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Planning to Win: The Best Way to Predict the Future

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Planning in many organizations today is often more of a mechanical exercise than a value-adding process. But planning should not be about merely forecasting results. Instead, it should be about making results happen. Planning is about driving shareholder value each and every day. © 2005 Wiley Periodicals, Inc.

Can a company systematically create and manage shareholder value? Can it create its own future? And, if so, does this happen by chance or by design? These questions are central to defining what value planning is and what it can accomplish.

If you mistakenly believe that the success of your company hinges on the Fates, the actions of your competitors, and changes beyond your control in the marketplace—in short, that "changes out there" drive your company's results—then business planning is really about *predicting* results rather than *managing* them.

In that case, you could easily draw an analogy between business planning and weather prediction. The objective of both is to predict uncontrollable events and their impacts accurately. The thinking here is that you cannot control market growth, revenue growth, or other critical aspects of your business any more than you can control the weather. For those who believe this, the real need is for rigorous statistical analysis and sophisticated modeling tools.

There are many erudite books and articles on forecasting uncontrollable events, and many thoughtful textbooks on statistical analysis. But the emphasis of this article is not forecasting, because the truly outstanding companies that focus on shareholder value do not believe that their results are driven by uncontrollable factors. Instead they "predict" their future by creating it.

If you believe that your company can create shareholder value in spite of brutal competition and an ever-changing consumer landscape—in other words, that it's possible for an organization to anticipate change and to formulate a winning response to it—then business planning is really about driving shareholder value. The more appropriate term in this case is *value planning.*

VALUE CREATION BY DESIGN, NOT BY CHANCE

How can a company truly drive shareholder value? To illustrate, consider the challenge facing a vice president of operations at a large beverage company when the senior vice president of his division told him that the strategic planning committee had devised a way to achieve consistent earnings growth of 15 percent over the next five years, thus creating significant shareholder value. Even though the company had met considerable challenges in the past and had a remarkable track record, the 15 percent growth target was its most ambitious and aggressive test yet. It would require the absolute best from every corner of the organization, the utmost in commitment, persistence, and leadership.

This goal would require significant sales and revenue growth in a mature market,

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though that was not the main challenge facing the vice president of operations. Somehow, he had to keep costs essentially flat for the next five years—and in the face of rising volumes! This wasn't just a challenging goal; it was a necessity if there was any hope of meeting the 15 percent earnings growth target promised to the board of directors and the Wall Street analysts.

Does this sound like a typical budgeting experience? Probably not. If this were a typical planning session at most companies, the vice president of operations would probably not have been handed such a considerable challenge. Instead, he would be asked to "forecast" his costs for the following year. So he would probably have asked his managers to roll over their previous year's rates for production, materials, and logistics costs and then applied the latest volume assumptions. Perhaps he would have even tried to cushion his plan by tossing in assumptions for inflation or the like. In any event, his "forecast" would have resulted in higher costs and poorer results than those he was actually able to manage.

So how was this vice president of operations able to pull a rabbit out of a hat and achieve five years of flat cost growth in the face of increasing volume growth? He clearly understood what he was responsible for and had the motivation to achieve it. He was then able to align the members of his entire organization in support of his goal and he worked very hard with them to achieve it. Despite the preoccupation with shortcuts in the popular business press, there is no substitute for hard work and dedication to a goal.

The vice president of operations, when handed the goal of keeping costs flat despite increasing volumes, examined what he controlled:

- Plant costs
- Materials costs
- Distribution costs

He then examined the *key value drivers* in each of these areas. For instance, plant costs were driven by productivity, labor costs, and the number and frequency of special orders, to name a few factors. Distribution costs were driven by load factors, freight rates, warehouse utilization rates, and so on. Materials costs were driven by contractual rates of purchased materials. Looking at all these variables, he began to think about how he, and the rest of the organization, could favorably influence them.

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- *The most important element of his success was his own mind-set.* He perceived his own ability to shape outcomes, rather than have those outcomes dictated to him.
- *How different would the outcome have been, for him personally and his organization as a whole, if he had instead focused on why the goal could not be met.* Conventional thinking that rising volumes imply rising costs would have provided him with a case against attempting to meet this goal, but where would that mind-set have led him?

