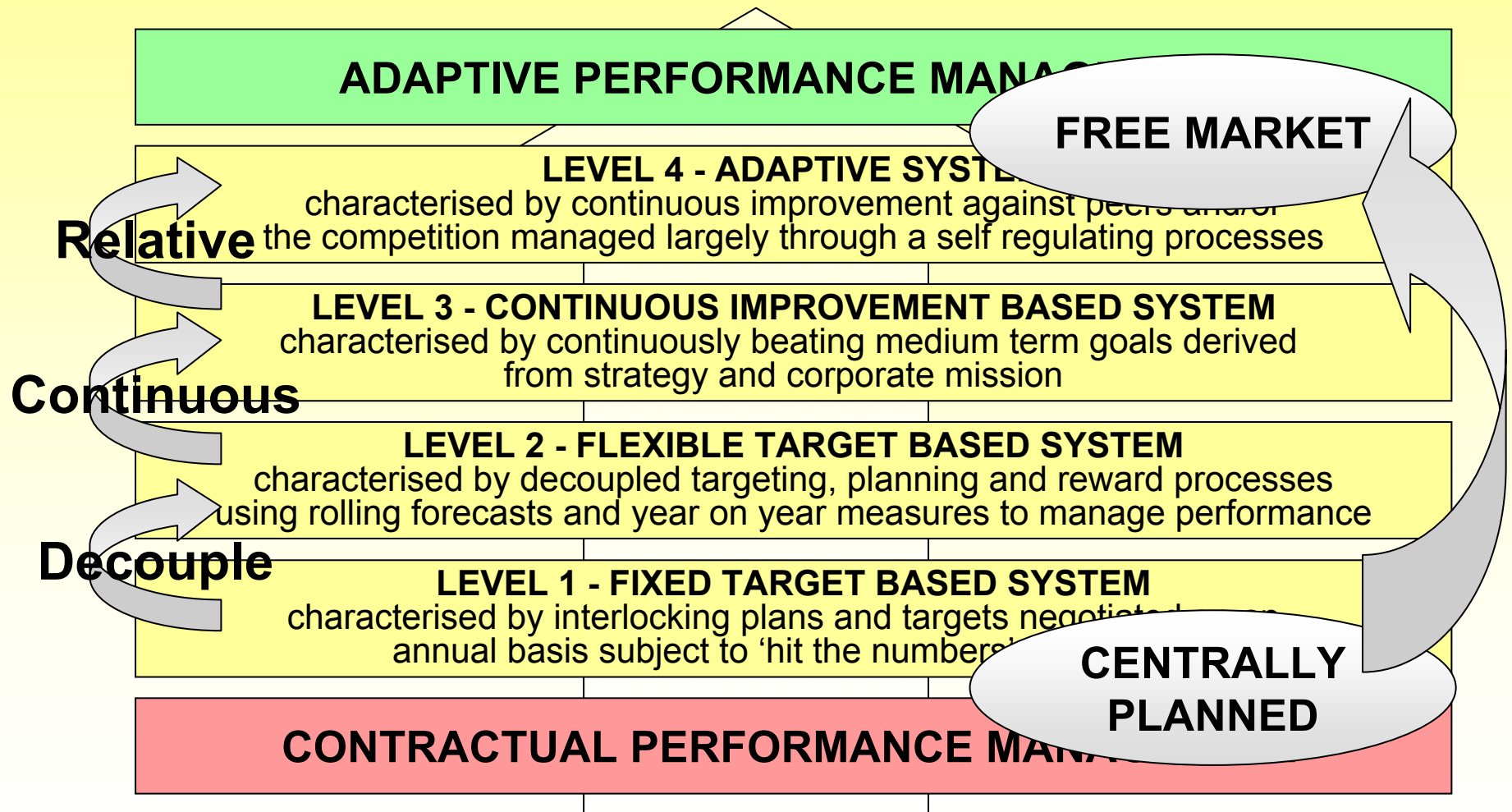
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Major change is 'challenging'!

- Needs CEO/Board approval and sustained commitment
- Change programme must yield 'quick wins'
- Involves changing organization, processes and culture
- Leaders must learn to guide, coach and support
- People must buy in, and acquire new capabilities ... and some managers may feel they will lose power
- It may be *perceived* as weakening control
- Changes are radical, interdependent and take time
- Immediate risks *versus* long term benefits

Is it a 'journey' or a 'giant leap'?



