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# Eliminating roadblocks to Accelerated Performance Transformation

A three-step Accelerated Performance Transformation can help industrial, technology, and consumer companies obtain benefits that eluded them in the past.

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**Across industries,** the typical performance transformation runs into roadblocks. Leaders are pulled in multiple directions by the crush of daily work and have little time to devote to new initiatives. Companies lack systems for monitoring progress and fail to see that they are falling behind. Employees lapse into old habits after the initial excitement dies down, erasing any gains. These problems contribute to one well-known statistic: 70 percent of performance transformations fail.

As noted in the first article in this series, "A new approach to Accelerated Performance Transformation," businesses now have a greater imperative to improve performance. The current economic expansion is the longest in US history, but many executives believe that financial conditions are declining and are concerned about current global trade tensions. If a downturn does occur, companies may not be able to sustain their investments in innovative technologies and new initiatives unless they undertake a performance transformation that produces rapid results.

So how can companies avoid repeating past mistakes as they attempt to improve margins? The answer may lie in an Accelerated Performance Transformation (APT), which typically occurs over 18 to 24 months. An APT is not simply an accelerated version of a longer transformation. It is a new process specifically designed to address common challenges that throw companies off track. This article discusses the major benefits that APT delivers. It builds on the first article in this series, which described the rationale behind APT and provided a practical guide to implementation.

## The Accelerated Performance Transformation advantage: A review

Each APT involves three major steps (Exhibit 1):

— determining a company's full potential

— measuring progress toward absolute financial goals, rather than the money nominally saved by implementing cost-reduction initiatives

— driving a coordinated path to execution

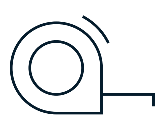
While many companies do not achieve substantial results from transformation programs for about five years, the three-step APT approach can deliver as much as 70 to 80 percent of the intended impact in less than two years at some companies. The secret behind this speed? Each APT step is designed to

Exhibit 1

### Companies should take an accelerated approach to improving core performance.

**Determining full potential**

– Getting detailed insight into baseline performance
– Conducting analyses of head count operational expenditures, cost of goods sold, cash flow, and revenue
– Creating a list of initial improvement actions



**Measuring absolute change in EBITDA,[1] not deltas in cost**

– Ensuring tight integration between improvement actions and profit-and-loss outcomes
– Creating an early-warning system
– Monitoring all changes that could affect EBITDA, including unexpected headwinds

**Driving a coordinated path**

– Establishing individual accountability
– Eliminating conflict among business units, functions, and sites
– Getting input from frontline workers

[1] Earnings before interest, taxes, depreciation, and amortization.

promote efficiency and eliminate common problems that arise as companies transform their workplaces.

## Determining full potential

In any transformation, companies must first establish an accurate baseline and then determine the organization's full improvement potential. It sounds simple, but many businesses struggle with these tasks, undermining the entire transformation. The APT approach brings new rigor and accuracy to baseline calculations for both financial metrics and head count, eliminating many problems.

**Defining the baseline**

Too often, companies use plans or forecasts rather than actual data when calculating baseline numbers for financial and operational metrics, and this can have serious consequences. For example, a division within a company might overestimate its spending in the annual operating plan. If the actual spending falls below this estimate, it might look like the division has achieved major savings. In reality, however, these are costs avoided rather than real gains—and that translates into little bottom-line improvement.

During APT, companies will ideally review hard data when establishing baselines. To identify the most reliable information, they should examine multiple sources, including those related to transaction histories, departmental spending, and profit-and-loss (P&L) records. Companies should give preference to the data that require the least manipulation, if possible.

For accuracy, companies must determine how much was spent, who spent it, exactly what they purchased, and when the transaction occurred. Each dollar will tie to a general-ledger code and vendor. Beyond spending, companies must also attempt to establish actual numbers for head count, operating expenses, cost of goods sold (COGS), cash management, and revenue optimization.

A capital-goods manufacturer followed the APT approach to get its travel and expense (T&E) spending under control. It examined specific sections of different reports, including a daily-spending breakdown for each person who traveled, to get new insights. With this information, the company could identify specific solutions to reduce travel costs, such as having service employees who are paid hourly fly on Monday mornings for short trips rather than on Sundays. The company also identified opportunities for employee car pools during business trips. Altogether, it reduced T&E spending by more than 30 percent.

