



Strategy Execution: Setting Strategy is Just the Beginning

Table of Contents

Why Don't Good Strategies Lead to Good Results?	3
The Path Toward Advanced Business Planning	4
How Strategy Execution Works	6
The Roads Merge: Integration.....	6
Summary	10
About Hitachi Consulting Corporation.....	11
About Hitachi	11

Every year, companies invest an extraordinary amount of time, money and effort into the creation of the perfect strategic plan. A well-planned road map for success. Yet few companies actually reach their destination.

A recent study of companies with over \$500M in revenue found that more than 66% set targets that exceeded 9% real growth, yet less than **one company in 10** achieved this level of success¹. In fact, of the companies analyzed only 13% were able to achieve 5.5% compound annual growth rates while providing shareholder returns in excess of their cost of capital. Clearly, there is a significant roadblock between the strategic plans these companies develop and the results they achieve.

Why Don't Good Strategies Lead to Good Results?

The performance gap between strategy creation and benefit realization is frequently a company's inability to execute the strategies they define. Larry Bossidy, the former CEO at Allied Signal and Honeywell, and the co-author of *Execution: the Discipline of Getting Things Done*, said it like this: *"Corporate strategies are intellectually simple; their execution is not. The question is, can you execute? That's what differentiates one company from another."*

So what makes this road to strategic execution so precarious? The most commonly identified potential hazards can be grouped into **four** basic categories: Clarification, Communication, Alignment and Measurement.

Clarification

A strategy must be a tangible, relevant statement of business intent, rather than a collection of broad, sweeping statements that force individual interpretation. The strategies often lean heavily on financial outcomes as the destination, without specifying the roadmap of objectives that drive those expected results. For example, a company may claim that they will be #1 and double revenue in five years, without providing any insight into what value proposition, customer segment, geography, product or channel will differentiate them in the marketplace and make these goals a reality. Without clear connections between the drivers, actions, outcomes and rewards, a strategy is irrelevant to the organization as a whole.

Poor clarification of the value proposition, in particular, is not a trivial detour on this journey. The value proposition is the archstone of an organization's overall strategy. The extent to which a company can provide a relevant, differentiated value proposition to its customers not only drives financial performance, it provides valuable insight into the processes, competencies and culture it must cultivate to be successful.

The benefit of creating a clear value proposition is evident at a company like Southwest Airlines: the low-cost, high performing carrier. Southwest uses this concisely stated value proposition to prioritize investment in people, processes and technology, thus delivering optimal value to its customers. At many companies, however, this value proposition is uncertain or unshared, even among executive team members. If a company cannot clearly and crisply define the value it provides internally, it is hard to imagine that value being clear to external customers.

Communication

Even when clearly defined, strategy isn't always effectively communicated. Often, an organization's size and complexity makes communication of even the most concise strategy statements challenging. Establishing a common language for communicating strategy, and enabling that communication at every level is nearly as important as creating the strategy itself.

Alignment

Clear, concise strategies that are effectively communicated still can't drive significant value unless the entire organization understands how their individual actions are strategically aligned. In many cases, strategies are defined at the pinnacle of an organization, with no clear cascade of responsibility for the tactical specifics necessary to achieve results. High-level strategies must be broken down into specific

sub-objectives, which can then be owned and executed at every organizational level.

Measurement

A final obstacle on the road to strategic execution is the inability of most companies to accurately measure true strategic performance. Too many organizations focus measurement efforts on lagging financial outcomes (lag indicators) instead of key drivers of performance (leading indicators). As a result, intangible assets are typically undervalued or not measured at all. These intangible assets can account for 80% of a company’s valuation, and are the key levers to pull when making corrective actions. Examples of intangible assets include management effectiveness, process excellence, brand recognition and innovation. Focus on tangible assets alone, like financial results and budget discrepancies, limits management’s view of performance to past performance alone. To effectively measure past performance and make accurate predictions of future performance a more holistic approach to measurement is necessary.

The Path Toward Advanced Business Planning

A key first step along the path to successful strategy execution is the creation of a concise, but holistic, description of the strategy. One of the most commonly used frameworks for this exercise is the Balanced Scorecard. The approach, developed by Dr. Robert Kaplan and Dr. David Norton, has undergone nearly 15 years of enhancement through academic research and practical application by leading organizations. Part of these enhancements, a tool called a Strategy Map, is one of the most effective mechanisms for developing a clear, crisp roadmap of an organization’s strategic intent.