Adapted from material developed by Steve Morlidge, Unilever

The problem with a 'journey'

The model is 'incoherent' for too long a period ... and liable to revert

Principles		Do this!	Not that!
Leadership	1. Customers	Focus everyone on improving customer outcomes	<i>Vertical relationships</i>
	2. Accountability	Create a network of teams accountable for results	<i>Centralized hierarchies</i>
	3. Performance	Champion success as winning in the marketplace	<i>Internal targets</i>
	4. Freedom	Give teams the freedom and capability to act	<i>Adherence to fixed plan</i>
	5. Governance	Base governance on clear goals, values and boundaries	<i>Detailed rules and budgets</i>
	6. Transparency	Promote open and shared information	<i>Restricted to 'need to know'</i>
Processes	7. Goals	Set aspirational goals for continuous relative improvement	<i>Fixed annual targets</i>
	8. Rewards	Reward shared success based on relative performance	<i>Meet fixed targets</i>
	9. Planning	Make planning a continuous and inclusive process	<i>A top-down, annual event</i>
	10. Controls	Base controls on relative performance indicators and trends	<i>Variances against fixed plan</i>
	11. Resources	Make resources available as needed	<i>Annual budget allocations</i>
	12. Coordination	Coordinate cross company interactions dynamically	<i>Annual planning cycles</i>

The problem with a 'giant leap'

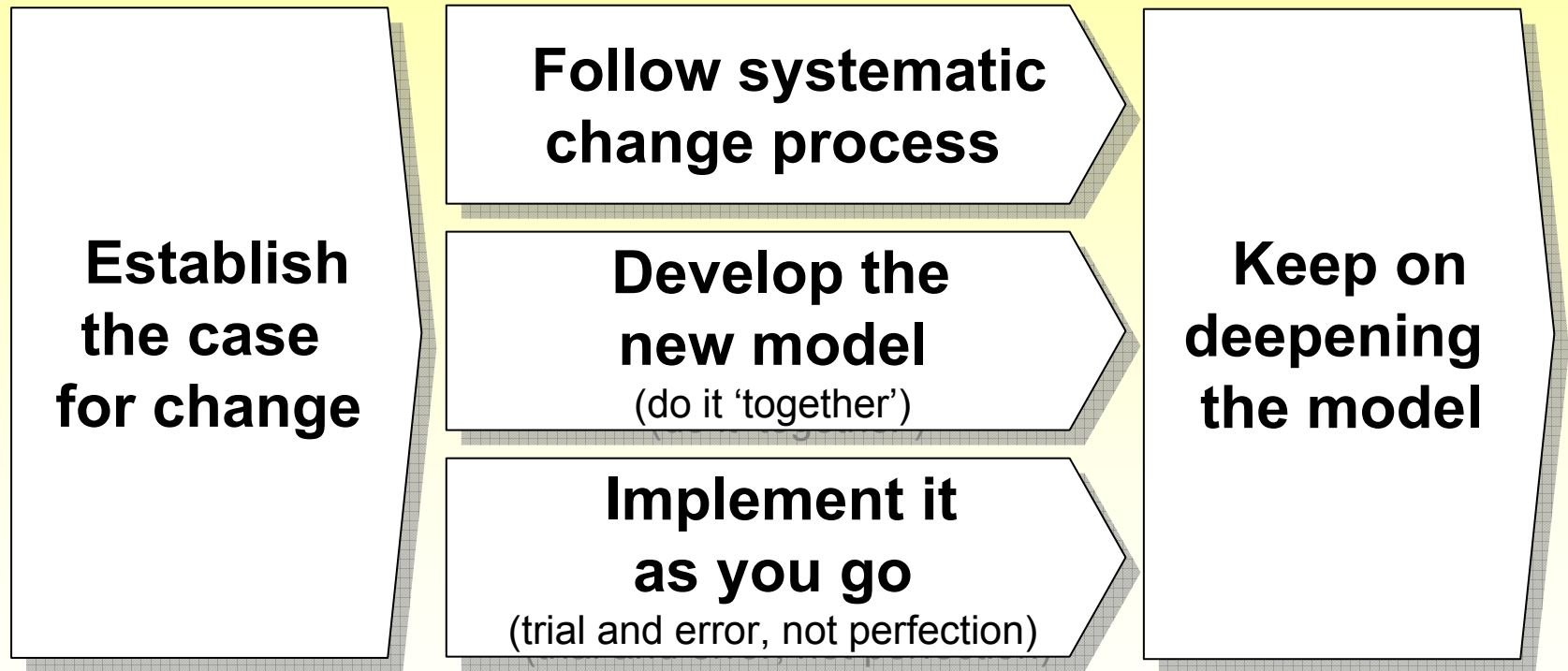
It is impossible to implement all the changes at once ...

