



How the Beyond Budgeting Management Model Enables Lean Thinking

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“Imagine you had a way of managing that generates initiatives among everyone in the organization to adapt, improve and keep the organization moving forward.”

Source: Rother, M. *Toyota Kata*, Mc Graw Hill, New York

The rise of “Beyond Budgeting”

- BBRT started in UK in 1998; BB is an idea, RT is a community
- BB idea:
 - > Reform the Performance Management Model from annual, fixed and bureaucratic to continuous, adaptive and devolved – more in tune with today’s competitive imperatives
- RT community is a worldwide movement of members sharing knowledge and best practices about implementing the new model
- Aim is to enable Adaptive, Lean and Ethical Organizations
- “Mindset” battle is with Finance



Outline

- Why we need to change
- Lean and agile requirements
- Changing mindsets
- Transformational change to “Beyond Budgeting”
- Some implementation insights

Volatility and Uncertainty are Now “Business as Usual”

EUR/USD - Last 2 Years

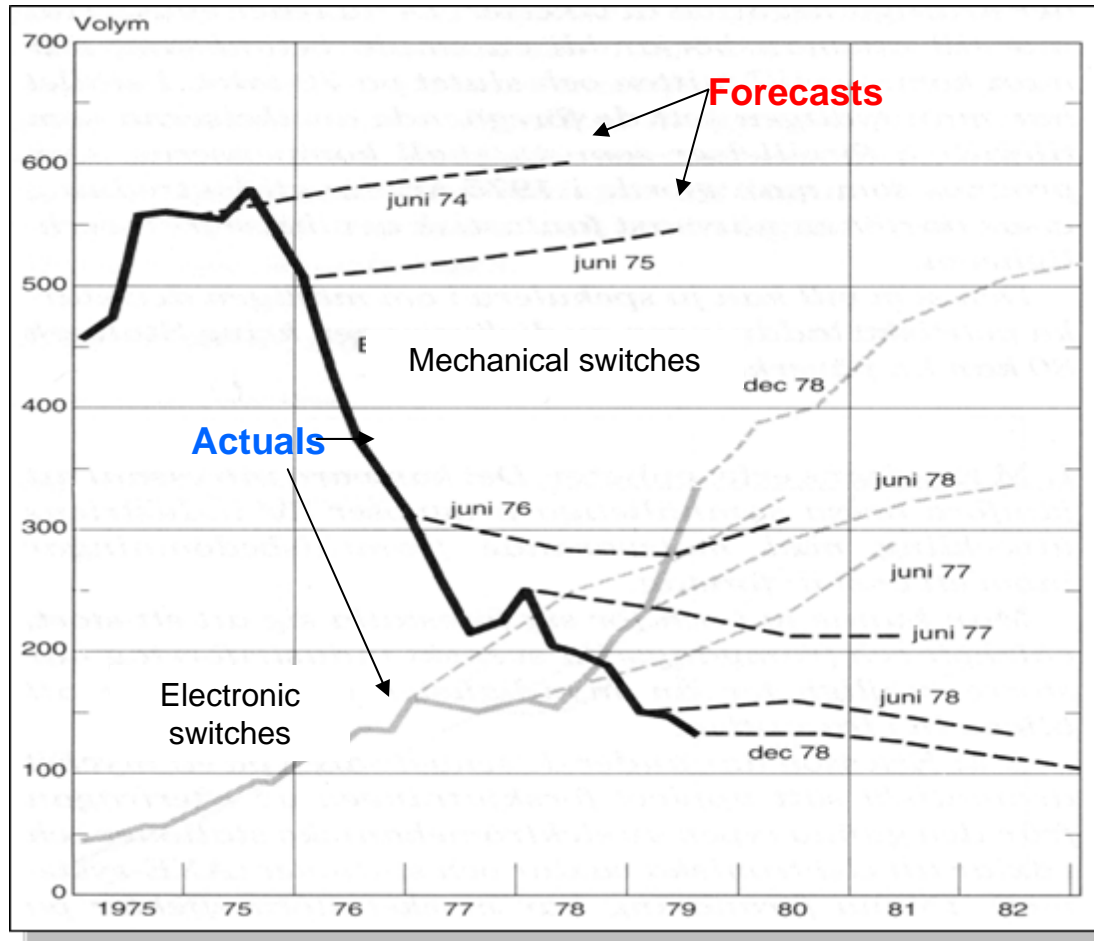


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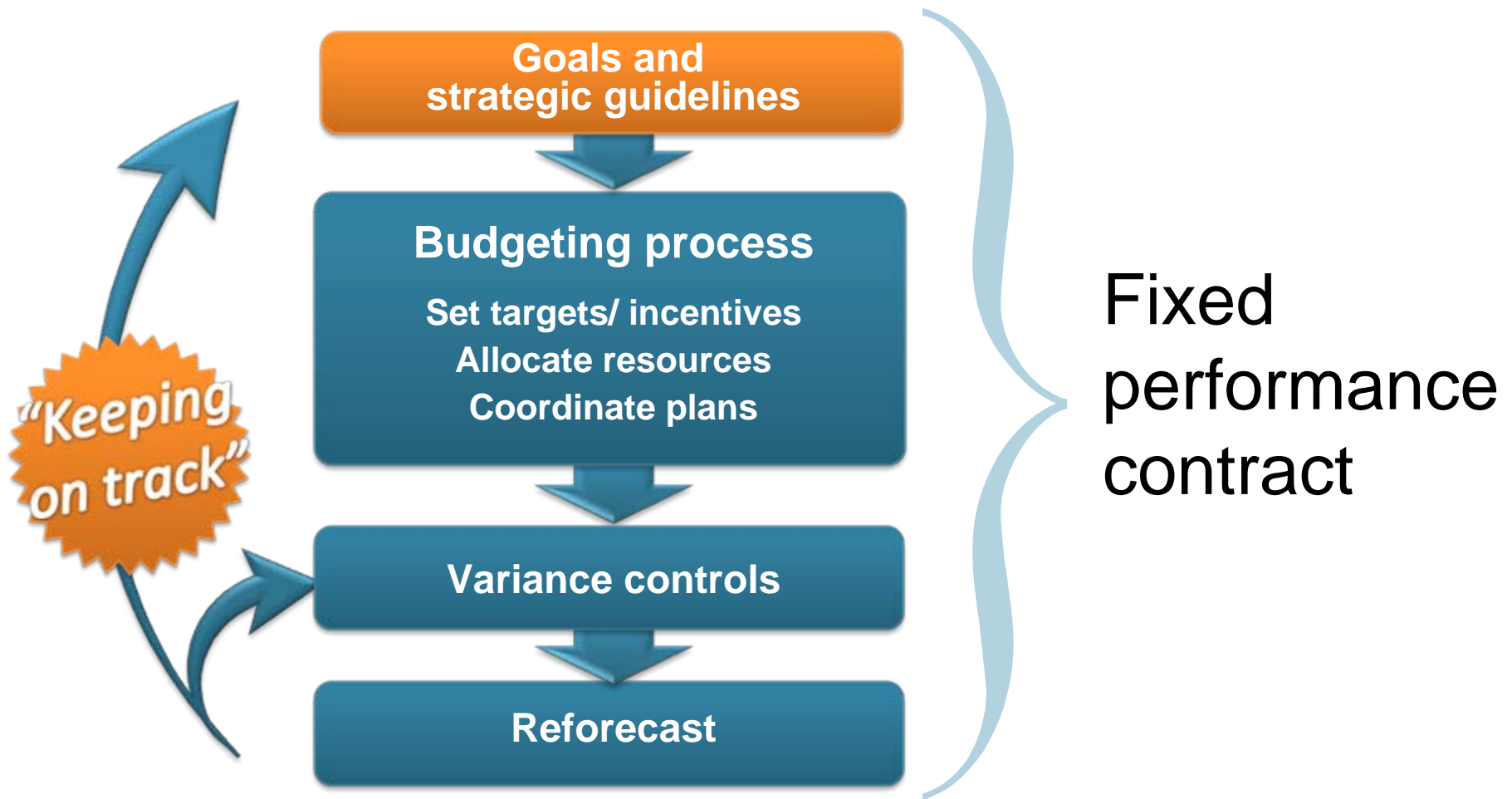
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Is your business predictable?



Source: Jan Wallander, Budgeten - ett onödigt ont, 1994, p24

The trouble is that the budgeting process is annual, negotiated and fixed



Budgets drive the wrong behaviour

We always provide forecasts that bosses want to see

We always spend what's in the budget

We always negotiate the lowest targets and the highest rewards

We never share knowledge or resources with other teams – they are the enemy

We always make the bonus, whatever the risk!

While we like to please customers, our sales targets come first

We always ask for more resources than we need, expecting to be cut back to what we actually need

Budgets create a ceiling on costs ...



... they also create a floor

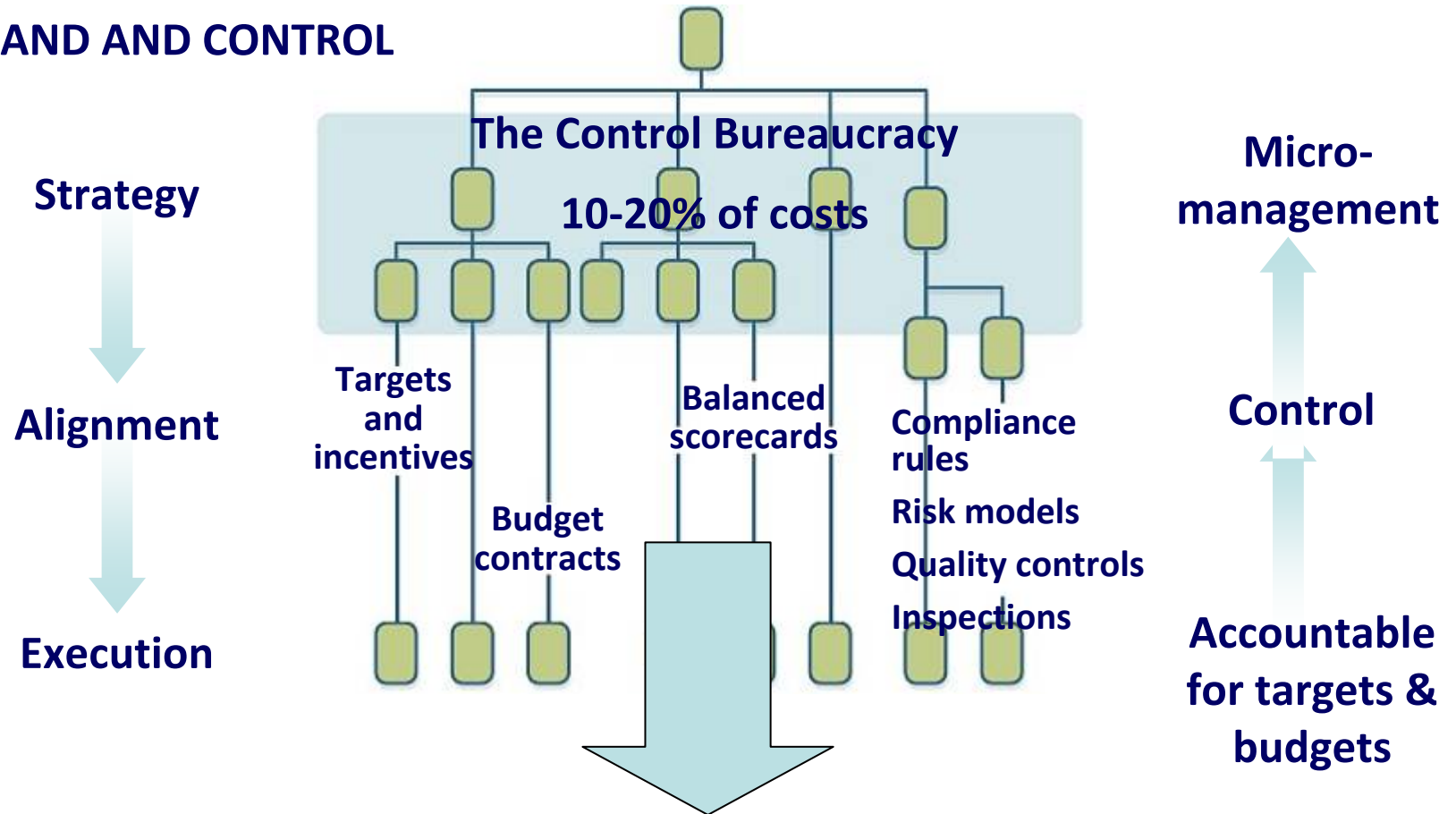
Too many forecasts are tied to the budget and provide little value



