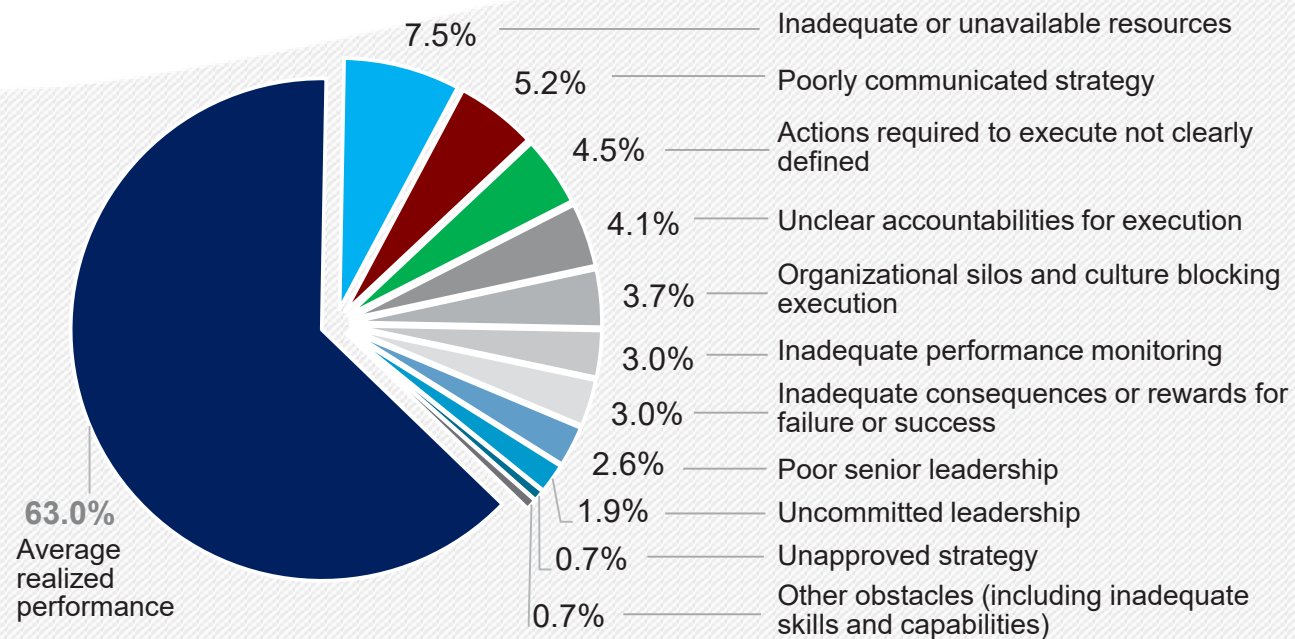


Closing the

STRATEGY-TO- PERFORMANCE GAP

Closing the Strategy-to-Performance Gap



Contents

- **Overview**

- **Root Causes of the Strategy-to-Performance Gap**

- **Rules to Close the Strategy-to-Performance Gap**

This framework explains how to close the Strategy-to-Performance Gap, which equates to an approximate 40% loss in value

Presentation Overview

Most organizations only realize 60% of their strategies' potential value due to issues in strategy development and/or execution. This gap between the strategic plan and actual performance results is known as the Strategy-to-Performance Gap.

This presentation explains the Strategy-to-Performance Gap, its root causes, as well as identifies 7 rules to follow to close this gap. These rules allow an organization to objectively assess any performance shortfall and determine whether it originates from the strategy, the plan, the execution, or its employees' capabilities.

The 7 rules are:

- ① Keep it simple—make it concrete.**
- ② Debate assumptions, not forecasts.**
- ③ Use a rigorous framework—speak a common language.**
- ④ Discuss resource allocation early.**
- ⑤ Clearly identify priorities.**
- ⑥ Continuously monitor performance.**
- ⑦ Reward and develop execution capabilities.**