The Strategy Map is, at the highest level, a model for how an organization creates value. It uses this model as a lens to identify the critical few objectives, measures and initiatives required to drive performance. The Strategy Map incorporates the Balanced Scorecard concept of breaking the strategy down into (typically) four interrelated perspectives: Financial, Customer, Internal Process and Learning & Growth¹¹. The figure (Figure 1) below outlines these perspectives and demonstrates how the objectives in the latter two perspectives (Learning & Growth, Internal Process) drive the outcomes in the former (Customer, Financial).

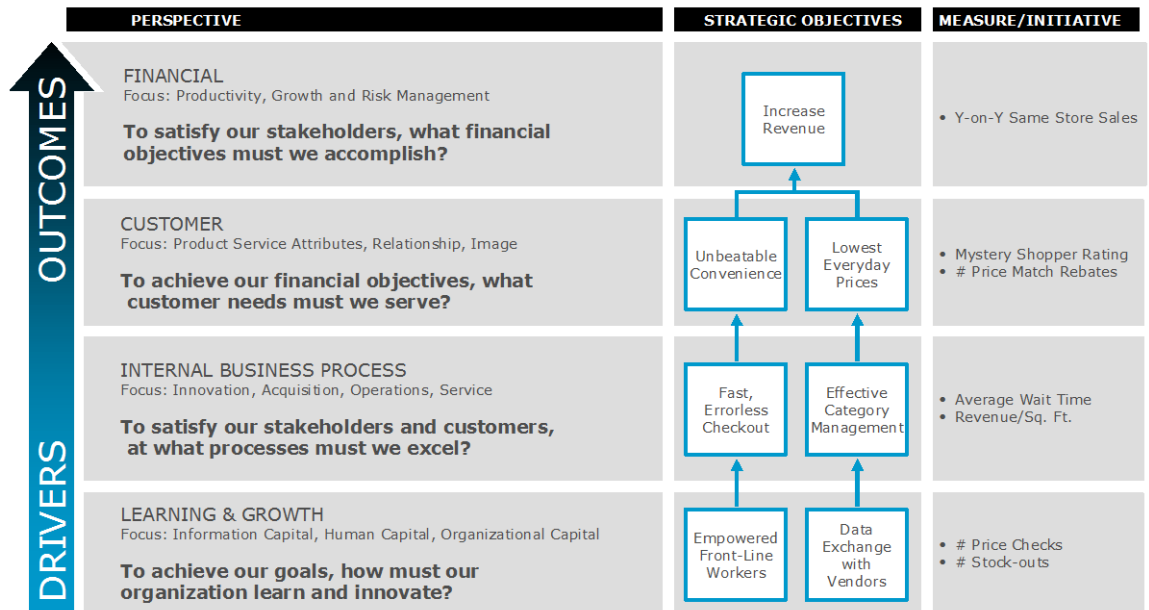


Figure 1

A Strategy Map breaks a company's strategy into constituent parts and puts in place an approach for reporting on not only the company's performance, but also on the overall effectiveness of the company's strategic hypothesis. Companies measure performance on the strategy by evaluating how well they performed against the targets they associated with each objective (the boxes in Figure 1). The Strategy Map also enables executives to measure the accuracy of their strategic hypothesis by gauging how accurately they anticipated the cause and effect relationships between objectives (the arrows in Figure 1). With the key objectives and measures clearly articulated in the Strategy Map, the next step is to link these objectives to the individuals or groups responsible for their achievement and key initiatives that will drive their results.

Once the top-level Strategy Map is complete and communicated, the strategy for the organization should be clearer and more understandable to all stakeholders. The next step in the approach is often to link and align departmental strategy with enterprise strategy via "cascading" strategy maps and scorecards. The goal is to make the measures relevant and actionable for each individual that uses the Strategy Map tool. Ideally this is done in a "top-down" manner, using the enterprise level strategy map and scorecard as a guidepost. As the diagram below (Figure 2) demonstrates, each sub-scorecard should be closely aligned with the superior scorecard, insuring strategic alignment and actionable measures across the organization.