- Forecasts are tied to year-end targets that lead to “gap-filling” decisions
- Forecasts are treated as performance contracts that lead to bias
- Forecasts are prepared for “corporate” and dilute local ownership

Many leaders believe that more micro-management provides more effective accountability and control

COMMAND AND CONTROL



More... cost centres, budget lines, cost allocations, data errors, scorecards, targets, risk models, reports, inspections

Lean concepts

- Specify the value desired by the customer
- Identify the value streams for each product providing that value and challenge all the wasted steps
- Make the product (or service) flow continuous
- Introduce “pull” between all steps where continuous flow is impossible
- Manage toward perfection so that the number of steps and the amount of time and information needed to serve the customer continuously falls

Lean focuses on efficient process execution, but is this enough in a world of increasing change and uncertainty?

Lean & Agile

- Organizations also need to be agile
- Agility is the ability of an organization to *thrive* in a continually changing and unpredictable business environment.
 - > Produces competitive advantage for a company and high levels of satisfaction for its customers
- Lean and Agile - couples lean thinking with an organization that is physically, technologically and managerially structured for rapid and unpredictable change

Agile organization conditions

- Decentralised & devolved decision-making
- Leveraging employee creativity across the organization
- Eliminating departmentalisation within the organization
- Forming partnerships in the supply chain
- Treating each customer as an individual and providing a whole solution
- Ability to address niche markets rather than merely addressing mass markets

Lean implementation approaches

Rapid Improvement Events (Kaizen Blitz)

- Provide fast return for effort
- Higher visibility
- Less challenging to existing management style
- Lack of overall visibility
- Only shorter, simpler projects
- May not embed culture of continuous improvement

Full Implementation Approach

- Complete cultural shift
- Sustainability of changes
- Whole system change
- Links changes with strategy
- Bigger implementation challenge
- Greater potential for resistance
- **Challenges existing management styles**

Source: Radnor et al (2006) *Evaluation of the Lean Approach to Business Management and its use in the Public Sector*. Scottish Executive Social Research

Findings from Scottish Executive study

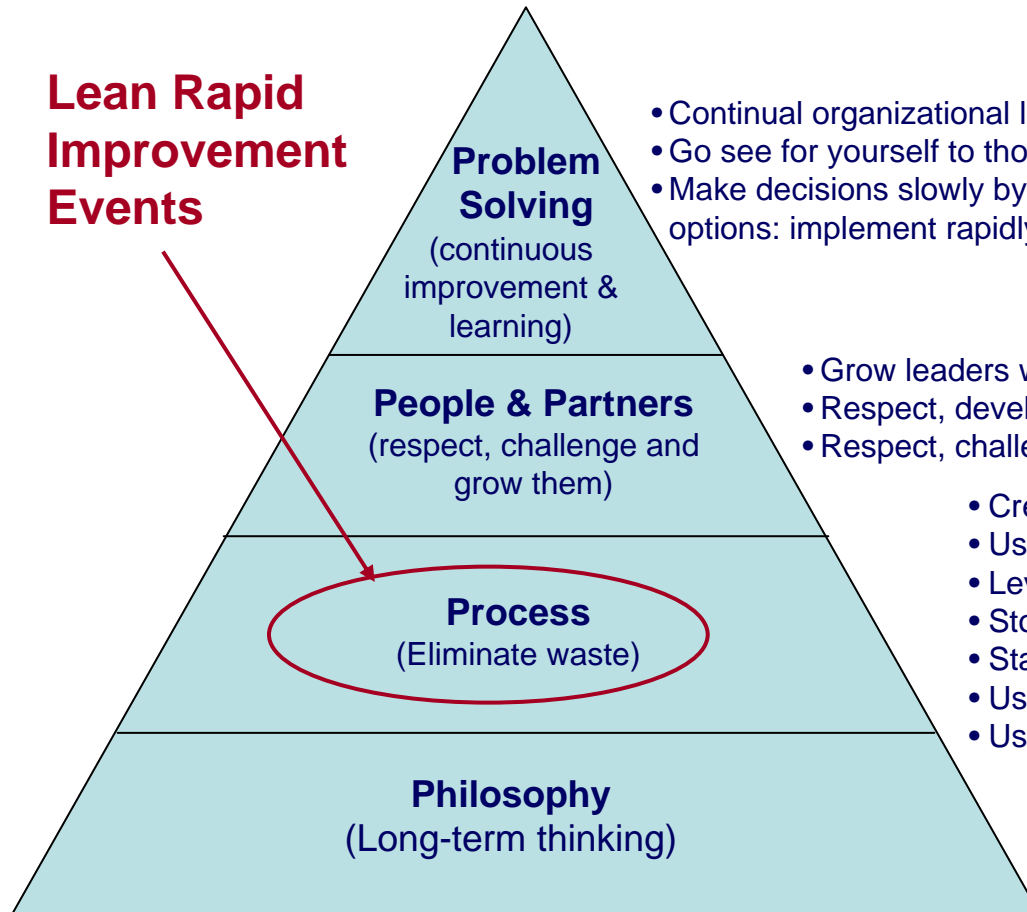
- Lean improvement initiatives were not integral to organizational strategy
- Need to more clearly allocate resources to improvement activities to sustain success in the longer-term
- More sustained and effective Lean application would link strategy and operational improvement in a whole systems approach

“The long-term aims of its Lean programme could not be achieved purely through a succession of operational-level RIEs without some form of strategic level direction.”