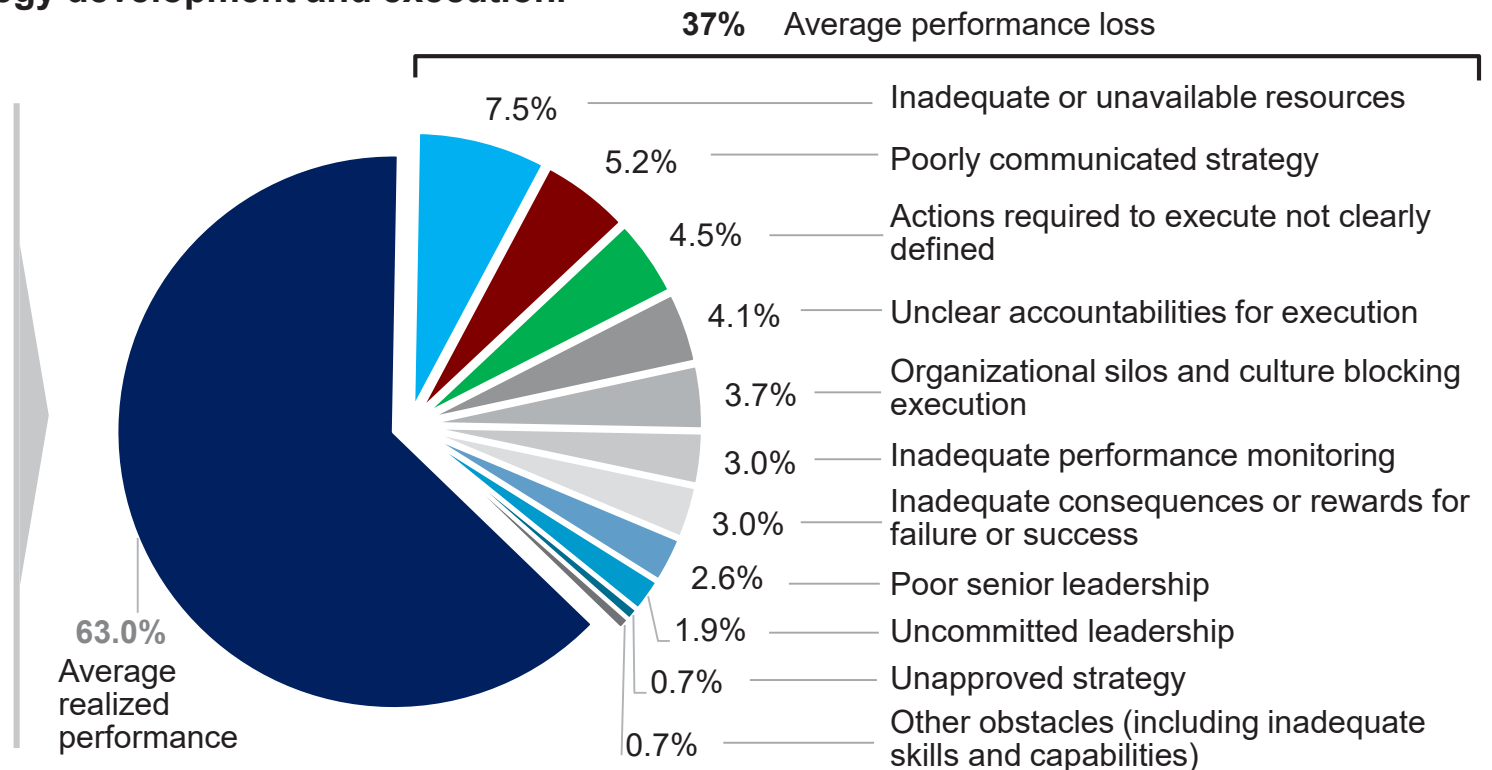
By closing the Strategy-to-Performance Gap, organizations also eventually develop a culture of overperformance.

Organizations typically only realize about 60% of their strategies' value due to issues in strategy development and execution

Sources of Performance Loss

Organizations typically only realize about 60% of their strategies' potential value due to defects and breakdowns in strategy development and execution.

The chart below shows the average performance loss, as determined by the importance ratings in a survey conducted by Marakon Associates of senior executives from 197 companies with sales exceeding \$500MM.



This survey was conducted by Marakon Associates in collaboration with the Economist Intelligence Unit (EIU).