With his management team, the vice president formulated a set of challenges for everyone who reported to him. For example, although the director of purchasing was accustomed to simply passing on rising market prices of raw materials, he was given the challenge of actually reducing purchase prices for key raw materials. This was ultimately achieved through a strategy of leveraging global agreements with a reduced number of supplier "partners." What is interesting to note here is that the director of purchasing accepted the challenge set for him by the vice president of operations (in much the same way that the vice president of operations had accepted the challenge set by the president of the beverage company) and, in much the same way, worked with his organization to set appropriate goals for his managers. Each manager, in turn, devised a strategy to minimize contractual costs for his or her specific ingredients. This well-orchestrated strategy proved very effective, because some previously separate ingredient purchasing was combined to achieve aggressive price reductions. The overarching goal of flat cost growth over a five-year period cascaded down into functional, and eventually into specific, individual commitments.

Completing this illustration, freight costs were driven down by, among other things, new software that maximized load factors. Plant costs, unquestionably the largest and most complex expense area, were reduced by the successful implementation of a worldwide quality initiative. Over the five-

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year period, every plant and operational area was trained in, and eventually excelled in, implementing quality improvements, which greatly increased productivity and reduced costs. This was done not just for the sake of implementing an increasingly popular business program but, rather, to deliver shareholder value by reducing variable costs. The implementation of any initiative—whether a quality initiative, reengineering, or an enterprise-wide software application—was not just paying lip service to the latest business trends. Instead, it was undertaken in order to deliver shareholder value. It was always a means to an end, never an end in itself.

The takeaway from this illustration is that value planning is more about designing commitments and creating the future than it is about "forecasting" some uncontrollable series of outcomes. Despite significant volume growth, the result was five years of flat costs, which contributed heavily to achieving the company's overall goal of 15 percent ongoing earnings growth. It is safe to say that this outstanding achievement would not have been accomplished through a traditional "forecasting" process.

THE VALUE PLANNING APPROACH

Given that a management system exists that can drive shareholder value and "create the future," the next question is how to make this happen. The rest of this article describes the value planning methodology, especially the basic tenets on which it is founded.

Shareholder value, which should be the aim of any business organization, is driven by people who are accountable, motivated, and knowledgeable. A closer look reveals why this is true.

People must clearly understand what results they are accountable for. When people clearly understand what they are accountable for, they can focus their time and energy appropriately to achieve desired results. But if accountability is obfuscated, as it so often is in large organizations, people's energies and efforts can easily become misdirected, and their personal goals can become confused. Without clear accountability, people focus on the wrong things, such as interdepartmental rivalries.

Accountability is greatly leveraged through appropriate motivation.

In the illustration discussed earlier, the vice president of operations had very clear accountability for delivering a challenging shareholder value result—five years of flat cost growth. He, in turn, was able to define supporting accountabilities for his purchasing, manufacturing, and logistics directors. These responsibilities cascaded down into focused individual responsibilities and accountabilities that drove the ultimate success of the organization in achieving what could have been viewed as an "impossible" goal.

Accountability is greatly leveraged through appropriate motivation. One of the reasons that clear accountability was so effective in the illustration is that personal success (compensation promotions, status, and so on) in that company was directly tied to achieving accountable results. People generally act in their own economic best interests. To the extent that their economic best interests are tied to achieving clearly defined results, those results will be achieved if they are at all possible.

For any of us to be successful in what we do, we need to be knowledgeable. It goes without saying that we must have the requisite background, training, and general knowledge to do our jobs. All that is by way of preparation, but when we put such preparation to work, our ongoing need is for data and information. If we are responsible for marketing a product, we need up-to-date market data, reliable sales trends, and so on. If we are responsible for plant costs, we need data concerning productivity, line speeds, and so on. No matter what we are responsible for, the foundation of knowledge is accurate, timely, and reliable data.

The umbrella term *knowledge* also refers to the process by which we learn and constantly build upon our understanding, which gets to the heart of why data integrity is so essential. The process of increasing our knowledge (and, therefore, our potential effectiveness) can be broken down into three basic elements:

1. Understanding of our current environment;
2. An intentional change to the current environment; and
3. Observation of the response.