Source: Radnor et al (2006) *Evaluation of the Lean Approach to Business Management and its use in the Public Sector*. Scottish Executive Social Research

Comparison with the Toyota Way

Lean Rapid Improvement Events



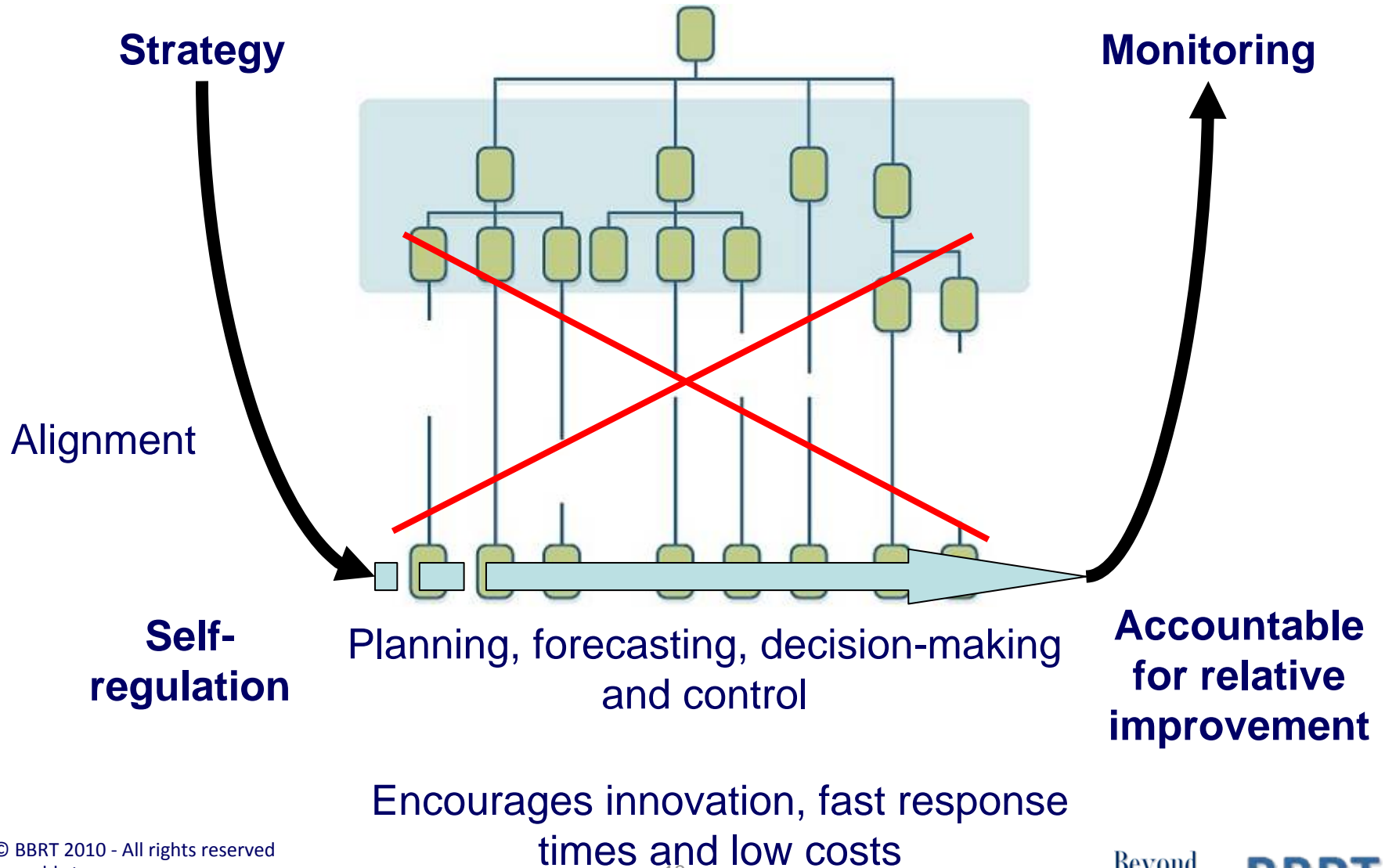
- Continual organizational learning through Kaizen
- Go see for yourself to thoroughly understand the situation
- Make decisions slowly by consensus, thoroughly considering all options: implement rapidly

- Grow leaders who live the philosophy
- Respect, develop and challenge your people and teams
- Respect, challenge and help your suppliers

- Create process “flow” to surface problems
- Use pull systems to avoid over-production
- Level out the workload
- Stop when there is a quality problem
- Standardise tasks for continuous improvement
- Use visual controls, so no problems are hidden
- Use only reliable, thoroughly tested technology

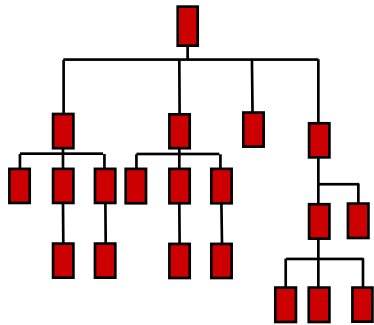
- Base management decisions on a long-term philosophy, even at the expense of short-term financial goals