While these results are impressive, other companies may not be able to go beyond estimates and rely on actual data for two reasons. First, the necessary information may simply not be available. In other cases, companies have the data but either overlook them entirely or use very little. This problem is especially common when companies keep critical performance information in multiple function- or division-specific databases rather than in a central location, where it is readily available. Companies that have multiple business units and those that routinely undertake M&A may encounter this issue most frequently.

If actual data are not available, companies must make assumptions and improvise—although with a greater reliance on available data and observations. For instance, an industrial-machinery manufacturer on an APT journey wanted to establish a baseline for shop-floor-operator productivity but lacked hard data. Instead of trying to estimate the baseline, the production managers addressed the data gap by making multiple observations of shop-floor operators across activities. After gathering information, the managers could knowledgeably discuss work patterns with frontline employees and develop a list of improvement initiatives.

*Systems and processes for collecting and disseminating baseline data.* Companies do not need to build sophisticated databases or models before they begin their APT efforts, since that might delay the desired impact by several years. Instead, they should build new systems as the APT proceeds. The resulting tools and models will suit their organizational needs better, since the APT process will help them understand what information is most important and how they should analyze it.

When calculating baseline numbers, companies should ensure that spending categories are consistent across the organization. In addition, the information for different sites, business units, and functions should always be in the same format to facilitate comparisons.

*The process for reaching agreement.* Above all, a good baseline must reflect the consensus of all relevant groups and have their full support. All critical stakeholders, including site and functional leaders, business-unit controllers, HR heads, the CFO, and other C-level executives, should agree on the financial and head-count numbers. To gain this consensus, companies should set up a project-management office and install a dedicated team that consolidates financial and operational information into a single, centralized database (Exhibit 2). In addition to information from headquarters and sites, the database may contain information from third-party contractors. All relevant employees should have access to the system, which will allow them to see the same information in real time.