These elements hold true whether we are in manufacturing, marketing/sales, engineering, or human resources. It is easy to see why having accurate, timely, and reliable data at each

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stage is so critical. If a person's understanding of the current situation is based on inaccurate or incomplete data, all of the decisions that follow are at risk. Likewise, if a person's assumption about what the intentional change should be (e.g., an 8 percent increase in net wholesale prices after trade allowances across all regions) is different from what is actually executed (e.g., a range of increases from 3 to 11 percent across regions), then that person's conclusions will be at risk. Finally, if the data reviewed on the response to the change are inaccurate or just incomplete, then the decision to keep or discard the change will be at risk. However, if the data a person has available at each stage are accurate, timely, and reliable, then that person can apply his or her education and background to make effective decisions.

Everyone has a new job description in this New World—a world in which everyone is responsible for creating shareholder value. Whether a person's responsibilities include running a research program, taking customer orders on the phone, or developing new advertising campaigns, that person is there to create shareholder value. The way he or she creates shareholder value may be different from one job to the next, but all share the same fundamental purpose. The term *value maker* recognizes the pivotal role of the individual in creating shareholder value.

Before moving on to the central issues of value planning, it is worth reviewing the underlying assumption of this article—namely, that *shareholder value is driven by people who are accountable, motivated, and knowledgeable.*

Given that underlying assumption, there are three bedrock fundamentals that must be in place if value planning is to succeed. Unfortunately, they tend to be glossed over for a variety of reasons. In order for value planning to be effective, a company must have:

1. Unambiguous accountability/responsibility at every level in the organization;
2. Vigorous linkage of compensation to performance; and
3. Indisputable data integrity.

On the surface, none of these might appear to be a challenge—which is one of the reasons they can be overlooked. Remember that these three elements are essential to achieving effective value planning. The effectiveness of value planning is in direct proportion to the degree to which these issues are addressed. No extent of systems implementation, rigorous reporting requirements, or frequency of updates will have any meaningful impact unless these three bedrock issues are addressed.

...shareholder value is driven by people who are accountable, motivated, and knowledgeable.

Apart from these three fundamental issues, there are four *leverage* issues. They are separated in this manner to stress that addressing the core issues is an absolute prerequisite to having an effective value planning process, whereas the four issues that follow can significantly leverage the foundation laid. The full and complete benefits of value planning can be realized when:

1. Finance is structured to vitally support value planning;
2. Ownership is embraced by those who have committed to delivering results—the Finance function is therefore recognized as the facilitator, but not the owner, of value planning;
3. Priorities are made compelling and clear; and
4. Value planning is incorporated as a management tool throughout the organization.

Each of these leverage issues, if properly understood and addressed, can yield remarkable results, especially if addressed in concert.

VALUE PLANNING IS A MANAGEMENT SYSTEM, NOT A PROCESS

The focus of most traditional planning approaches is on the process itself. Typically, the issues that are addressed are how long the process takes (cycle time), how many people are involved, how many versions of the annual plan the organization develops, and so on. The goals for improvement are commonly reduction in cycle time, reduced keying of data, fewer people involved in the process, and fewer iterations. There are potential benefits to all of these, but they barely scratch the surface of the transformation that is possible when planning is viewed as a management system.

Value planning is not about generating reports faster or reducing the number of full-time equivalent employees (FTEs) involved in the process. Value planning is about a management system to increase

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shareholder value. The appropriate performance measure focuses on the *results* of the approach: improved decision making. Although measuring cycle times and process costs may be appropriate in looking at the process of producing the payroll every month, it is wholly inadequate and unintentionally misleading in assessing a management system to drive shareholder value.

There is also a caveat of importance. Implementing an effective value planning infrastructure can be one of the hardest things a company ever does. Whenever an organization shines a spotlight on performance—whenever it brings people out of the relative safety of their offices and holds them visibly accountable for achieving results, whenever it decrees that "good enough is no longer good enough" and builds an infrastructure to enforce it, it faces a demanding challenge, and only disciplined leadership can make it happen.

Ultimately, value planning should be based on a hard-nosed management system that requires leadership and hard work at every level of the organization. If the true objective is to make results happen—to drive shareholder value—then that is precisely what is required.

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