Discussion Board Articles Year 2003

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All of the articles posted to the Financial Management Discussion Board during the year 2003 have been compiled within this document. Visit the Financial Management Discussion Board each month for a new article. The Financial Management Discussion Board is located on the internet at www.exinfm.com/board/board.html.

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The VDF Tool

One of the major challenges facing strategic planners is to bridge the gap between strategizing and building a performance measurement system (Balanced Scorecard). Despite attempts to bridge this gap, strategic thinking is often isolated or apart from those who develop measurement systems such as the Balanced Scorecard. In an effort to close this gap, we can focus on assets; i.e. identify those assets that we must develop for meeting strategic goals and objectives.

Similar to how the structure of a balanced scorecard allows us to reframe strategy into four or five perspectives, we can structure our strategic assets into a framework known as the Value Dynamics Framework (VDF). VDF is an organized approach to categorizing all assets that are required for strategic execution. Assets can fall into several categories, such as the following:

- Physical Assets such as inventory, facilities, equipment, vehicles, etc.
- Customer Assets such as strategic partners, suppliers, distributors, and other assets needed to service customers.
- Organizational Assets such as employees, executives, board members, organizational structures, culture, processes, reputation, etc.
- Financial Assets such as cash flow, revenues, debt, equity, and other financial resources needed for the strategy.

In his article, "Putting Strategy into the Balanced Scorecard"[1], Peter Brewer outlines four steps to building the VDF:

1. Identify the assets you will need to execute your strategy.
2. Map your assets into a framework, making sure everything relates to one another resulting in one cohesive model.
3. Do SWOT (Strengths, Weaknesses, Opportunities, Threats) Analysis of your VDF - make sure it works against the current competitive environment.
4. Connect critical success factors in the strategy to the assets within the VDF.

Once we have the VDF established, we can now select the appropriate measurements for the Balanced Scorecard. Measurement selection becomes easy since assets are the focal point of measurement. Therefore, the VDF Tool connects assets that drive strategy to measurements that populate the Balanced Scorecard.

Arthur Andersen, once a major accounting firm, has described the VDF Tool as a means of "cracking the value code."

[1] Putting Strategy into the Balanced Scorecard, Strategic Finance Magazine, January 2002

> “ . . companies in today’s superheated economies are in a race to discover the underlying code of value creation. That is, they are trying to find out which combination of assets – tangible and intangible – create the greatest economic value and to avoid those combinations that destroy it. How do companies create value today? Our answer: To succeed, they need to see what matters – all of the assets contributing to value creation.”
>
> - Cracking the Value Code by Richard E.S. Boulton, Barry D. Libert, and Steve M. Samek

By using the VDF Tool, we can help ensure that we invest in those assets that have the biggest strategic impact. Once we know where to invest, we can budget our resources accordingly. This in turn links our budgets to our strategy, something that often escapes the strategic process. Overall, the VDF Tool can be a powerful technique for exposing those assets that require major emphasis for value creation.

Humanizing the Financial Mindset

Financial Statements, Organizational Charts, Employee Handbooks, and all those traditional things that go into running the business are increasingly unreliable, out-of-date, and ineffective in a world driven by human and intellectual capital. If leaders of organizations are honest about high performance and creating value, then they must pay close attention to the human side of running the business.

> "Unleashing Intellectual Capital . . is about the power of unmanagement. It is grounded on the inherent genetic tendencies of human beings, which have so far been almost totally ignored by business and other social institutions."
>
> - Unleashing Intellectual Capital by Charles Ehin

For people in finance, it can be particularly challenging to "humanize" since business finance is so driven by numbers and shareholder value. In his book The End of Shareholder Value, Allan A. Kennedy contends that too much emphasis on shareholder value has led many companies to mortgage their futures away by doing short-term things (such as reorganizations) to boost shareholder value, but in the long-run, such tactics end up destroying value.

> "Effective organizations possess a supply of employees willing and able to make contributions to organizational success. Organizational restructuring should emphasize the most effective application of human resources to accomplish the organization's mission."
>
> - Organizational Learning, Performance, and Change by Jerry W. Gilley and Ann May Cunich

Instead of focusing so much on shareholder value, the real focus should be on the relationships a business has with its customers, employees, partners, and other stakeholder groups. By investing in these stakeholder groups, you support those things that lead to higher shareholder value. This argument is well made in the Performance Prism, an alternative measurement model to the Balanced Scorecard; i.e. focus on your stakeholder groups before doing your strategy.