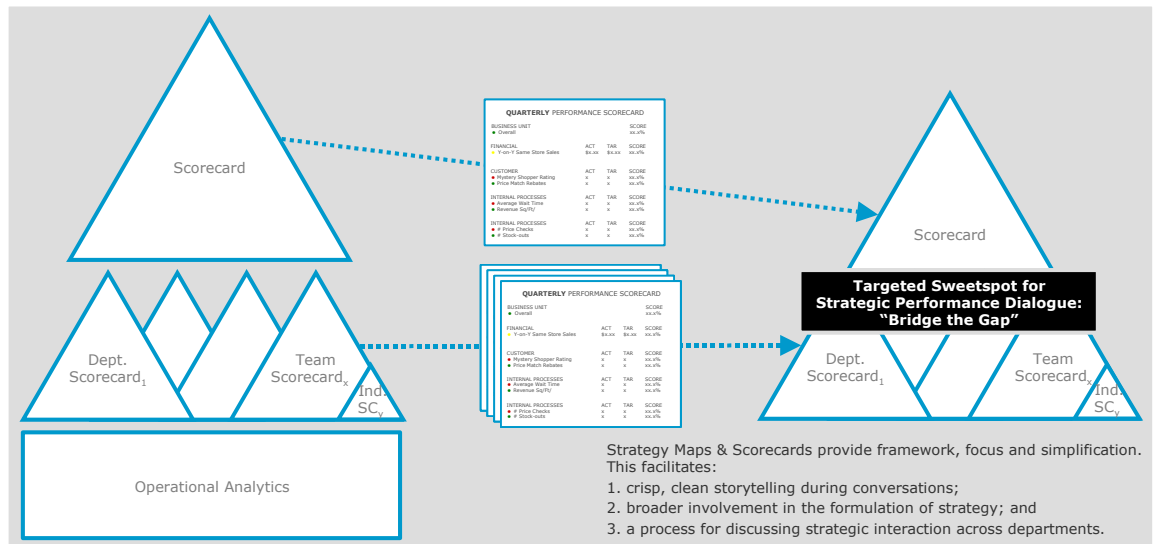


Figure 2

The completed and cascaded Strategy Maps will serve not only as useful clarification tools for defining what is, and what is not, a part of the strategy, it will also serve as a valuable communication tool for educating the entire organization on what executives deem to be important. It should also begin to insure that all parts of the company have a "line-of-sight" between their actions on a daily basis and the company's overall strategy.

Still, the value of these tools will quickly be lost if the process for using them as a critical measurement approach is not addressed. It is the creation of the rhythm of use that begins to engrain strategy into the operation of the company and is the only way to begin to generate lasting value from the Scorecard exercise.

Strategy Maps are a Good First Step

Even companies that implement the scorecard approach, however, often find that they are not achieving their expected levels of benefit. Despite clarifying, communicating, aligning and measuring their strategy; despite linking initiatives that will drive strategy improvement and identifying owners for measures and initiatives...performance may not get better. A study by Bain & Company found

that the Balanced Scorecard was in use by over 60% of 6000+ respondents, making it one of the most popular management tools in use todayⁱⁱⁱ. Yet, as mentioned earlier, only one in 10 companies is successfully creating significant value. What is causing this discrepancy?

Two culprits may be primarily to blame. One possibility is that companies are not implementing the Balanced Scorecard framework as it was intended. The ways to sub-optimize the effort are plentiful: they may not truly be making significant measures non-financial, they may not be identifying cause and effect linkages, they may not be getting management buy-in to the approach, they may not be linking initiatives to the performance objectives, etc. The Balanced Scorecard Collaborative has estimated that half of Scorecard efforts are not implemented in the manner that Kaplan and Norton have proposed^{iv}. Still, that leaves as much as 2/3 of the companies that are using the Balanced Scorecard correctly with approaches that do not provide significant creation of value. So, what is left to be done?

How Strategy Execution Works

The primary reason strategies do not reach their intended destinations, is that companies stop short of creating an integrated approach for strategy execution. The Balanced Scorecard framework is an excellent approach for *clarifying* what is important, for *communicating* what is important, for *aligning* the organization with what is important and for creating a process from *measuring* performance. Simply putting a Scorecard in place (actually, often not so simple), however, is just the first step. If the organization's description of the strategy is not *integrated* with the management rhythms of the business, the link between strategy and tactics will not be complete. The Scorecard is just one component of the full corporate performance management system necessary to not only measure strategy, but also:

- to set strategy;
- to allocate and manage resources in alignment with that strategy;
- to align human capital with the strategy; and
- to generate, organize and distribute the underlying detailed information necessary to make decisions.

