**Innovation in Action Series**
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# Dynamic planning for today's uncertain world

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**Information Management**

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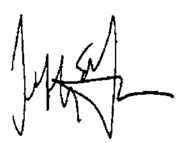
*The planning process as most of us have known it is a complicated pain in the neck, largely ineffective, and mostly irrelevant. Companies need a new approach to planning that offers simple methods for setting performance targets and for developing action steps to move the business ahead – an approach that's centered on tactics rather than numbers.*

*This is the third in a series of six articles seeking to establish a new agenda for finance. In the first, David Axson and Greg Hackett make a case for change, providing a wake-up call to today's finance leaders. The second describes the new vision in greater detail. This article discusses transforming the planning process to make it simple, flexible, short, and relevant to today's dynamic business environment.*

*David Axson and Greg Hackett are advisors to the Innovation Center. They also are unflinching advocates for innovation in business management practices. Both question the effectiveness of the status quo and urge companies toward better ways of doing business.*

*Subsequent articles will elaborate on other elements of the vision and describe an implementation road map. Read on as David and Greg make the case for committing more than a passing glance at the future, especially when the competition is consumed by the past.*



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### Planning presently is a pain

In the typical company today, annual planning is a very painful, highly distracting, four- to six-month forced march fraught with tremendous political perils and pressures. Plans are weighed down with excessive detail having little bearing on an organization's forward progress. Further, plans are overly focused on internal factors, ignoring important external influences. The process takes an exceedingly long time, it wears people out, and its end-product lacks accountability, ownership, and flexibility.

The outcome is a static tool, obsolete from its conception. The longer it takes, the more likely it is to be wrong, and managers spend the next 12 months explaining how and why their results don't match the plan—and accounting for variances over which they have little or no control.

Annual planning is ineffective, and people hate it. But despite perceiving its value to be dreadfully limited, most managers are reluctant to give up on the process. It may be inadequate, but they can't conjure up a better alternative. So they make believe that annual planning is useful and necessary.

But vanguard managers are suspecting that planning in their organizations is becoming an impediment: Planning is so poor that they are becoming afraid of making bad decisions because of it. And today's markets are too unpredictable and volatile to allow any highly detailed, longer-term plan to serve as an effective guide to resource allocation, let alone decision-making.

The annual plan as the tool is known today evolved in the 1930s and '40s from the approaches of Alfred P. Sloan at General Motors Corporation. Numbers-based, detailed plans were developed to a degree of precision that served organizations well in stable, manufacturing-oriented businesses where the challenge was to keep up with ever-increasing demand. The approach is outdated and is neither relevant, realistic, nor especially helpful in an increasingly unpredictable business world. Far worse is managers' reluctance to abandon an old-style planning process that causes companies to continue on courses known to be flawed, doing irreparable harm to performance and stockholder value.

Instead, what companies need are simple methods for setting performance targets that chart progress toward organizational goals, for developing action steps that aggressively move the business forward, for agreeing upon performance metrics, and for building shared commitment to performance. Companies need a new planning approach that is centered upon tactics rather than numbers and budgets. Plans should focus on what needs to be accomplished and how it will be achieved, while embracing risk and uncertainty. Any numbers should be results extracted from the tactics—in effect, the budget is only a financial representation of the tactical plan. Plans would be completed in weeks, not months, and could be updated on demand within a few days in response to events or opportunities.

But to achieve such an approach, the entire annual planning process as corporations know it today must be gutted.

There are three fundamental changes required to eviscerate and re-establish the typical corporate planning process so it can assume its rightful position as the most-valued, rather than most-loathed, management process. First, action begins at the top, rather than the bottom of the organization. Second, tactics replace budgets. Third, planning and the resulting decisions become continuous, rather than static.

### Action starts at the top

In this new planning vision, action commences from the top, rather than the bottom, where it typically starts today. Bottom-up planning and budgeting has long been defended as a means to secure broad organizational commitment to action; the reality is that this serves merely to encourage pandemic conservatism and "sandbagging." Managers seek to negotiate the most advantageous performance contract for themselves and their organizations, rather than define actions that will result in superior corporate performance.

In the new vision, an organization's performance management system automatically generates a baseline business plan predicated upon recent actual results—a picture of the current situation that is immune to politics and self-interest. (See Exhibit 1.) This baseline assumes that a company will continue to execute as it does today and shows what this looks like numerically. The baseline offers reliable information that assists managers in understanding drivers of the business and interrelationships within the business. From this baseline, managers are able to model and predict the effects that different scenarios—such as a five-percent growth in sales or a spike in energy costs—could have throughout the company.