Exhibit 2

## Companies should keep all baseline data in central repositories.

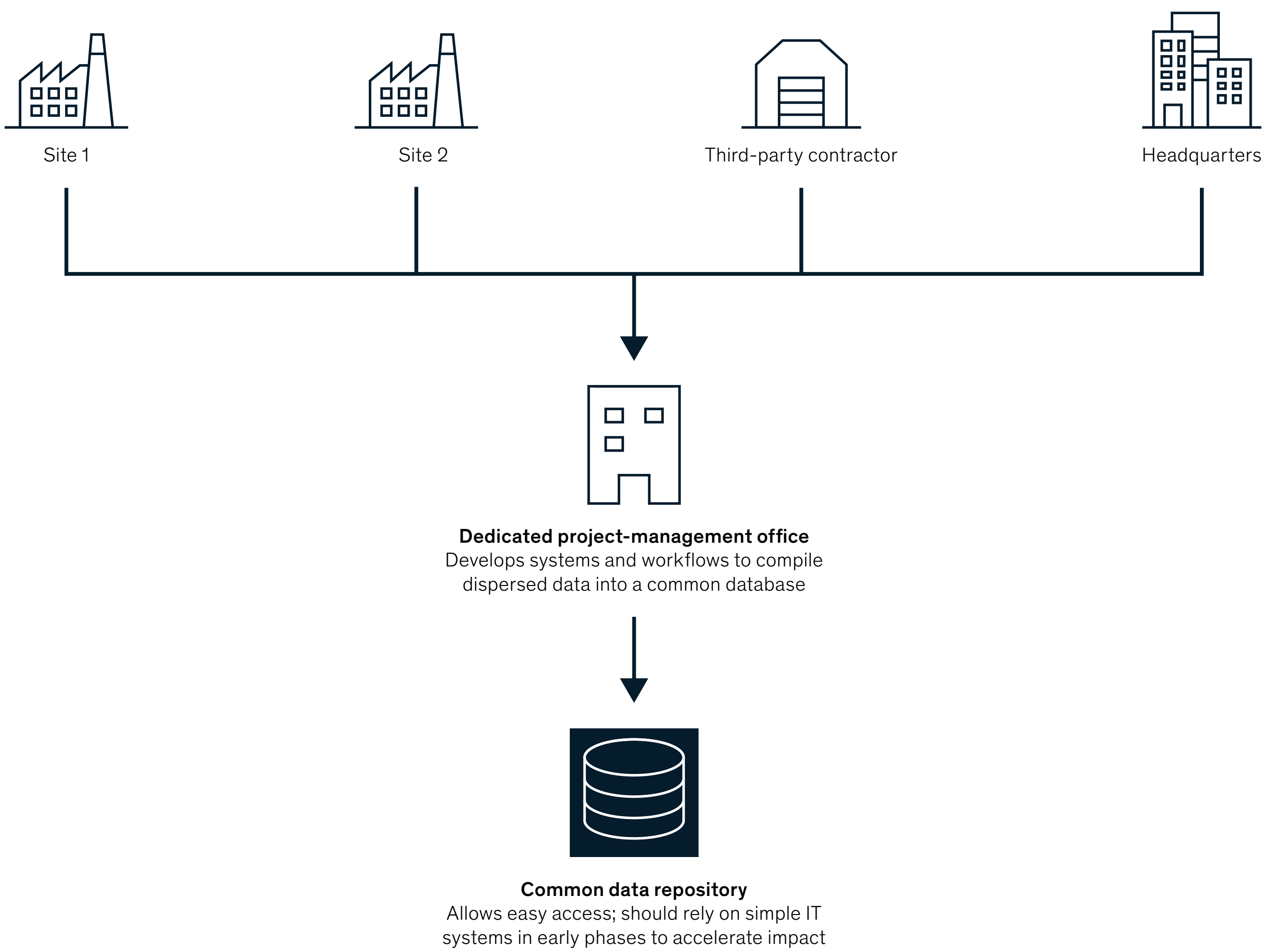


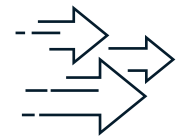
Exhibit 3

## Reliable baselines provide companies with a single source of truth.

**Steps to reach a fact-based baseline,** 4-week effort

**1. Identify best data sources**
- Ideally, examine actual data rather than estimates
- Consult multiple sources and break down spending at a detailed level (eg, who spent it, what was purchased, when transaction occurred)
- Harmonize inputs across organization

**2. Align across organization**
- Ensure that baseline head count and financial numbers reflect consensus of CFO, business-unit controllers, HR managers, functional leaders, and other critical staff
- Consider that multiple reviews may be necessary



**3. Harmonize output**
- Use same output format and spending categories across sites, functions, and business units
- Ensure that baseline data have enough detail for managers to track progress easily and identify opportunities for improvement

One semiconductor manufacturer took dramatic steps to achieve a baseline consensus. First, it created a database that harmonized spending categories across different manufacturing sites and ensured that the same accounting methodologies were used within specific spending categories. The company also reconciled the method for computing intracompany transfer costs. While this effort required multiple rounds of syndication, it allowed the company to reach a consensus about baseline spending across regions and sites (and, in turn, made cost comparisons across locations easier). Employees could also easily consolidate spending at the regional and global levels if they wanted to see the big picture.

Exhibit 3 summarizes the process for establishing a reliable baseline.

### Setting targets

When companies set improvement targets, they often set year-on-year goals and strive for the same amount of annual improvement. Another common method involves peer-to-peer benchmarking. Both methods tend to leave opportunities untapped or overlook nuances, such as the areas with the highest improvement potential.

With APT, managers avoid these problems by relying on a unique method: "you to you" benchmarking. This process involves examining a company's current performance and then determining its full potential for each function and subfunction. In other words, it compares where you are now with where you could be, always considering a company's specific context and circumstances. Such investigations help managers understand roadblocks and uncover opportunities that would otherwise go unnoticed, allowing them to develop customized improvement programs.

To see the benefits of you-to-you benchmarking, let's return to the example of the industrial-machinery manufacturer that wanted to improve shop-floor productivity. During visits to the shop floor, the production managers made close observations and engaged in discussions with frontline employees. In addition to enabling a solid understanding of baseline productivity, their investigations helped managers identify areas of waste and estimate the full improvement potential of the shop floor. Among other findings, the production managers learned that engineering drawings often omitted important details—and when that happened, operators often had to wait for 30 to 60 minutes for engineers to arrive and address their concerns. The production managers then asked a manufacturing engineer to move his work desk to the shop floor, where he would be immediately accessible whenever an operator had a question. This initiative, and other changes made because of you-to-you benchmarking, helped boost labor productivity by 35 percent.

This example shows another major benefit of you-to-you benchmarks: their development occurs with input from all employees, ranging from senior executives to frontline workers. By contributing feedback, employees feel a sense of ownership and are thus more likely to accept the numbers. A top-down program, developed by senior managers in isolation, would be less likely to receive support.