The Roads Merge: Integration

By leveraging the Balanced Scorecard approach, organizations can begin to integrate the amalgam of strategic and tactical management processes that typically operate in, at best, a loosely coordinated manner. The figure below (Figure 3) demonstrates how cascading scorecards merge with the broader performance management framework, and provide an example of the management rhythms necessary to engrain and sustain the scorecard effort long term.

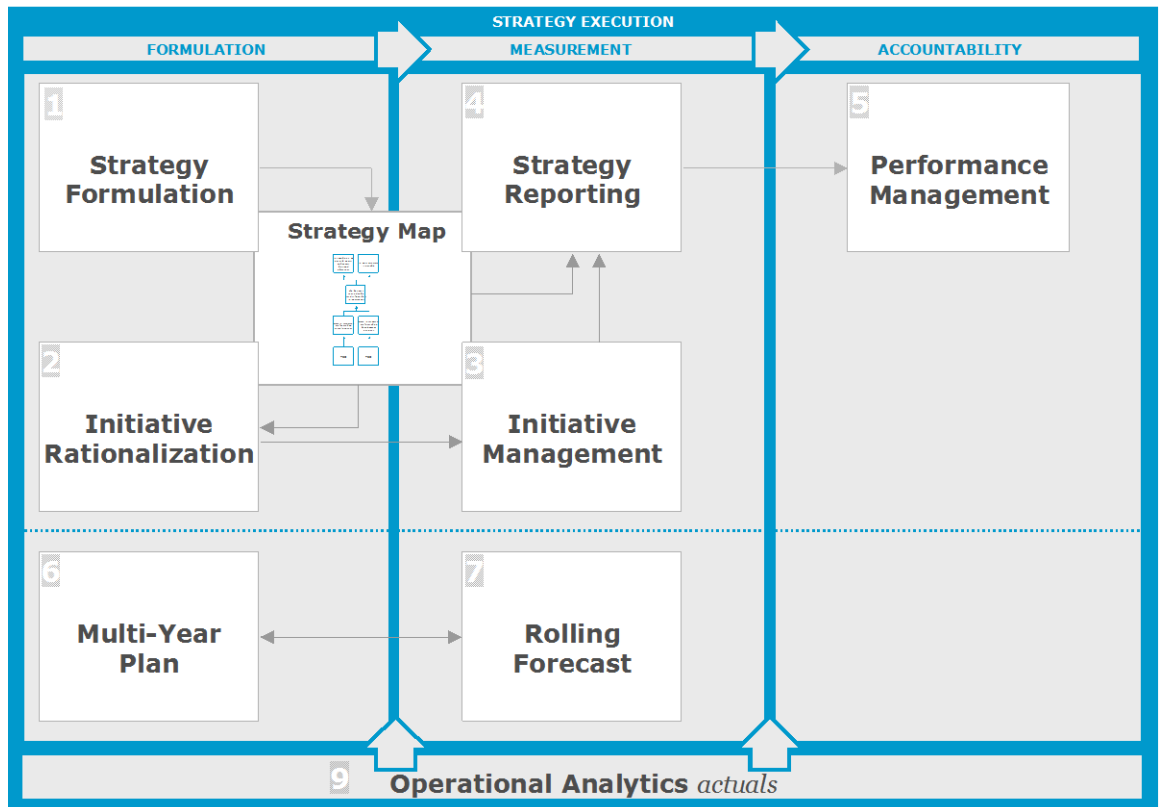


Figure 3

The most successful organizations integrate key processes, establish the recurring rhythms, and implement the tools required to make this system sustainable and agile.

Strategy Formulation

The integration of Strategy Formulation with the actual processes that drive company performance increases the probability of successful strategic execution significantly. However, for true integration to occur, Strategy Formulation must deliver a description of the strategy (often using a Strategy Map) which outlines specific strategic objectives the company believes will produce its desired financial outcomes. These objectives should:

- be balanced across perspectives;
- push the organization beyond status quo;
- be actionable, measurable and concise; and
- expose cause and effect (tying drivers to outcomes).

Knowing that strategy must be clarified for all perspectives (Financial, Customer, Process and Learning & Growth) will help to insure that Strategy Formulation is holistic, rather than simply financial, in nature.