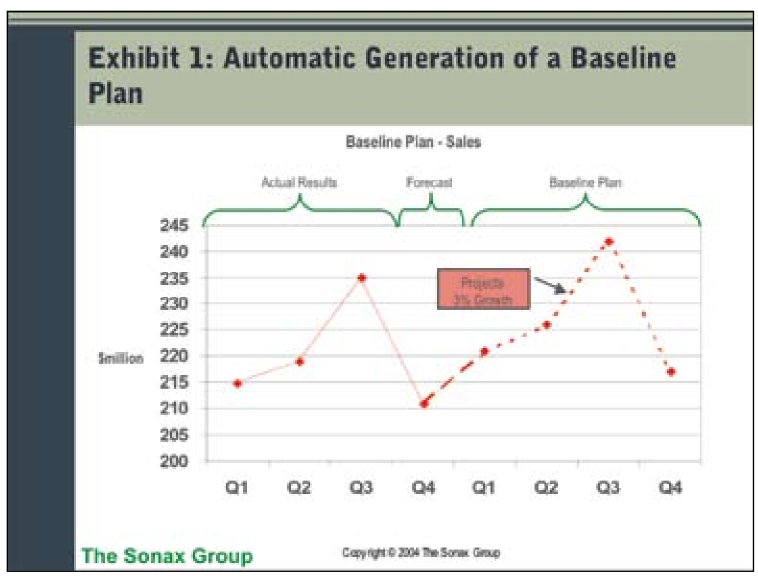
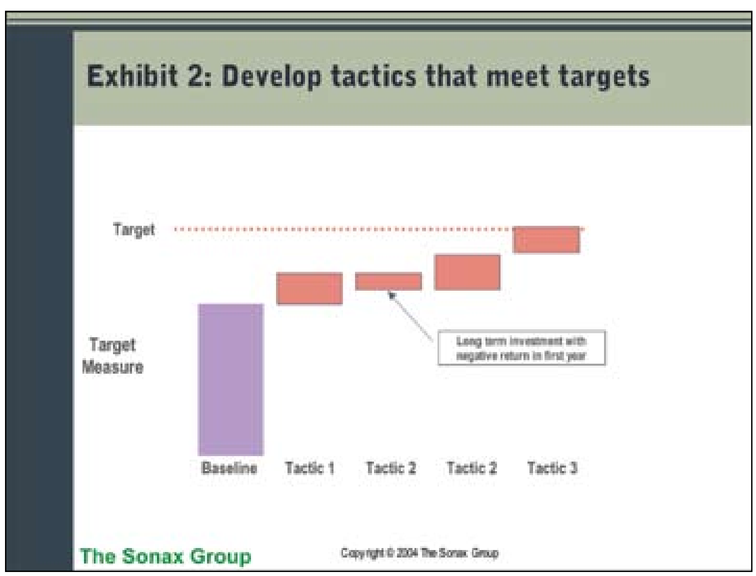



**Exhibit 1: Automatic Generation of a Baseline Plan**

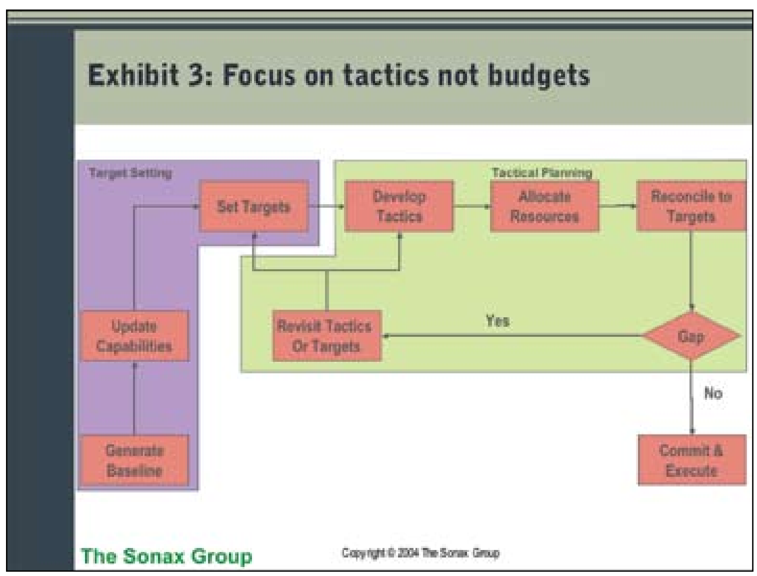
Once a credible baseline has been established, it is modified using predefined productivity and growth assumptions along with data regarding material events and trends on the horizon that may affect the company. This includes adjustments to reflect anticipated events such as divestiture of a business, the opening of additional distribution outlets, retirement of certain products, or the installation of new computer systems. Also considered will be the impact of external factors such as price increases from suppliers, changes in customer behavior, or the introduction of new products by competitors. The impact of these events is compiled using a sophisticated performance management tool that is a must for assembly and adjustment of baseline data.