*A new approach to reaching targets.* During most performance transformations, many managers turn to wide-ranging initiatives that require significant funding and resources, such as automation programs or large-scale analytics. While large initiatives certainly produce results, managers should not overlook small-impact initiatives that are easier to implement. These smaller efforts, which departments own, usually generate impact within six months. The quick wins build support and energy among staff and give up-and-coming employees a chance to demonstrate their leadership. (Medium-impact initiatives typically produce results within six to 12 months and are under the control of regional or functional managers.)

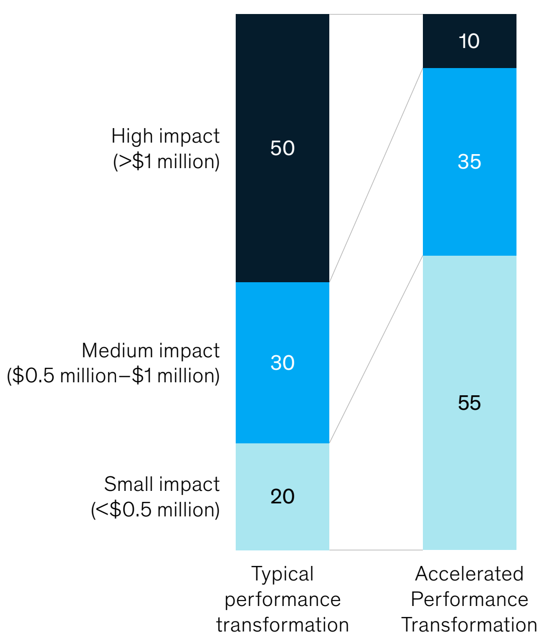
To see the importance of small-impact initiatives, consider the results achieved by an industrial-goods manufacturer. One division set up a spend-control tower, staffed by midlevel managers, within each of its departments. All indirect expenditures greater than $1,000 had to be approved through this channel, effectively capping the spending authority of lower-level managers. Within six months, the division reduced its spending by 21 percent without adversely affecting critical purchases, including those related to maintenance services and consumables. Beyond the immediate impact on the bottom line, the spend-control towers created unprecedented transparency about the division's regular expenditures—and that gave them a critical role in subsequent cost-reduction efforts.

With the observation-based analyses generated during APT, companies will be able to develop a more balanced portfolio of initiatives (Exhibit 4). Typically, the new portfolio will include a mix of company-wide initiatives that require the participation of senior leadership and generate significant savings along with a greater number of medium- or small-impact initiatives.

Exhibit 4

**Accelerated Performance Transformations have a greater number of small- to medium-impact initiatives than typical transformations do.**

**Share of initiatives defined as high, medium, or small impact,** %




## Creating standard operating procedures

If managers are changing common practices and

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workflows to drive improvement, they must codify their new, more efficient processes into organizational standard operating procedures (SOPs). Under pressure, however, many managers fail to take this step. Recognizing this problem, the APT approach specifically calls for them to create a new SOP whenever they change a process. Moreover, it requires companies to appoint and develop change leaders who are familiar with the SOPs and can ensure that they are followed throughout the organization.

### Measuring absolute changes in financial performance

If a performance transformation improves COGS by 5 percent, as predicted, is that reason for cheer? Not necessarily—although many companies now make that mistake. If the 5 percent savings are offset by high inflation, a change in product mix that results in lower sales, or other factors, companies may not achieve their target earnings before interest, taxes, depreciation, and amortization (EBITDA). For better results, companies could use APT to shift their financial focus and closely monitor progress toward their bottom-line goals.

#### Focusing on financials

Unlike typical performance transformations, APT requires managers to consider all forces that affect their financials, not just savings from cost-improvement initiatives. In fact, one of its primary goals is to set clear guidelines that specify how companies should account for changes in product mix, volume, or inflation as well as unexpected headwinds or tailwinds. By considering such factors, they will always understand their true performance.

Consider the case of an industrial company that achieved substantial EBITDA improvements during the early stages of a transformation. Managers lauded this change, but deeper investigation revealed that the company was primarily benefiting from two unexpected tailwinds: volatile prices in raw-material procurement and temporary changes in the product mix that increased profits, at least over the short term.

With a greater understanding of the factors that affect progress toward target EBITDA, companies are more likely to detect problems and take corrective action quickly. Since APT helps identify a company's full potential at the outset of a transformation through you-to-you benchmarking, managers should already have a good idea where they might find additional opportunities, even if they encounter unexpected headwinds or other complications.