We need a 'giant leap' of vision ... and a step-by-step 'journey' towards full implementation by the shortest route.

The top team must provide leadership ... their approach, the 'vision' and 'case for change' are vitally important.

Generic 'liberation' methodology

Every case will be different in its details ...



Months months/years for ever!

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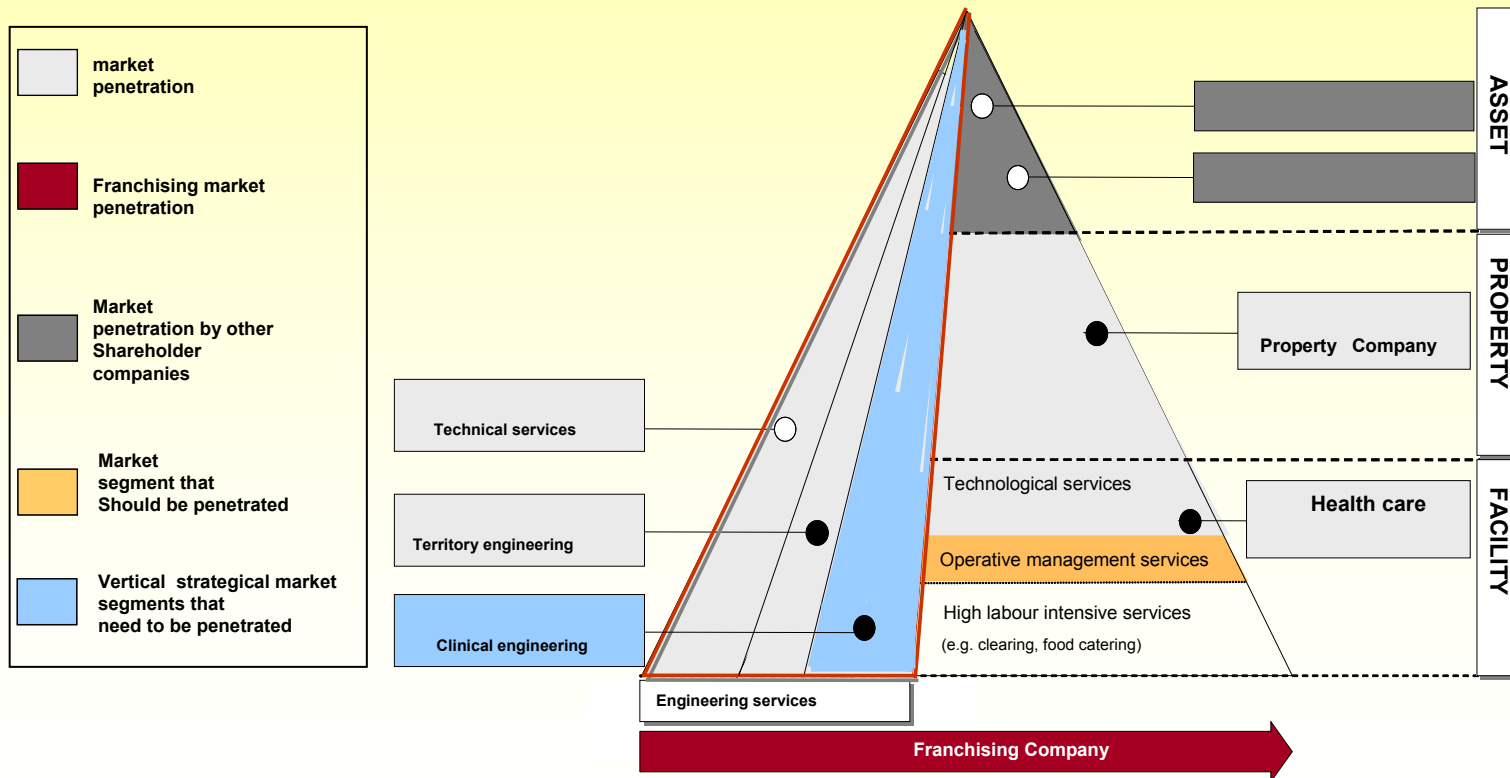
Why this case is interesting!