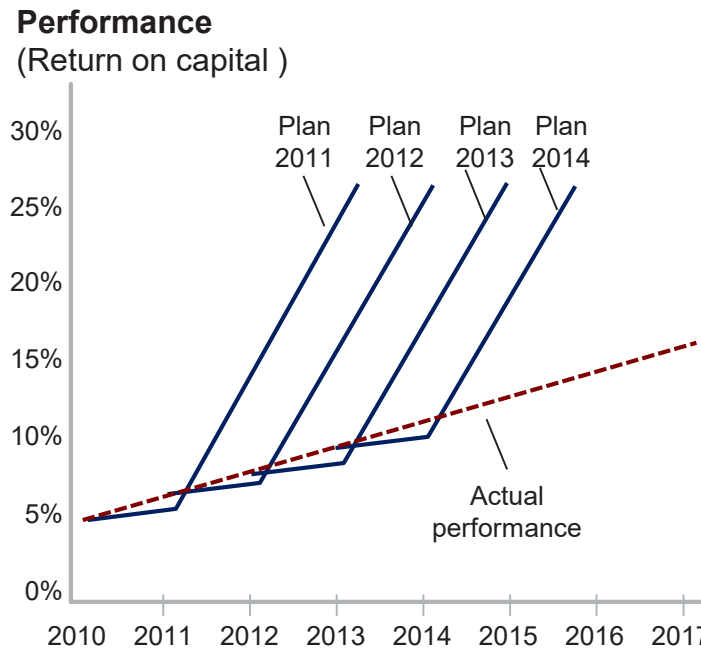
Source: Turning Great Strategy into Great Performance, Makins and Steele, Harvard Business Review, 2005

When each year's performance projections are view side by side, we often see a "venetian blinds" pattern

Venetian Blinds of Business

For most organizations, their projected performance based on strategic planning forecasts follow a "venetian blinds" pattern. In other words, when each year's performance projections are viewed side by side, the resulting diagram resembles a series of diagonal venetian blinds.

At the start of the year, let's say 2017, management approaches a strategic plan that projects modest performance for the first year and high rate of performance for subsequent years. For beating the first year's performance, management is commended for their results. A year later, a new plan is prepared with a similar promising of a slow first year and strong performance for years thereafter.



The actual performance (dotted line) can be seen by joining the start points of each plan. Clearly, the actual performance is much slower than the projected hockey-stick forecasts.

This pattern signifies a deeper issue of an institutional practice of setting unrealistic goals, which has damaging impacts to the organization's culture.

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We've identified 5 root causes to the Strategy-to-Performance Gap

Root Causes of the Strategy-to-Performance Gap

So, what causes the Strategy-to-Performance Gap? It is often difficult to determine whether this gap is driven by poor planning, poor execution, both, or neither. However, 5 specific root causes have been determined that are universally true:

- 1 Organizations Rarely Track Performance against Long-term Plans.**
- 2 Multi-year Results Rarely Meet Projections.**
- 3 A Lot of Value Is Lost in Translation.**
- 4 Performance Bottlenecks Are Frequently Invisible to Top Management.**
- 5 The Strategy-to-Performance Gap Creates a Culture of Underperformance**

Virtually all large organizations struggle with producing accurate financial performance forecasts in long-range plans.

Less than 15% of organizations actually track performance against long-term plans

Cause 1. Organizations Rarely Track Performance against Long-term Plans

1 Organizations Rarely Track Performance against Long-term Plans.

2 Multi-year Results Rarely Meet Projections.

3 A Lot of Value Is Lost in Translation.

4 Performance Bottlenecks Are Frequently Invisible to Top Management.

5 The Strategy-to-Performance Gap Creates a Culture of Underperformance

- This may seem shocking to some—but less than 15% of companies make it an ongoing practice to go back and compare the businesses' actual results with the performance forecast for each business unit in its prior years' strategic plans.
- Therefore, management cannot easily determine whether projections that underlie their capital budgeting and strategic decisions are in any way predictive of actual performance.
- This thus becomes a recurring problem. This disconnect between results and forecasts continues for future capital budgeting decisions.

This is a fundamental reason as to why organizations continue to fund bad strategies and develop better ones.

There is year after year of underperformance relative to plan, which creates a number of issues

Cause 2. Multi-year Results Rarely Meet Projections

- 1 Organizations Rarely Track Performance against Long-term Plans.
- 2 **Multi-year Results Rarely Meet Projections.**
- 3 A Lot of Value Is Lost in Translation.
- 4 Performance Bottlenecks Are Frequently Invisible to Top Management.
- 5 The Strategy-to-Performance Gap Creates a Culture of Underperformance

- This cause refers to the “venetian blinds” phenomenon depicted earlier.
- The clear implication is that there is year after year of underperformance relative to plan.
- This creates a number of related problems:
 - Because financial forecasts are not reliable, management cannot confidently tie capital approval to strategic planning. Consequently, strategy development and resource allocation become decoupled and the annual operating plan or budget ends up driving the organization’s long-term investments and strategy.
 - Since financial forecasts are not reliable, management will not know whether business units are more worth to the company and its shareholders or if they should be divested. Therefore, businesses they reduce shareholder value will remain within the portfolio too long.
 - Incorrect financial forecasts run the risk of damaging an organization’s reputation with analysts and investors. In such situations, the CFO may frequently impose a “contingency” or “safety margin” atop of forecasts produced by consolidating business unit plans.