Emerging Management Model



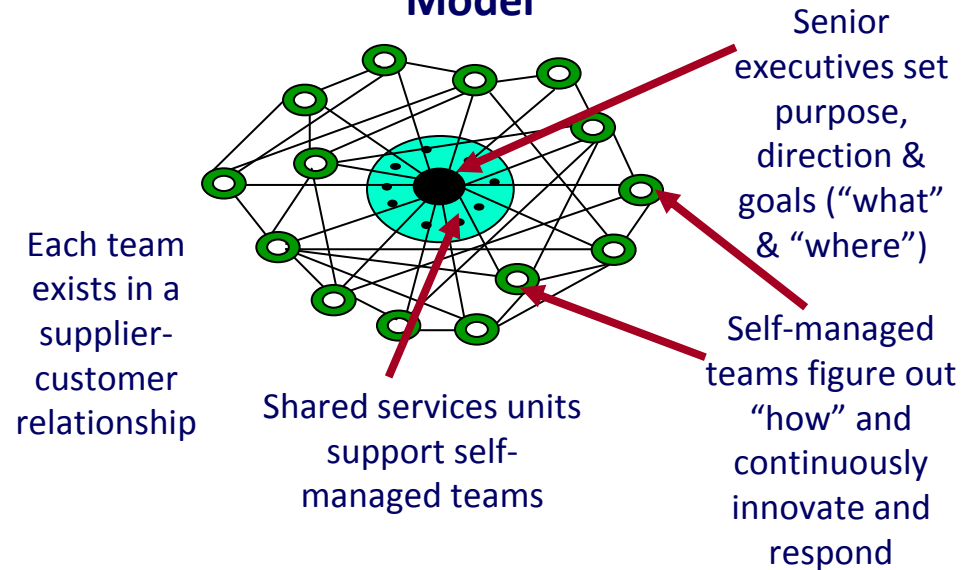
Changing mindsets

'Command and Control' Model



- Organizations are obedient machines
- Organizations are a collection of replaceable parts (parts determine performance of the whole)
- Organizations comprise of 'cause and effect' relationships that are predictable
- Organizations need central planning, coordination & control
- Change is reactive and project driven

'Beyond Budgeting' or 'Empower & Adapt' Model



- Organizations are adaptive systems
- Organizations are holistic systems (whole system determines performance)
- Organizations are webs of relationships that are unpredictable
- Organizations are self-organizing and self-regulating
- Change is integrative and adaptive

The Beyond Budgeting Vision



GOVERNANCE & CONTROLS

- Establish inspiring values/purpose
- Define success as “being the best”
- Make information open and transparent
- Use holistic controls

TEAMS, ROLES & RESPONSIBILITIES

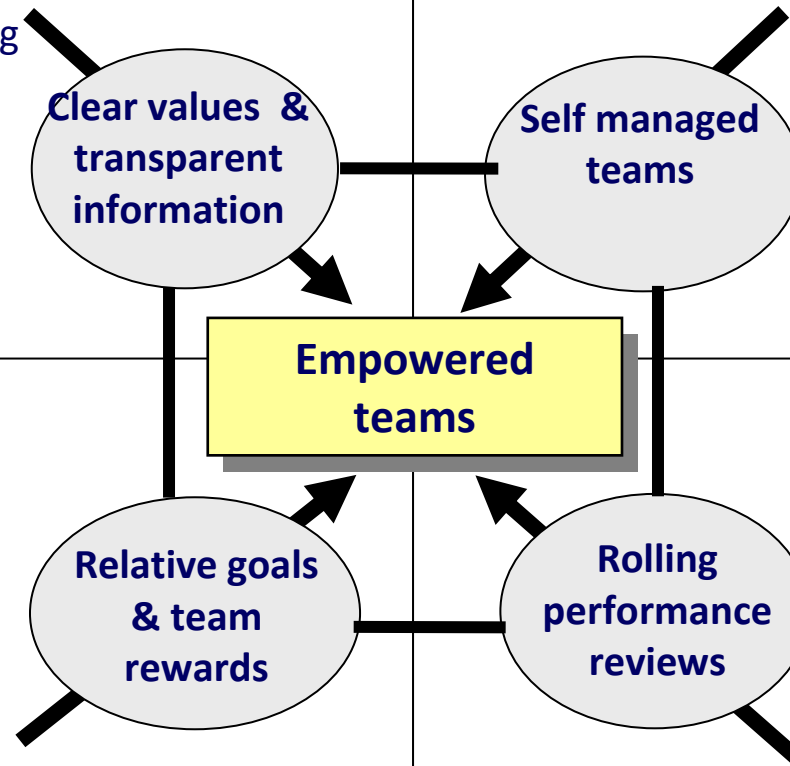
- Organize around 3 types of team (executive, support services & value centres)
- Devolve planning & decision-making to teams
- Make teams accountable for their performance

- Enable teams to set goals
- Decouple goals from performance measurement & rewards
- Recognize & reward relative improvement

- Use a rolling performance review process
- Use trends & rolling forecasts to guide actions
- Fund best current action plans (not budgets)
- Coordinate actions in real-time
- Use benchmarks & ratios to manage costs

GOALS & REWARDS

PLANNING & RESOURCES



Exemplars of the new vision



Europe's best performing bank

Svenska Handelsbanken



Alexander V Dokukin

- Swedish bank but growing rapidly in UK
- \$5bn revenue
- Lowest costs in Europe (cost/income ratio around 40%)
- Customer focused model (highest customer satisfaction)
- Transparent information
- No bureaucracy, no budgets
- 600 profit centres; Peer comparisons drive performance improvement
- Branches 'run their own business'

Beyond Budgeting at Statoil



- 1 October 2007 - merger between Statoil and Hydro's oil and gas activities
- About 29,500 employees in 40 countries
- The world's largest operator in waters more than 100 metres deep
- Operator for 39 producing oil and gas fields
- Market capitalisation worth more than \$70 Billion
- Production averages more than 1.7 million barrels of oil equivalent per day
- World leader in the use of deepwater technology and carbon capture and storage
- Strong collegiate culture
- Over 800 value centres using "Ambition-to-Action" scorecards that drive growth and innovation
- No budgets or fixed contracts
- Fast, continuous investment decisions

Best airline?