One simple approach to humanizing the financial function is to express financial metrics in relation to stakeholder groups. For example, we can "humanize" Economic Value Added (EVA) by expressing it per employee:

> Value Added Employee (VAE) = EVA / Full Time Equivalent Employees
>
> VAE has been popularized by Metric Performance (www.metricperformance.com), not unlike how Stern Stewart popularized EVA.

But we need to go beyond financial human metrics like VAE and focus on those things that enhance Human Resource (HR) Capital. In their book The Value Added Employee, Edward J. Cripe and Richard S. Mansfield outline three simple steps for increasing HR Capital:

1. Increase the number of high performers in the workforce. A combination of competency testing and performance evaluations are used to distinguish high performers from low performers.
2. Actively recruit high performers for building the organization.
3. Reduce or improve low performers in the workforce.

If people are the foundation behind performance and the goal is to increase shareholder value, then the real question to ask is: How do we secure a future for all of our stakeholders? A narrow focus on shareholders only has led us to witness the so-called bubble (overvaluations of publicly traded companies) and the subsequent market collapse.

> " . . leadership is all about people, and if you're going to lead people you have to care about them."
>
> - Encouraging the Heart: A Leaders Guide to Rewarding and Recognizing Others by James M. Kouzes and Barry Z. Posner

In conclusion, financial leadership requires an emphasis on those things that matter to people. Leaders need to be asking questions like: How do we build our business around the human resources of the company, what organizational structure best serves all stakeholders, and how do we improve how we manage our human resources. Those organizations that are overly pre-occupied with financial results only will be less profitable in the long run than those organizations that cater to building their human resource capital.

> "Despite all the change swirling around any successful business, some things appear to remain constant for relatively long periods of time. Foremost is that business needs people to make it function, and people inevitably leave their mark upon it."
>
> - The End of Shareholder Value: Corporations at the Crossroads by Allan A. Kennedy

SWOT the Baldrige Way

Assessing your organization on a regular basis is a pre-requisite to strategic planning. One of the most widely accepted approaches for assessing strength's, weaknesses, opportunities, and threats (SWOT) is the Malcolm Baldridge Model. The Baldridge Model provides a structure for measuring and assessing organizational excellence by assigning points to various categories:

2000 Baldridge Template for SWOT Assessment
Leadership (125 points)
Organizational Leadership
Corporate Responsibility
Strategic Planning (85 points)
Strategic Development
Strategy Deployment
Customer and Market Focus (85 points)
Customer and Market Knowledge
Customer Satisfaction and Relationships
Information and Analysis (85 points)
Measures of Organizational Performance
Analysis of Organizational Performance
Human Resource Focus (85 points)
Work Systems
Employee Education, Training, and Development
Employee Well Being and Satisfaction
Process Management (85 points)
Product and Service Processes
Support Processes
Supplier and Partnering Processes
Business Results (450 points)
Customer Focused Results
Financial and Market Results
Human Resource Results
Supplier and Partner Results
Organizational Effectiveness Results

Let's quickly review the above template:

Leadership – An organization must have direction and guidance from an overall leadership system. Leadership systems include a balanced and strong executive management team, an effective organizational structure, and other attributes that allow the organization to move quickly without over-reliance on one single leader (such as the Chief Executive Officer).
Strategic Planning – Strategizing must be an integral part of the business and strategic planning drives much of what happens. Additionally, strategic planning has a quick turnaround; i.e. people spend most of their time trying to execute strategies as opposed to developing strategies.
Customer and Market Focus – You must clearly identify your customer and understand the marketplace. Customer requirements and their satisfaction are critical, but you must go beyond this and build customer alliances and relationships for customer retention.

Information and Analysis – You must collect quality data and transform it for timely and effective decision-making. A performance measurement system (such as the Balanced Scorecard) and competitive intelligence are two primary components behind information and analysis.
Human Resource Focus – An overall human resource management system must be in place for maximizing human resource capital. This can include numerous components – hiring practices, compensation plans, recruiting, job design, reward / recognition programs, training, safety, and employee satisfaction.
Process Management – Products and services require various business processes. Numerous issues must be properly managed: Supply chain efficiency, consistency in delivery of products / services, quality improvement, control over defects / complaints, performance measurement, etc.
Business Results – The final category within the Baldridge Model are the results of the business. This is "proof positive" that you are successfully executing on the other six categories and as a result, almost half the points are assigned to this category.