Poorly performing business units consume valuable capital and other resources that should be allocated to value-creating businesses—thus further reducing growth for the company.

About 40% of value is lost in translation (from plan to action)

Cause 3. A Lot of Value Is Lost in Translation

- 1 Organizations Rarely Track Performance against Long-term Plans.
- 2 Multi-year Results Rarely Meet Projections.
- 3 A Lot of Value Is Lost in Translation.**
- 4 Performance Bottlenecks Are Frequently Invisible to Top Management.
- 5 The Strategy-to-Performance Gap Creates a Culture of Underperformance

- From strategy to execution, almost 40% of the expected value is lost.
- In other words, management starts with a strategy it believes will generate a certain level of financial performance over time. However, failure in execution—largely in improper resource allocation—close to 40% of the value is never realized.
- The primary loss of value is driven by poor communication. This results in the translation of strategy into specific actions and resource plans impossible. Lower levels within the organization thus do not know what they need to do it to realize the strategy and likewise what resources are required to deliver the expected performance targets

Because no one is held responsible for this shortfall, the vicious cycle of underperformance repeats year after year.

Unfortunately, the bottlenecks to performance are usually invisible to management

Cause 4. Performance Bottlenecks Are Frequently Invisible to Top Management

- 1 Organizations Rarely Track Performance against Long-term Plans.
- 2 Multi-year Results Rarely Meet Projections.
- 3 A Lot of Value Is Lost in Translation.
- 4 Performance Bottlenecks Are Frequently Invisible to Top Management.**
- 5 The Strategy-to-Performance Gap Creates a Culture of Underperformance

- Many plans possess overly ambitious performance targets—paradoxically, this makes it easier for management to attribute the performance shortfall to unrealistic performance projections.
- On the other hand, when plans are actually realistic, management has few early warning signals for when performance falls short. Oftentimes, management has no way of knowing whether the critical actions were executed as expected, initiatives were properly resourced, competition responded as predicted, etc.
- Without proper information on how and why performance falls short, it is impossible for management to take necessary correction actions.

Organizations lack the proper processes used in strategic planning, resource allocation, and performance tracking—this makes diagnosing the Strategy-to-Performance gap impossible.

Perhaps the most deadly cause, the Strategy-to-Performance Gap fosters a corporate culture of underperformance

Cause 5. The Strategy-to-Performance Gap Creates a Culture of Underperformance

- 1 Organizations Rarely Track Performance against Long-term Plans.
- 2 Multi-year Results Rarely Meet Projections.
- 3 A Lot of Value Is Lost in Translation.
- 4 Performance Bottlenecks Are Frequently Invisible to Top Management.
- 5 **The Strategy-to-Performance Gap Creates a Culture of Underperformance**

- Oftentimes, unrealistic strategic plans create the expectation throughout the organization that plans simply will not be fulfilled. Thus, plans paradoxically achieve the opposite result as they intend to.
- As this defeatist expectation becomes a reality, it becomes normal and accepted that performance commitments not being met. This leads to a behavior where managers seek to protect themselves from eventual fallout by covering their tracks, rather than spending their energies identifying actions to enhance performance.
- The organization's culture becomes less self-critical and less intellectually honest about its shortcomings—the organization loses its capacity to perform.

This shift to a defeatist, unproductive culture is occurs subtly, but quickly—once it's taken root, it is difficult to reverse.

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To close the Strategy-to-Performance Gap, high performing organizations follow these 7 rules—first, keep it simple and make it concrete

Rules to Close the Strategy-to-Performance Gap (1 of 5)

To minimize and hopefully eliminate the Strategy-to-Performance Gap, we can follow 7 rules. These rules enable us to objectively assess any performance shortfall and determine whether it originates from the strategy, the plan, the execution, or our employees' capabilities.

RULE 1

**Keep it simple—
make it concrete.**

In most organizations, strategy is a highly abstract concept, often misused to be synonymous with vision or aspiration. It is likewise something that's not easily communicated or translated into action. Resultantly, without a link between strategy and performance cannot be drawn, because the strategy itself is not sufficiently coherent and concrete.