- Project based, service organization
- Young, dynamic, ambitious, and growing
- Regional, product and industry mix
- Part centralized, and part decentralized
- Aiming to be entrepreneurial, not bureaucratic
- Transformational approach
- Italian, not Nordic culture
- BBRT member in Europe

Our mission and strategy

XYZ

Our mission is to become a full line service provider, seen as the leader in the Real Estate Management field, integrating different competencies (from planning to execution) and delivering innovative services to the final client (public and private).



Our vision for the 'new' model

XYZ

We want “a hundred leaders”, each building more leaders, so that we can fulfil and expand our ambitions.

Why 'decentralized' and 'adaptive'?

- Exploit huge potential market
- Develop local and continuing opportunities
- Respond to competitive and rapidly changing market
- Retain entrepreneurial, *not* bureaucratic culture
- Improve communications and staff motivation
- Reduce costs and improve continuously
- Make the CEO's job 'possible'

Our 'case for change' report

XYZ

1. Our competitive pressures
2. Our strengths and weaknesses
3. Our ambitions and strategies
4. Our vision for management model
5. The guiding principles
6. Our outline design
7. Our implementation approach
8. Resources we require
9. Benefits we expect

How long did 'buy-in' take?

XYZ

In XYZ it took about 12 months ...

- Top management workshops Feb '04
- Meetings with senior managers Jun '04
- Final 'case for change' report: Sep '04
'Shaping XYZ for Success – Together'
- Steering Group (and Board approval) Oct '04
- Guiding Coalition meeting Nov '04

- Group-wide staff workshops Jan '05
- Empowered project teams Feb '05
- Management workshops ... Feb '05