- Icon of Corporate America - consistently profitable for >30 years; highest shareholder returns of peer group
- Top of independent customer satisfaction ratings in USA + lowest number of customer complaints for last 13 years
- Best productivity and safety record.. Company that graduates most want to work for
- Puts employees first and customers second. 'Hires for spirit and trains for skills'. Unleashes the imagination and energy of its people. Makes work fun
- No fixed performance contracts. 'Budgets' treated like rolling forecasts. 15% of pre-tax profits paid into profit sharing pool and paid into a retirement fund for all employees according to base salary

Park Nicollet



- Non-profit serving Minneapolis-St Paul area
- Four primary sub-units:
 - > Methodist Hospital (426 beds, 960 doctors)
 - > Park Nicollet Clinic (25 locations)
 - > Park Nicollet Foundation (money-raising)
 - > Park Nicollet Institute (research)
- Implementing both **Lean Management** and **Beyond Budgeting**
 - > Both centred on CFO's office

Lean Management at Park Nicollet

- A few KPIs had to replace detailed budget reports
- Set targets for improvement and track actual performance to them
 - > No comparison with forecasted performance
- 2005 – dual system
- 2006 – no annual budget
- Example of process difference to manufacturing:
 - > Key “inventory” – number of patients waiting → communication
 - Wait times at urgent care centres updated on web site every 30 minutes

Budgetless Reporting at Park Nicollet

- Financial planning process – for finance, not for operational managers
- Better processes deliver better services at lower cost
- Finance keeps a check on cash flow
- Six-quarter rolling forecast updated quarterly by CFO
 - > Not distributed to operational leaders
- Capital spending plan based on cash flow from prior years
- Senior managers direct money where it's needed without budgets
- Measure their unit's performance by KPI:
 - > Units of service per WTE
 - > Actual cost per unit of service
 - > Margin on units of service
 - > Total expenses
 - > Units of service per square foot

Toyota - the source of Lean



TOYOTA

TPS

- Consistently profitable for over 30 yrs
- Top of JD Power customer satisfaction ratings. #1 car maker in world (goal is 15% of global sales by 2010). Net margins of 8% dwarf big 3 rivals.
- TPS (Toyota Production System) based on 'Pull', not 'Push' leads to "half of everything"
- Costs seen through 'process' lens; NVA costs eliminated
- Simple organization; Job rotation in teams
- Continuous improvement (Kaizen); Aims for perfection
- Resources as required (JIT); Self coordination at team level (Kanban); Visual controls (Andon)
- No top-down controls; information is in the line; No fixed performance contracts.

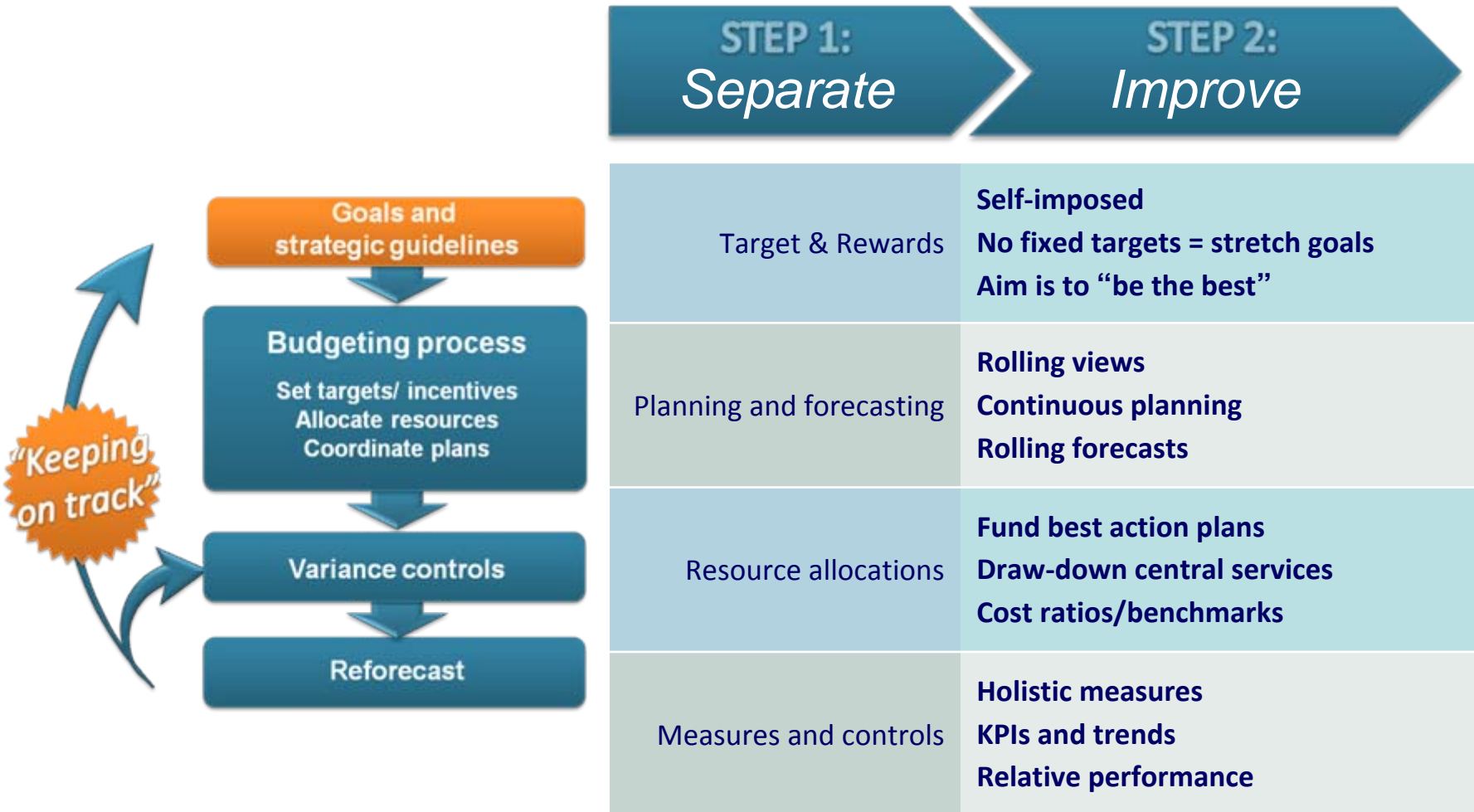
Toyota

“One of the best examples we currently have of an adaptive, continuously improving company is Toyota. Of course, Toyota makes mistakes too ,but so far no other company seems to improve and adapt - every day in all processes - as systematically, effectively and continuously.”