Initiative Rationalization

The Initiative Rationalization exercise is the vetting process that ultimately determines funding. With a Strategy Map in place to provide direction, integrated Initiative Rationalization ensures the projects and programs most critical to strategic execution are appropriately weighted. Funding will not be haphazardly influenced by corporate gamesmanship, political clout or PowerPoint slides detailing lofty intentions to drive returns. For this to work, first, existing and prospective initiatives are inventoried and linked to the Strategy Map objectives they support. Then, the owners of objectives granted supporting initiatives must account for this commitment of resources in the form of more aggressive targets. Objectives with no supporting action items should be flagged for evaluation. It is

unrealistic to expect improved performance without some form of intervention. Best practices include:

- differentiate tactical and baseline from strategic;
- prioritize initiatives on strategic fit and value (e.g. NPV);
- discontinue initiatives lacking strategic linkage;
- adequate funding for initiatives; and
- assign accountability for initiatives

A common problem with predicting and calculating actual value from initiatives is the complexity involved with defining the costs associated with their implementations. Without visibility into how “staff”/salaried resources (e.g. marketing) spend their time, it’s extremely difficult to get a fully burdened P&L for a robust initiative. Activity-based Costing efforts can solve this issue by providing a mechanism for allocating implementation costs in a logical and insightful way.

Initiative Management

Once an initiative is approved, progress must be managed and tracked throughout the course of its development and implementation lifecycle. Organizations often have Program Management Offices to direct this effort, but they don’t always integrate the necessary criteria, including:

- delivery dates;
- scope changes;
- budget issues;
- project risks; and
- milestones.

Once this information is accessible, companies are able to integrate with the Performance Management process by translating how initiative status should affect KPI performance, targets and importance. As initiatives are executed, the corresponding targets need to be adjusted accordingly.

Strategy Reporting

The ability to manage and measure strategy is a fundamental weakness in many organizations, and the reason for the widespread adoption of frameworks like the Balanced Scorecard.

<p><i>KPI Considerations</i></p> <ul style="list-style-type: none">- A KPI makes a strategic objective more explicit, timely and actionable- Every objective should ideally have one or two measures- Balance between leading and lagging measures- Easily understood (complexity is bad)- Generally quantifiable (may be subjective)- Each KPI should have a target goal defined- Target should reflect a “stretch”- Understanding of relative importance (weighting)- Relative targets if possible (benchmark)- Accountability assigned for KPIs/Objectives

The Strategy Map (or Strategy Description), as described earlier, is a very effective tool for documenting and communicating the strategic objectives, metrics, initiatives, accountabilities and targets for the. The most important aspect of Strategy Reporting effort, however, is not the Strategy Map itself; it is how the map is used. The best map in the world does not help a driver that does not know how to read it. Regularly scheduled sessions (preferably monthly or quarterly) to review performance, evaluate strategy, and redirect resources must be created and managed. All stakeholders should understand the following items:

- the participants in the review session;
- the agenda of topics;
- the expectations for participation;
- the process for review and revision of measures and targets; and
- the accountabilities for action.

Performance Management

In many companies, individual and group incentives are focused on subjective evaluation of performance against goals that may or may not be aligned with overall strategy. It has been estimated that only 25% of managers have their personal objectives linked to strategy^v. If personal and group incentives are not aligned with company intentions, driving desired performance is nearly impossible.

For strategy execution to become an organizational strength, clear accountability for strategic objectives/initiatives must be in place to focus and align individuals with organizational goals. The Strategy Reporting “scorecard” that provides overall feedback on the performance of the organization can be leveraged to accomplish this goal. By using the same approach for creating performance objectives for individuals/groups all employees are given personal objectives that are aligned with organizational goals. Key points:

- high level (BU) performance and individual goals must be closely linked
- the focus of performance management shifts to strategic objectives
- cascading of objectives down to the individual level may be appropriate

The individual/group scorecard can easily be derived from the high-level scorecards since accountability has been established up front. Potential changes include the following:

- accountability for metrics that are now directly tied to desired outcomes
- more balance in performance measurement...not just financials
- weighting of KPIs provides relative level of importance guidance

Multi-year Plan and Rolling Forecast

Jack Welch, the ex-CEO of GE has identified budgeting as no less than “the bane of corporate America”. In fact, it has been estimated that as much as 90% of companies are dissatisfied with their budgeting and planning processes^{vi}. The reasons for this dissatisfaction are numerous, but include the following:

- budgets are not strategy driven – the culture of X% over last year prevails
- budgets do not reduce costs – the spend-it-or-lose-it mindset can actually increase costs
- budgets stifle innovation – encourage employees to focus on meeting budget, not driving growth
- budgets prevent responsiveness – only 1 in 5 firms change budgets within a cycle
- budgets are different than planning and forecasting – the business requirements for each exercise are different, the deliverable should be as well

A solution to these problems requires companies to take the, often uncomfortable, step of integrating their budgeting and planning process with the CPM effort. This integration is best accomplished by syncing its timing with the strategy formulation and description processes, allowing strategy, as documented in the Strategy Map/Strategy Description, to define and set stretch targets for both the long- and short-term organizational objectives. Specific best practices for making this integration successful include:

- Scenario Based Modeling
- macro driver assumptions that impact strategy
- KPI (controllable) targets fed from strategy
- driver based Rolling Forecast (4-6 Quarters)
- flexible/relative targets
- tolerance driven by business maturity
- external benchmarks (if possible)

Operational Analytics

The Strategy Reporting scorecard holds strategic-level measures that provide a crisp, concise view of performance. It does not, however, provide the detailed, multidimensional view of information that is necessary to make decisions on what actions must be taken to correct or sustain performance. Coming out of the holiday season, a particularly relevant analogy for the difference between operational analytics and strategic-level measures is a person's weight. Strategy Reporting measures can tell a person that they weigh too much. This is obviously important information to have, but to make a decision on how best to rectify the situation, additional information may need to be collected and analyzed. How long has this person been overweight? Does this person have a medical condition that would make exercise difficult? Are there dietary considerations that should be investigated? The answer to these questions would be solved by the equivalent of operational analytics. The key is to insure that the appropriate information is accessible when needed, and focused on the strategic measures they are intended to support.

Strategy drives the need to understand not only KPI results but also very specific data sets that add context to why hypotheses are proving true or false. The following information should be readily available to support strategic decision-making:

- KPI results for strategy reports and rolling forecast;
- supporting granularity for KPIs (e.g. hierarchical breakdown); and
- contextual information (e.g. segment, geography views).

Summary

Many organizations spend a significant amount of effort and money creating lofty roadmaps for success that, more often than not, doesn't lead the company to its intended destination. The reason companies lose their way is not because they are unable to craft a good strategic roadmap, it is because they don't have the mechanisms in place to keep their car on the road. Tools like the Balanced Scorecard help organizations effectively *clarify* their strategy in a holistic manner, *communicate* the strategy to all stakeholders, *align* all departments behind the strategy, and *measure* strategic performance. Without connecting the Scorecard's roadmap for success to the management processes that steer the business, however, true value creation will still be elusive. Integration of these critical management processes enables companies to effectively execute strategy, to reach their intended destinations. To paraphrase Robert Frost, that can make all the difference.

About Hitachi Consulting Corporation

As Hitachi, Ltd.'s (NYSE: HIT) global consulting company, with operations in the United States, Europe and Asia, Hitachi Consulting is a recognized leader in delivering proven business and IT strategies and solutions to Global 2000 companies across many industries. With a balanced view of strategy, people, process and technology, we work with companies to understand their unique business needs, and to develop and implement practical business strategies and technology solutions. From business strategy development through application deployment, our consultants are committed to helping clients quickly realize measurable business value and achieve sustainable ROI.

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About Hitachi

Hitachi, Ltd., (NYSE: HIT / TSE: 6501), headquartered in Tokyo, Japan, is a leading global electronics company with approximately 390,000 employees worldwide. Fiscal 2007 (ended March 31, 2008) consolidated revenues totaled 11,226 billion yen (\$112.2 billion). The company offers a wide range of systems, products and services in market sectors including information systems, electronic devices, power and industrial systems, consumer products, materials, logistics and financial services. For more information on Hitachi, please visit the company's website at <http://www.hitachi.com>.

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ⁱⁱⁱ Darrell Rigby, *Management Tools 2003*, Bain & Company

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^v Balanced Scorecard Collaborative, *North American Summit*, New Orleans, LA (2003)

^{vi} Jeremy Hope and Robin Fraser, Beyond Budgeting: How Managers Can Break Free from the Annual Performance Trap, Harvard Business School Press (April 2003)

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