With an updated baseline in hand, analysis is carried out to model various performance scenarios, so that senior management can gain an understanding of the likely impact of risk and uncertainty under different sets of assumptions. This gives management a range of performance potential that provides a rational basis for setting targets. (See Exhibit 2.) Senior management determines what must be attained to stay on course toward overall strategic objectives. The resultant targets set by senior management are chiefly numeric and should establish a bandwidth of desired performance, not achievement of a single number. It is then up to operating management to identify the appropriate mix of actions and resources required to move the organization forward.



### Establishing tactics, not budgets

The focus then shifts to determining the major tactics, improvement efforts, or new initiatives needed to achieve the performance targets. (See Exhibit 3.) When expectations are measured against a company's present capabilities, two situations will occur. In some cases, corporate capabilities will match expectations, which then become the target for the ensuing period. In other cases, gaps will become apparent. New tactics will be needed to close the gaps, and tactic development becomes the heart of the new planning process. Operating management must work out the details, driving down into the organization as far as needed or desired to come up with new programs (and their resource requirements) to tell senior management how the company will close the gaps and what is needed to do so. Each business unit develops a set of tactics which must be a collaborative, cross-functional activity.

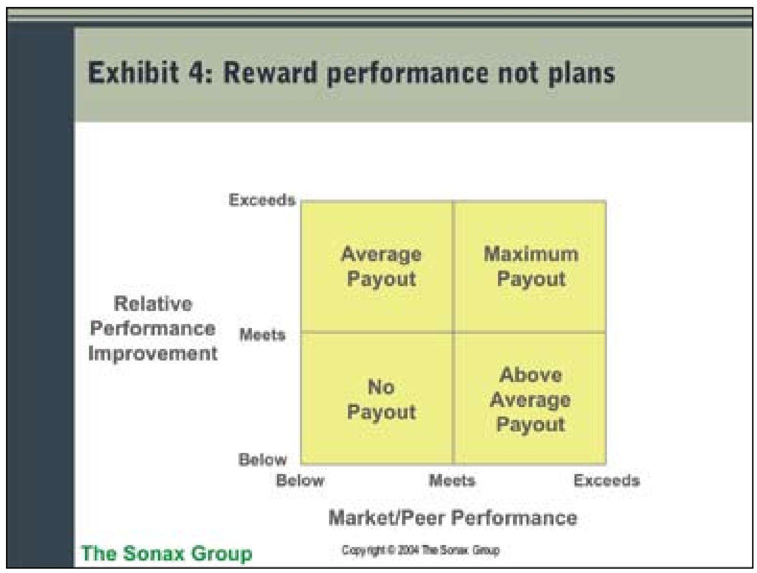


The tactics and resource requirements determined by operating management are committed to senior management's targets through a process of consolidation, balancing, and problem resolution. When pinch points occur, the preference is to revise the tactics, rather than to adjust the targets. For example, the planning process may bring to light that multiple business units are planning new initiatives in China; if possible, plans should be consolidated to achieve economies and free up resources for other improvement programs. Such resource balancing driven from the review of proposed tactics is much more constructive than the arbitrary top-down budget cuts that characterize so many outdated planning processes today.

Once the operating tactics are settled, managers assess the probability and materiality of key risk factors against each major business/project and define not only the criteria for success and appropriate contingencies, but also the exit/abandonment points that ensure failing initiatives do not continue to drain valuable resources. Adding a clear definition of the conditions under which initiatives should be abandoned is a crucial component of any effective planning process and one that is sadly missing in most companies. It is naïve to suppose that the assumptions made when approving an initiative will continue to remain valid during execution. For example, many business cases projected stellar returns from dot-com ventures, but few contemplated failure; the result was billions in wasted investment.