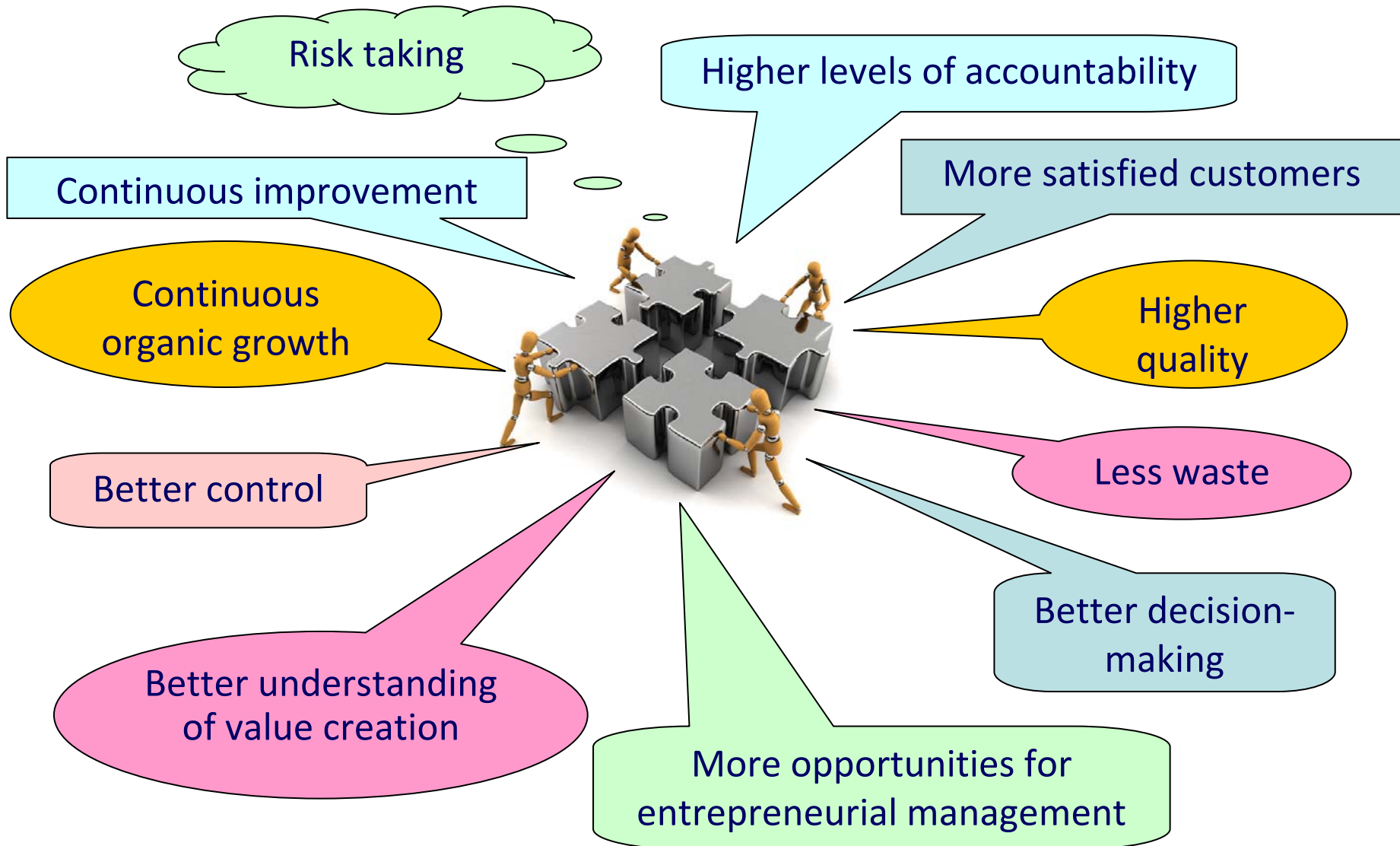
Mike Rother

Source: Rother, M. *Toyota Kata*, Mc Graw Hill, New York

They have all broken free



What you can gain



Formula for successful change

Formula for a successful change programme

$$f(D \times V \times S) > R$$

D = Dissatisfaction

V = Vision

S = Strategy and steps

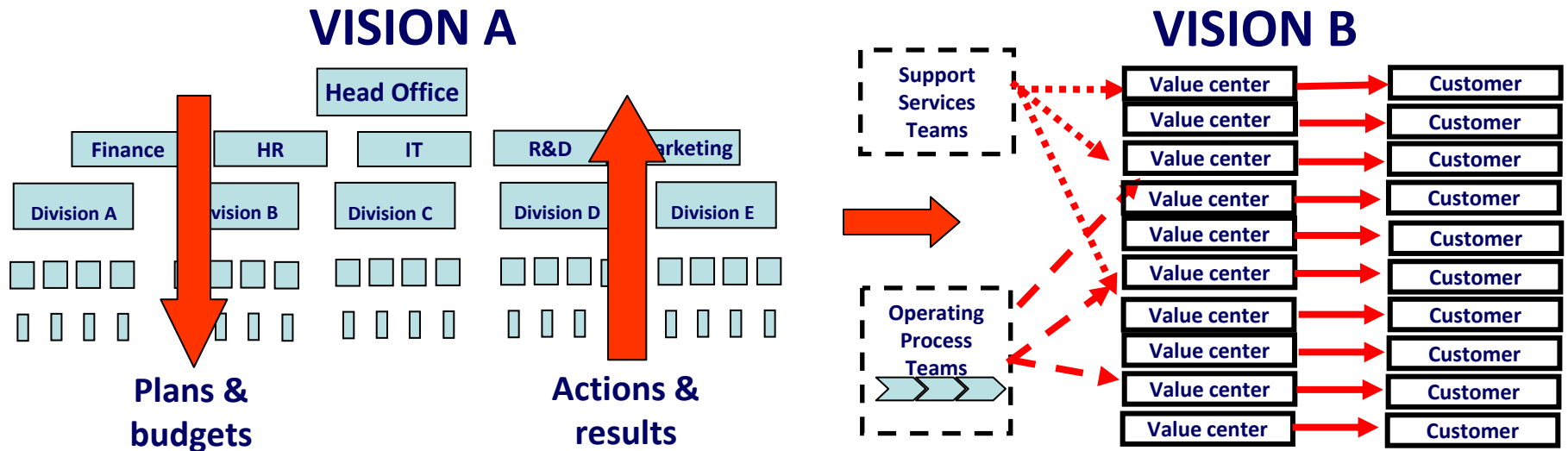
R = Resistance

D – Create a compelling case for change

Tap into what people really care about...