On the other hand, high-performing organizations avoid long, drawn-out descriptions of lofty goals. Instead, they utilize clear, succinct language describing their course of action. By being very clear on what the strategy is and isn't, we can keep all employees headed in a unified direction.

A clear strategy also safeguards against value loss from ineffective communication. Accountabilities are also easier to specify.

Rule number 2—debate assumptions, not forecasts

Rules to Close the Strategy-to-Performance Gap (2 of 5)

RULE 2

**Debate assumptions,
not forecasts.**

Developing a business unit's strategic plan can be a very political process, particularly for large organizations. The business unit leadership negotiates for lower near-term profit projections (thus making it easier to reach goals and secure higher annual bonuses). On the other hand, top management pushes for high long-term projections. This leads to the expected hockey-stick projections, with the first year's projections being understated and future years overstated.

Even in organizations where the strategic planning isn't very political, there are often biases built into the financial projections. Oftentimes, the financial forecasting is performed in isolation from the marketing of strategy functions. The short-term assumptions may be realistic, possibly conservative, but long-term assumptions are largely uninformed.

On the contrary, for high-performance organizations, they want their forecasts to drive the work they actually do. To do this, they need to ensure that the assumptions underlying long-term plans reflect both the actual economics of their markets and the performance experience of the company relative to competitors. Thus, projections is a collaborative effort of a cross-functional team comprised of strategy, marketing, and finance folks.

We should use a rigorous framework (e.g. Profit Pools) across the organization—and discuss resource allocation early

Rules to Close the Strategy-to-Performance Gap (3 of 5)

RULE 3

Use a rigorous framework—speak a common language.

To be productive, the dialogue between corporate and the business unit about market assumptions must be conducted within a rigorous framework. An example of a rigorous framework is Profit Pools, developed by Bain.

The specific framework used to ground our strategic planning isn't the most important. What is critical is that the framework establishes a common language for dialogue between corporate and the business units—one that also unifies and the strategy, marketing, and finance teams.

Without such a framework, it is difficult for management to determine whether the financial projections are reasonable and realistic. Thus, management can't know with confidence whether performance shortfall stems from poor execution or a poor plan.

RULE 4

Discuss resource allocation early.

Organizations can develop more realistic forecasts and executable plans if they discuss up front the level and timing of critical resource deployments. Once agreement is reached on resource allocation and timing at the business level, those elements are factored into the organization's multi-year plans.

When we challenge business units on when they require new resources, this channels the dialogue on what actually needs to be happen across the organization in order to execute each business unit's strategy.

Furthermore, an early assessment of resource needs fosters informed discussions around market trends and drivers, thus improving the quality of the strategic plan and make it more executable.

We need to also clearly identify priorities—and continuously monitor performance

Rules to Close the Strategy-to-Performance Gap (4 of 5)

RULE 5

Clearly identify priorities.

Strategy execution is comprised of thousands of tactical decisions. Obviously, not all tactics are equally important. In fact, it only takes a few key actions executed at the right time and right way to hit planned performance.

Organizations must make these priorities explicit, so that each executive has a clear idea where to focus efforts.

Organizations can also have business units define explicit priorities required to realize the performance goals in its strategic plans. Then, each priority is translated into action items with clearly defined accountabilities, timelines, and KPIs.

RULE 6

Continuously monitor performance.

High performing organizations utilize real-time performance tracking. They continuously monitor resource deployment patterns and their results against plans, leveraging continuous feedback to reset planning assumptions and reallocate resources accordingly. This real-time approach allows management to identify and fix flaws in the plan and shortfalls in execution—and to avoid confusing one with the other.

Continual performance monitoring is particularly important in highly volatile industries. In such environments, events outside the organization's control can render a plan useless.

Lastly, we reward and develop execution capabilities—remember, good planning is worthless without good execution

Rules to Close the Strategy-to-Performance Gap (5 of 5)

RULE 7

Reward and develop execution capabilities.

At the end of the day, no plan can be better than the people who actually execute the plan. Organizations should motivate and develop their staffs with this in mind. Likewise, selection and development of management is an essential ingredient to the success of high performing organizations.

Improving the capabilities of the workforce often takes many years. However, once capabilities are built, this can drive superior planning and executions for decades to come. Organizations that strong on execution always also emphasize people development.

Although these rules may appear simple, when strictly and collectively followed, they can transform an organization's strategic planning and execution capabilities.

