# Addressing strategy management and the balanced scorecard

Part: 1

# Introduction: The strategy gap

Most organisations recognise that there is a significant gap between their strategic plans and their ability to execute. Part of the reason for this was shown in a survey conducted by CFO Research Services where 60 percent of organisations said they were dissatisfied in the alignment between strategy and budgets.1 This alignment is vital because the budget is often the only enterprise-wide process where users are directed and controlled in their use of company assets to achieve organisational objectives.

But why is this alignment so hard? In the book Competing for the Future, this disconnect was summed up in the statement:

> In too many companies there is a grand, and overly vague, long-term goal on one hand…and detailed short-term budgets and annual plans on the other hand…with nothing in between to link the two together…The long term doesn't start at year five of the current strategic plan. It starts right now!

Today, most organisations rely on the budget process to bridge the gap. Managers are told the results that are required for next year and in turn they develop a revenue/cost budget to achieve them. But this process is usually devoid of anything to do with strategy, providing little direction as to how strategies are to be achieved, little analysis as to whether budgeting activities make sense given the current overall strategic plan, and little thought for conflicts between activities and resource allocation. Instead, the "how" of strategy management is either assumed or, worse still, worked out as the year progresses and failure looms.

Which brings us to the other issue: How do we monitor the plan? Most management reports offer little or no real value in monitoring plans. Consider Figure 1, for example. While this report is great for telling an organisation what happened, in terms of managing performance this report has significant challenges. This report:

- Shows no relationship to the actions that produced the results. For example, we can see that revenue for the month was over budget but we have no idea why. Even if we were able to break this figure down into products and customers, it still doesn't tell us what actions took place that resulted in the reported performance.
- Provides little or no information of what needs to happen in the future. The report shows that, year-to-date, we are behind the goal for revenue. What it doesn't tell us is what needs to change in order for us to meet the year end goal.

| Last year | This Year - Month | | | | This Year - YTD | | |
|---|---|---|---|---|---|---|---|
| **Actual** | **Budget** | **Actual** | **Variance** | | **Budget** | **Actual** | **Variance** |
| 25,000 | 27,000 | 27,500 | 500 | **Revenue** | 320,000 | 315,000 | {5,000} |
| 6,250 | 6,750 | 6,857 | {125} | **Materials** | 80,000 | 78,750 | 1,250 |
| 5,750 | 6,210 | 6,325 | {115} | **Production Costs** | 73,600 | 72,450 | 1,150 |
| 2,500 | 2,700 | 2,750 | {50} | **Marketing** | 32,000 | 31,500 | 500 |
| 4,500 | 4,860 | 4,950 | {90} | **Sales** | 57,600 | 56,700 | 900 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **6,000** | **6,480** | **6,600** | **{120}** | **Gross Contribution** | **76,800** | **75,600** | **1,200** |
| 5,750 | 5,210 | 6,325 | {115} | **Head Office Allocation** | 73,600 | 72,450 | 1,150 |
| **250** | **270** | **275** | **{5}** | **Net Contribution** | **3,200** | **3,150** | **50** |

Figure 1. Standard management report.

- Is an accounting-based view and not directly related to operational managers' daily activities/responsibilities. Managers direct and control activities and it's these activities that ultimately determine whether organisational goals are met. Most financial statements are the results of activities that took place in the past—they are not the activities themselves.
- Provides no context on what's happening in the "real world." Budgets are usually the results of negotiations that took place many, many months in the past. Assuming (and this is a big assumption) that budget managers set these budgets based on the prevailing economic environment, if that environment changes, for example a competitor releases a much improved product/service, then the budget assumptions are no longer valid. Beating a budget that was unrealistic to begin with does not help, in the slightest, an organisation who wants to beat the market.
- Does not tell us if strategy was successful. There is no way of knowing from this report what the strategy of the company was, whether it was actually implemented and if the results reflected that implementation. Without this feedback, managers can delude themselves over the causes of success or failure. The question facing managers is this: How do we bridge the gap between strategy and execution?

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