'Guiding Coalition' conclusions

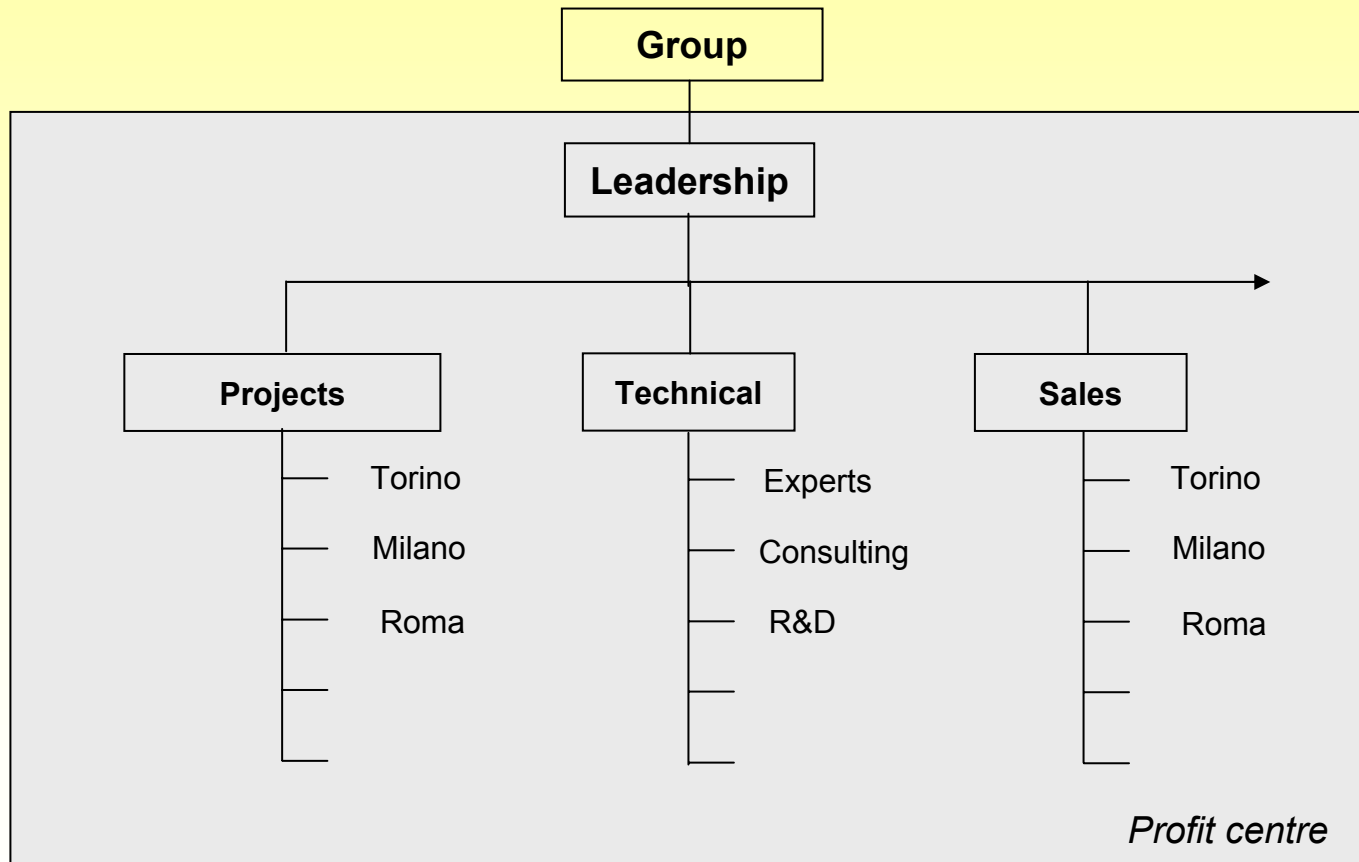
XYZ

- Acquisitions will be merged
- One model for the group
- Entrepreneurial, not bureaucratic
- Decentralized organization
- Adaptive processes