The Baldridge Model has received worldwide acceptance as a means for gauging the health of an organization. Using the Baldridge Model as part of your strategic planning process is often considered a "best practice" in strategizing. You can also expand your analysis for more detail audits, leading to compliance with ISO standards.

Finally, the Baldridge Model may not cover all the information you need to properly assess your organization. For example, intellectual capital (culture, technology, knowledge, brand recognition, etc.) is becoming increasingly important. Don't forget to include these critical areas in your SWOT analysis.

> Note: You can download Assessment Templates for applying the Baldridge Quality Model. Go to www.exinfm.com/training and download the supplemental material for Short Course 10. Case studies can be downloaded from www.baldrigeplus.com/eight.htm. Also visit www.efqm.org to download the EFQM Excellence Model.

Focusing on the Process (Part 1)

All businesses require processes for the creation of products and services. A process is a collection of activities that consumes resources and adds value to the consumer (in the form of products / services) with some form of benefit paid to the producer. Additionally, all processes have variation – in business we call this risk. As H. Edward Deming, pioneer in the field of quality management, points out – If you can better understand variation in a process, then you can plan for it and do things to prevent it.

Unfortunately, there is a viewpoint that people may represent the source of problems for most business processes. A much better approach is to understand how people and their activities fit within the process. Processes tend to superimpose control over people and in today's entrepreneurial world, no-one wants to be controlled. Therefore, by focusing on the process, as opposed to looking at people as the source of the problem, we unleash the human capabilities of the organization. Too often, management is working to change people when it should focus more on changing the process which in turn leads to positive change on people. Additionally, when you focus on the process, you switch over from short-term bottom line thinking to quality, customer driven thinking. This is a much more sustainable approach to real long-term growth and profitability.

By focusing on the process, you will:

- Better focus on the customer
- Improve competitive position through quality and service
- Gain insight into how errors are introduced into the business leading to preventative measures for improvement and elimination of error correction activities (such as Six Sigma)

Managing a process begins with a very detail understanding of how the process works. This may require organizing the company for process improvement – appointing team leaders, investing in training, and running pilot programs on critical processes. One simple way to understand a process is to flow the process using a block diagram. Block diagrams provide simple visual flows of what takes place within the process. Once you understand how a process works, the next step is to make it efficient. This usually requires an emphasis on reducing errors and defects that occur within the process. Additionally, removing barriers within a process is a common way of empowering people and improving the process.

> "We are spending all of our time saying: 'I'm sorry, I'll fix it', to customers who are increasingly sophisticated and understandably impatient. What we should be doing is developing processes that will make it unnecessary to ever apologize for inadequacies."

- Business Process Improvement: The Breakthrough Strategy for Total Quality, Productivity, and Competitiveness by H. James Harrington

Another common attribute of process management is measurement of the process. Common measurements for a process include resource consumptions per unit, cycle times, wait times, and % value added per unit. Reducing time related measurement's is often a goal behind process improvement. This may require additional automation and upgrading of technologies.

Many managers seem to equate process improvement projects in relation to costs. Unfortunately, many managers never evaluate a process in relation to quality, they always jump to the question: How much is it going to cost? Therefore, managers need to understand the relationship between quality and costs. Quality and costs go hand in hand for process management. By improving quality, costs naturally come down.

> "With better quality and lower costs, you can capture the market." – H. Edward Deming, leading advocate of quality management

Finally, instead of forcing people to fit with the process, try changing the process to fit with the needs of stakeholders involved in the process. This usually requires "reengineering" the process. Part 2 of this article will outline the foundation behind process reengineering and the importance of involving all stakeholders within the process.

Focusing on the Process (Part 2)

The words "business process reengineering" still leaves a negative impression to many of us in the business world. Years ago companies rushed to reengineer their processes to improve quality and efficiency. However, the end result was less than desirable – new processes were layered on top of existing processes resulting in more work with fewer people. Costs were temporarily lowered benefiting investors. However, other stakeholders in the process, such as employees, were victimized by reengineering.

Real reengineering is more about including everyone involved, so that there are no losers and winners from reengineering. The words collaboration, connecting all players, more transparency, and more openness are now part of the reengineering vocabulary. The buzzword for this new or real approach to reengineering is X Engineering. The "x" refers to crossing; i.e. reengineering must cut across all organizational boundaries. Author and consultant James Champy pioneered this more human approach to reengineering in his book: X Engineering the Corporation. Author and e-commerce expert Thomas Koulopoulos refers to this as the x-factor, creating communities whereby people can collaborate.