Once the tactical planning process is completed, managers select appropriate leading indicators and performance measures to track progress and to serve as crucial alerts. Managers commit to tactics, actions, and resources, rather than numbers. This significantly reduces the capacity for "sandbagging the numbers" and also establishes the basis for setting incentives.

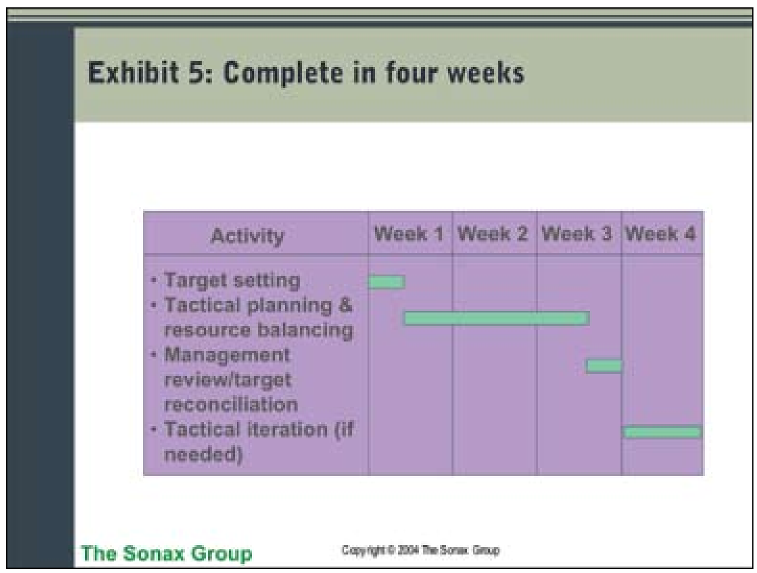
Compensation target setting must be kept separate from target setting for resource allocation. Compensation targets should be established based upon net change in performance over time, combined with performance relative to the market or a peer group. (See Exhibit 4.) The focus should be on rewarding improved performance, and this is best addressed by answering two questions: "How much have you improved?" and "How did you perform relative to the market or competitors?"




Rather than using meaningless budgets that fail to account for ongoing business activity, performance is managed solely using ratios and trends such as recruitment cost as a function of headcount added or sales close rates per customer call. Relating the management of any activity to volume adds relevance to decision-making and limits the endless reporting of variances to long-obsolete budget numbers.

**Planning becomes continuous**

Creation of a new plan should take about month. (See Exhibit 5.) The target-setting process by senior management should require no more than two to four days, with two to four weeks following for operating management to develop tactics and allocate resources, then two days for senior management to reconcile tactics to targets. If tactical iterations are required, the cycling back with operating management should take about a week.




Once tactical planning is complete, it should be able to be constantly refreshed upon demand, with new or modified tactics commissioned within a week, in response to the real-time flow of events. The integration of planning, reporting, forecasting, and decision-making into a single, continuous, and seamless process aided by the latest performance management tools and technologies brings core management activities into the 21st century. Planning becomes dynamic, continuous, and inextricably linked to the constantly changing environment in which every organization must operate. At any point in time, a plan update could be quickly generated. Changes in market conditions or failures inside the company should trigger a revision to the plan—not a laborious update of the numbers, but a review of the tactics and rapid decision-making about adjustments that are required. The focus is not on the achievement of some monthly or quarterly numeric targets and explanation of any variances, but on closing gaps for the future. Planning evolves into the core of the management decision-making process and is not isolated from the reality of survival in today's increasingly complex, volatile, and unpredictable markets.

**About the authors**

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### About the IBM Cognos Innovation Center for Performance Management

The Sonax Group is a consulting and advisory firm redefining business management practices. Established by David Axson and Greg Hackett, founders of the renowned benchmarking and finance transformation authority The Hackett Group, the firm works with executives to improve the effectiveness of their planning, performance management, and decision-making processes, radically simplifying and refocusing them to achieve flexibility, agility, confidence, and consistency. Learn more about the Sonax Group at www.sonaxgroup.com

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The IBM Cognos Innovation Center is dedicated to transforming routine performance management practices into "next practices" that help cut costs, minimize risk, streamline processes, boost productivity, enable rapid response to opportunity, and increase management visibility.

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