- Reduce overhead/operating costs
- *We will do it 'together'*

Old centralized organization

XYZ

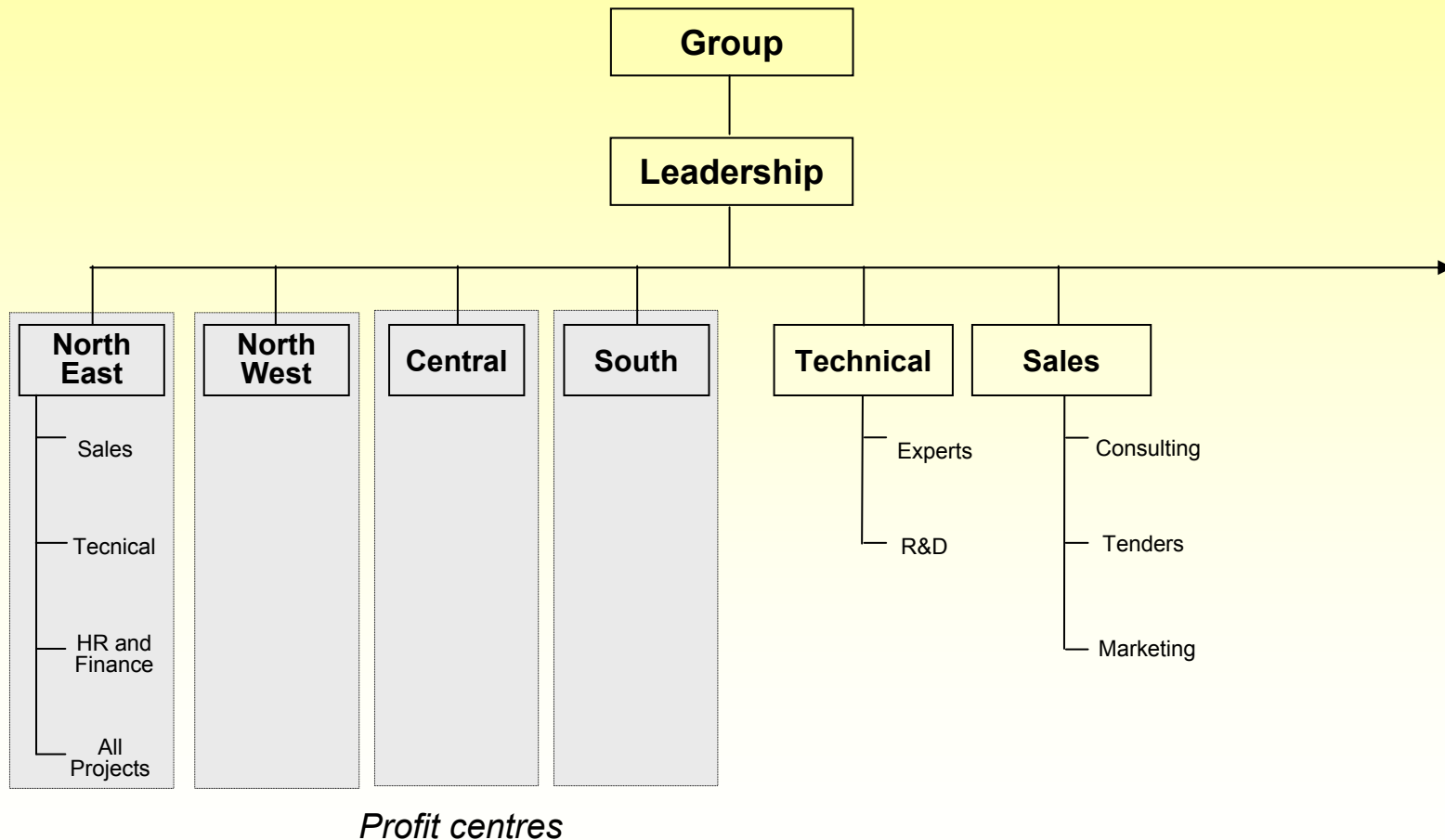
From one profit centre and most things decided centrally ...