"X engineering is about optimizing relationships so that companies can tap the full sum of the intelligence and experience of all of the people in its network of customers, suppliers, and partners. To accomplish this goal, the processes in which these people participate must be arranged to work smoothly both within an organization and between the organization and its customers, suppliers, and partners."
X Engineering the Corporation by James Champy

Processes are no longer tightly controlled and restricted from view. Processes are now easily accessed over the internet. If a process is performed in isolation from others, then management must determine if the process is really isolated. How do we open it up to outsiders so that we can improve it and lower its costs? Are we leveraging technology to transform this process?

One obvious obstacle to x-engineering is resistance. Many partners may not want open-up and change; they will refuse to share information. The challenge for management is to break through this deadlock by deploying a single, standard process that allows everyone to work together seamlessly. One reason this is so important is because customers are increasingly sophisticated and demanding. In order to properly serve the customer, everything within the supply chain must be connected and coordinated. Everyone takes ownership, assuming specific responsibilities for making sure their part of the process is managed flawlessly. Supply Chain Management (SCM) now evolves into Supply Chain Relationships (SCR). And we can compliment these processes with Customer Relations Management (CRM) and Employee Relations Management (ERM).

The reasons behind reengineering remain the same – increased competition, the need to improve customer service, the need to lower costs, and the need to keep up with technology. However, the significance of these drivers is becoming more demanding. As a consequence, many companies are becoming exhausted, run-down and giving up on these incredible demands to reengineer the business. However, instead of admitting defeat, management should view these challenges as new opportunities. And by connecting all players through technology, real reengineering (or x-engineering) can become a real value-adding proposition. It will require a new mindset whereby management is openly sharing their processes with others in a way that allows reengineering to take place for the benefit of everyone. And with technologies like the internet, there is no excuse for not making it happen.

Let’s Define Best Practices

One of the most overused terms in business has to be: Best Practices. It seems everyone (including myself) is always labeling something as a “best practice.” Thanks to Hackett Benchmarking, a common definition has emerged for best practices. According to Hackett Benchmarking, a best practice must:

1) Place the company in a top percentile ranking within its industry.
2) Leverage and take advantage of technology.
3) Improve quality and speed, and also lower costs.
4) Give management more control and influence.
5) And finally, it has to be working; i.e. it can’t be planned but not implemented.

If you can measure up to these five standards, then you can truly boast about a best practice. And the benefits of having such a best practice will separate your company from the rest of the competition.

What makes this so appealing is that the gap between average performing companies and best in class companies is widening. According to Hackett Benchmarking, once a company has met the five standards for a best practice, it begins to pull away from the competition as it becomes easier to initiate improvements while average companies continue to struggle with process improvement programs. Making improvements without measuring up to best practice standards is like being in a row boat race. The best practice rowboat keeps moving ahead while you try to catch up at a slower rate of speed.

A good example of this is the financial analysis function. According to Hackett Benchmarking, average performing companies spend about half their time collecting data for analysis and the other half of their time actually analyzing it. Companies with best practices spend about 13% of their time collecting data for analysis and the remaining 87% analyzing and producing high quality information for decision-making. Therefore, the gaps between average and best practices can be significant.

Many companies that are considered best in class often follow similar strategies. For example, using one single standard throughout the entire organization seems to be a recurring theme. In the case of Enterprise Resource Planning (ERP), most organizations force fit many of their processes to the ERP application, thereby achieving standardization, consistency, and lower costs.

Another common theme is the use of self-service for both internal and external customers. Once again, technology plays a central role behind this best practice. Examples include having employees (internal customers) administer their own benefits through a web based application and having outside customers resolve their questions through another web based application.

Therefore, many best practices seem to strive for things like consistency, standardization, simplifying the process, zero redundancies, leveraging technology, single source for all data, and moving processes over to the internet. Finally, don’t get discouraged – only a few companies can measure up to best in class. Now that you understand what it is and why it is important, you can begin your journey from average performance to best practices.