- 20% care about ***improving society*** (BB leads to more sharing, less greed and corruption, more sustainable investments and more ethical reporting)
- 20% care about ***improving the organization*** (BB leads to a better place to work, invest in and do business with (also lower costs, higher growth, etc))
- 20% care about ***improving the customer experience*** (BB leads to more ethical selling and more focus on keeping best customers rather than meeting sales targets)
- 20% care about ***improving the team they work in*** (BB leads to more team focus, more collaboration and more focus on internal/external customer outcomes)
- 20% care about ***improving their own position*** (BB leads to more opportunities for fast track development and more learning and self-improvement)

V – Choose the right vision (B)



- More bureaucracy and targets
- More budget accountability
- More top-down compliance and control
- More cost centre analysis
- Finance 80/20 controller/partner

- More freedom and capability
- More value creating accountability
- More local planning and self-regulation
- More performance insights
- Finance 40/60 controller/partner

R- The Wall of Excuses



The auditors won't like it
The regulators will object

Group will feel threatened

We have too many other priorities

We can't do the ROI

We don't have enough time/money/staff

I can't sell the idea to the board

It's too much work

We're too busy

It's too risky

It will take too long

It's not my responsibility It won't work in our culture

We tried it before and it didn't work

Our systems can't handle it

The bosses won't like it

We don't need to change



7 Deadly Sins

7. Not continuing

1. Not holistic

6. Wrong style

2. Not engaged

5. Not coherent



3. No vision

4. Wrong focus

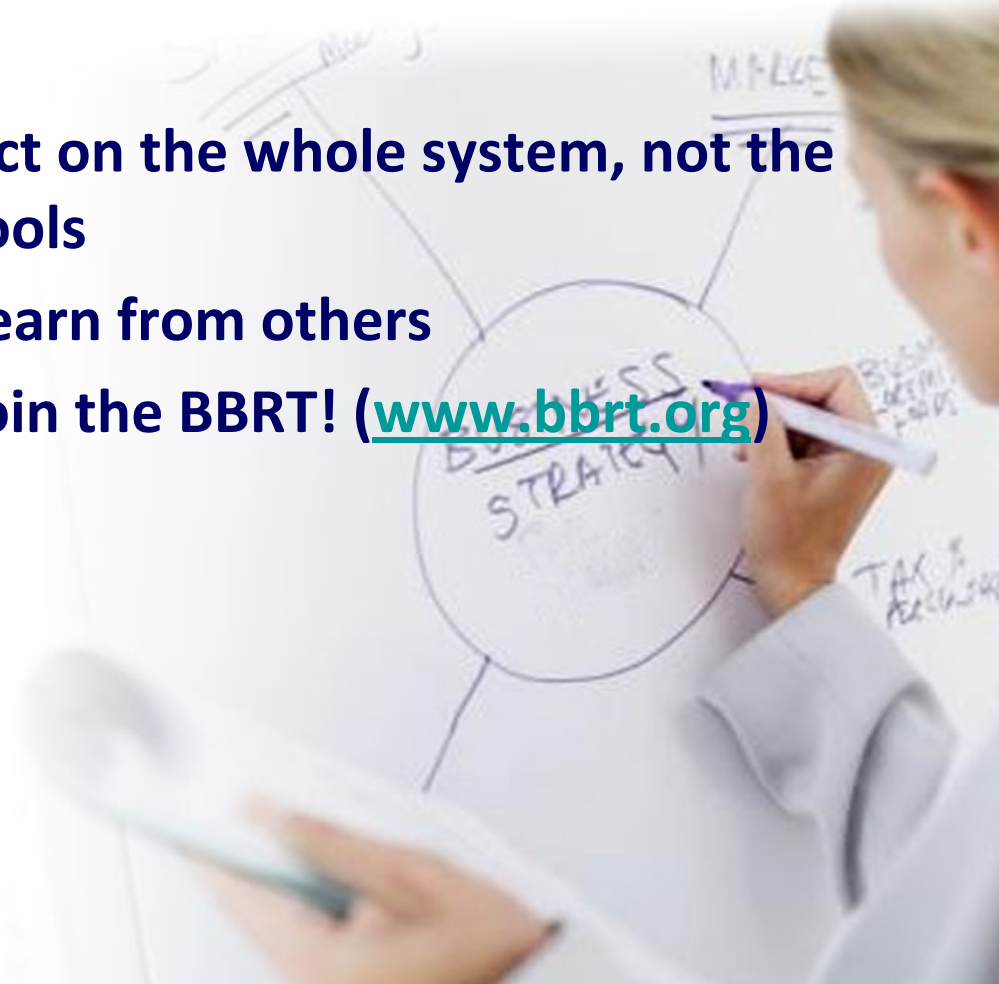
Beyond Budgeting management model

- Enables organizations to empower, endure and thrive in the face of high market volatility
- Provides the right platform for lean thinking and agility to realise their full potential
- Puts the emphasis on “means” and not “ends”

GET THE THINKING STRAIGHT BEFORE CHANGING



- Act on the whole system, not the tools
- Learn from others
- Join the BBRT! (www.bbrt.org)



The Beyond Budgeting Round Table

(www.bbrt.org)

- Packages now from only £6,000 to join for first year
- Gets access to all accumulated knowledge capital + major diagnostic
- Learn about cutting-edge performance management best practices
- Access to online Implementation Guide
- Access to research papers and interviews with leaders
- BBRT Team can provide courses and internal workshops

**Next Meeting:
21-22 March 2011**

Beyond
Budgeting®

Thank you

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