#### Closely monitoring progress

During a typical transformation, managers are juggling multiple tasks. In the rush of duties, they may spend little time examining data or may just look at metrics related to current performance, rather than those that are useful in forecasting future outcomes. Lacking a clear process for monitoring progress, managers may overlook problems until they escalate.

Under APT, managers must ensure that all activities link to P&L metrics. At the function level, companies should define a consistent set of key performance indicators for all groups. They should also review spending every month, examining, for example, the productivity and overtime for manufacturing labor and the utilization and overtime for field technicians. Within departments, leaders must review metrics daily. To complement this oversight, top executives should conduct regular progress reviews, sometimes taking a deep dive into particular initiatives.

At one industrial company, manufacturing supervisors had difficulty understanding both true performance and costs within their group. Their confusion arose because baseline spending was unclear, even when they looked at leading indicators such as productivity and on-time job completion. To gain greater clarity, the managers began reviewing plant staffing, including the spending on temporary workers and overtime, on a daily or per-shift basis. This oversight gave the company much greater clarity about costs.

## Driving a coordinated path to execution

Although an APT is shorter than a typical transformation, it is more difficult to coordinate. Since the transformation proceeds more rapidly, slight missteps could send the project irrevocably off course. To drive a coordinated path, leaders must focus on creating a vision, focusing on sustainability, and shifting mind-sets. These activities are familiar to anyone who has ever led a transformation, but they have an increased urgency in APT and sometimes take slightly different forms.

### Creating a vision

Here's the ideal: leaders create an inspirational vision for their performance transformation that rallies support across functions. All groups remain united behind the common goals until the vision becomes a reality. Progress is swift because employees understand their roles and believe in the transformation's purpose.

In reality, however, leaders often fail to communicate clear objectives. Employees may be aware that their company is attempting to cut costs, but they do not see the big picture or appreciate the transformation's goals. Some may even fear change, believing that cost-cutting efforts will eventually translate into widespread layoffs. Any initial enthusiasm for the transformation program quickly wanes, especially if leaders are slow to address unexpected roadblocks.

During a fast-paced APT, the need for a common vision is even more critical. Leaders must be extremely clear about their goals and help employees understand that the transformation is about much more than cost reduction. And their role does not end after APT launch. Throughout the transformation, they will need to reiterate the vision's importance to keep people on the same page. If groups or individuals are making significant contributions toward the transformation, they should receive public praise. And if the transformation appears to be going off track, leaders must quickly make organizational changes. If a team is moving slowly, for instance, leaders should consider changing its composition

### Ensuring sustainability

Once a transformation is complete, attention turns to other issues—and that can make it challenging to sustain impact. Over the years, leaders may retire or move to new roles, the economy may shift, or technologic advances may make familiar work processes obsolete. Many companies fail to prepare for such changes and lose any momentum that they gained during the early days of their transformations. Others have trouble sustaining progress because they have inadequate incentives to keep employees motivated over the long term.

A packaging manufacturer addressed these issues by identifying up-and-coming employees who could potentially take the reins if current leaders shifted into different roles. It gave the most promising employees responsibility for some major transformation tasks to build their competence. The company also created long-term incentives tied to financial goals for all employees, a practice that continued well after the transformation ended.

**Changing mind-sets**

In any transformation, leadership emphasizes the importance of mind-set shifts. If employees do not believe that new strategies are appropriate, the theory goes, they will only put in a half-hearted effort. But companies often devote little attention to cultural change. Although they may discuss the power of transformation and the importance of change, their efforts extend little beyond a discussion of buzzwords. Thus many employees, including the middle managers and other staff charged with leading the effort, tend to fall back on entrenched beliefs and attitudes.

To address this, one consumer-electronics manufacturer undergoing an APT appointed "change agents" to act as role models at the line, site, and regional levels. These employees actively embraced the new ways of working, which helped encourage others to follow suit.

Companies can also promote a change in mind-set by rewarding employees who help reduce costs, increase productivity, or otherwise enhance the bottom line.

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For many companies, performance transformation is not a choice but a necessity. But when it comes to how they carry out a transformation, they have options: they can continue repeating their past mistakes and barely move the needle on the bottom line, or they can consider the APT approach, which may take them closer to their financial goals. An APT requires just as much effort as a traditional transformation does, even though it is shorter, but the results may be far superior to anything that companies have achieved in the past.

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