New decentralized organization

XYZ

... to multiple profit centres with most things decided locally.

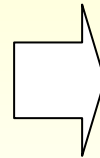


Work flows must change

XYZ

From remote central functions ... to units close to the customer

Business process	
Mission: <i>To complete projects profitably and be paid in full by satisfied customers.</i>	
Start: <i>Customer asks for help</i>	
Main activities	Team
1. Activity	Frontline unit
2. Activity	Central service
3. Activity	Central service
4. Activity	Frontline unit
5. Activity	Frontline unit
6. Activity	Central service
7. Activity	Central service
End : <i>Paid by satisfied customer</i>	



Frontline units
Main activities:
1. Activity
2. Activity
3. Activity

Central services
Main activities:
1. Activity
2. Activity
3. Activity
4. Activity

Relationships must change

XYZ

From hierarchical relationships ... to customer value flow relationships

CUSTOMERS

Regions and projects

To satisfy customers profitably and achieve growth.

Central Services

Support services – To provide support services and expertise to regions at cost (e.g. Sales, Technical, Legal, Payroll, HR).

Central functions – To undertake business sustaining functions (e.g. Corporate marketing, Product development, IT development projects).

Leadership Team

To set and communicate a clear framework of goals, values, policies, boundaries.

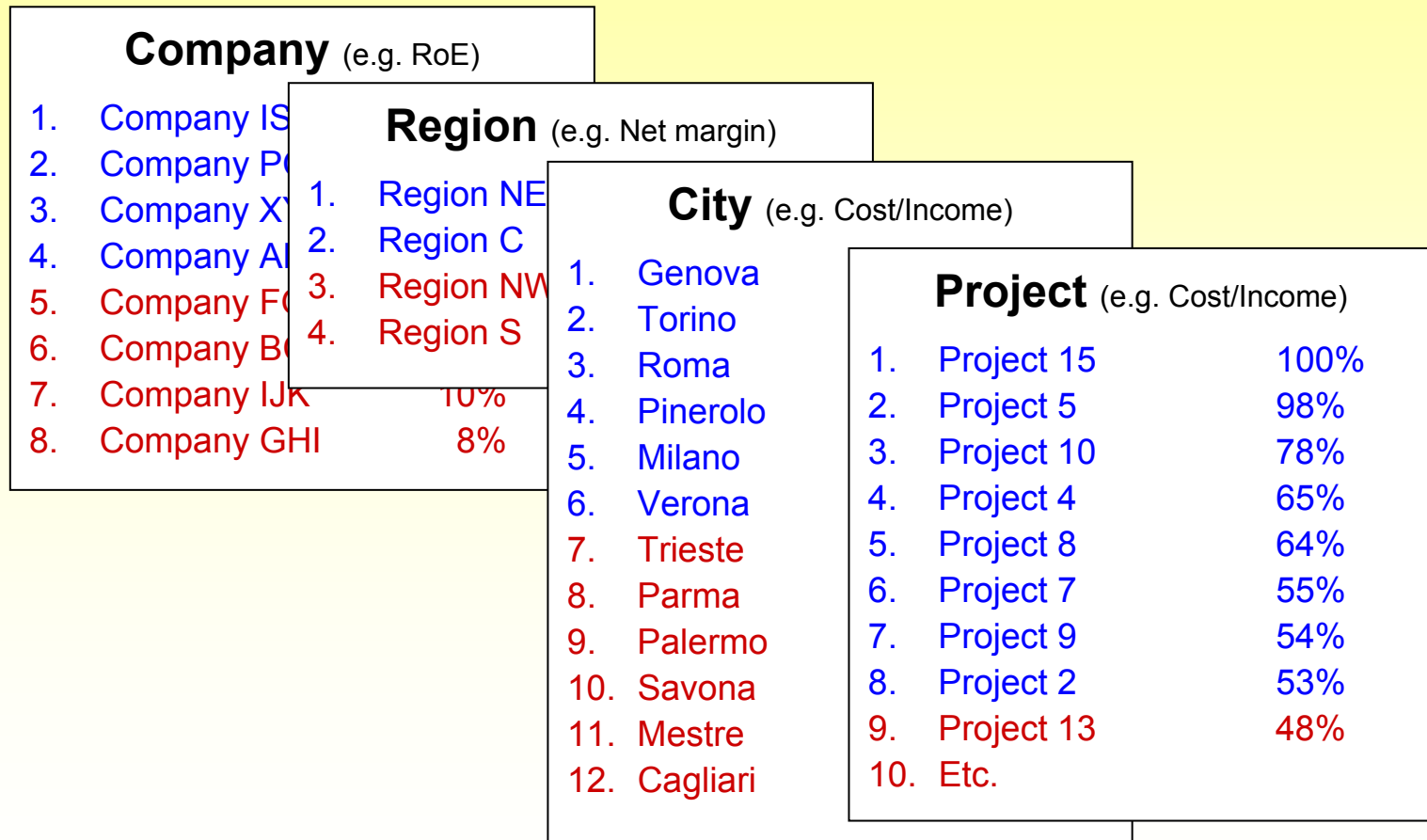
To provide challenge, coaching and support.

To represent the company externally at the highest level.

Governance must change

XYZ

From fixed performance contracts ... to relative improvement contracts



Leading 'major' change *(8-stage process)*

1. Establishing a sense of urgency
2. Creating the guiding coalition
3. Developing a vision and strategy
4. Communicating the change vision
5. Empowering broad-based action
6. Generating short-term wins
7. Consolidating gains and producing more change
8. Anchoring new approaches in the culture

John P. Kotter, *Leading Change*, HBSP 1996

'Budgeting' is NOT the big issue

Issue 1

Yesterday's management model
is in conflict with
today's competitive success factors

Issue 2

The change required is transformational

$$f(D \times V \times S) > R$$

Next step: The 'case for change'

$$f(D \times V \times S) > R$$

Table 9(a) - Your case for change											
Results from sections 2-8 above Scores in lines with asterisk have been inverted (i.e. Scores* = 100 - % reported above)	Your score %	Red Weak 0% - 25%			Amber Moderate 25% - 50%			Yellow Strong 50% - 75%		Green Compelling 75% - 100%	
2. Problems with budgeting process*	8									X	
3. Uncompetitive performance*	24			X							
4. Importance of <u>competitive</u> success factors	92										X
Misalignment of model with CSFs*	45					X					
5. Belief in the vision of <u>adaptive</u> processes Fixed, not adaptive management processes*	45					X					
6. Belief in the vision of <u>decentralized</u> leadership Centralized, not decentralized leadership*	56							X			
7. Belief in vision of <u>supportive</u> PM systems Unsupportive PM systems*	61							X			
8. Readiness to change your management model	75									X	
8. Readiness to change your management model	52						X				
Overall case for change	61							X			

Try (or update) the diagnostic!

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Enter: email address, password etc

Option selection: **‘Beyond Budgeting’ Summit**
(Frankfurt am Main, 8-9 June 2005) ’

Access code: **‘erster’**

Beyond
Budgeting

Towards the 'adaptive' organization

Thank
you

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8-9 June 2005 - Frankfurt am Main