Learning to Think

It has been said that everyone must possess three transferable skills – the ability to speak, the ability to write, and the ability to think. The most elusive of these three is probably the ability to think. Unfortunately, many organizations prevent people from thinking. For example, a lack of consistent standards throughout the entire organization may contribute to wide variations in results, making it difficult for people to make the right decisions. Many companies are plagued with compliance type thinking; i.e. people "go along" with decisions to avoid retribution, not challenging the bad decisions that are about to be launched. Instead, we need a simple and consistent framework for decision-making that allows everyone to think the way they need to think. In their landmark book BusinessThink, Dave Marcum, Steve Smith, and Mahan Khalsa have outlined eight standards that define a common framework for organizational thinking. Here are some quick excerpts:

1. Stop rushing to implement solution after solution. Instead, focus on the real sources of the problem so that results, not some solution unfolds. For example, make sure you define the problem accurately before launching some major project.
2. Make sure you have hard evidence that a problem really exists. For example, you may want to measure the issue just to substantiate the problem and determine the extent of the problem.
3. Don't forget to quantify your solution through some form of analysis such as a business case that considers all the angles. The true costs of launching a solution may exceed the costs of simply ignoring the problem.
4. Get to the root cause of the problem. Many companies put out fires or plug leaks in the organization without drilling down to the source. Eliminate the source and stop treating the symptoms.
5. Allow people to explore and let them be "nosey" into things that may not be their business. By giving people this opportunity to make inquiries into new things, change becomes easier to implement for the organization. In fact, by letting people penetrate new territories, you open up more possibilities, leading to change.

"Those who get curious often get it right – no matter what – and this leads to tangible competitive advantage." – BusinessThink by Dave Marcum, Steve Smith, and Mahan Khalsa

Thinking is about understanding people and removing organizational impediments that force people to act and behave outside their norm. Thinking is about equalizing everyone so that it no longer matters where the idea comes from, just as long as we get the right idea. Thinking is about going through some form of due diligence before committing organizational resources.

Too often organizations resist these "reality checks" because of management egos. And according to Jim Collins, author of Good to Great, management egos are one of the single biggest reasons that good companies never make it to great.

At a time when most businesses are struggling and failing, and at time when more and more people are becoming increasingly independent and entrepreneurial in their thinking, the time has arrived for all organizations to learn to think. Organizations must put people in charge within a single and simple framework that makes good business sense. And by making this framework for decision-making simple, people will be able to execute.

Sustainable Business Models

Long-term survival of any organization requires successful execution of strategies that secure or "lock-in" elements of sustainability. Unfortunately, not all organizations have made the distinction between sustainable strategies vs. short-term tactics that undermine sustainability. For example, the business model of amazon.com is somewhat predicated on becoming the lowest cost provider of books and CD's. In order to grow the business and make a profit, amazon must continuously increase volumes. This approach to strategy is not sustainable since it chases a lower and lower profit margin while at the same time, amazon must desperately try to make-up for the loss through higher volumes. A sustainable strategy tends to "lock-in" a company's future by doing things that don't exhaust the company, but set it apart from the competition. Hanging your strategy on easy to duplicate tactics such as lower costs usually doesn't work since the barriers to competitors are minimal.

Contrast this to a company that hangs its strategy on strong relationships with its customers, building loyalty and retaining existing customers. This "customer relationship" approach does a much better job of securing a company's long-term future. Therefore, elements of sustainability tend to be harder to execute on, but have much more lasting and enduring effects, adding to a company's long-term survivability.

Another important element of sustainability is branding of the business. As competition increases, it becomes increasingly difficult to get the attention of the customer. Therefore, strategic branding is now very important to many businesses. Without name recognition in the marketplace, holding on to market share is considerably difficult.

Perhaps the single most important element of sustainability is the ability of the organization to change. An organization must adopt and move with changes in the marketplace. When a company can react and suddenly run in a different strategic direction without significant lead-time, then it has a much higher chance of prospering within the changing marketplace. For example, years ago Microsoft dismissed the internet as insignificant. However, once Microsoft realized that the internet was the future, the company adopted to marketplace changes and responded quickly by changing its overall strategy. What makes this remarkable is that Microsoft is no small company – it was able to shift suddenly, becoming a leader of internet technology. This type of fast strategic redirection is truly one of the key elements of sustainability. Afterall, strategy is conditional on other things happening. And if what you think doesn't happen, then you have to move quickly in a new direction.

This article has touched on three elements of sustainability – customer relationships, strategic branding, and the ability of the organization to change. Each organization is unique and elements of sustainability will vary from organization to organization. The common theme behind sustainability is to secure a future through strategies that move a company away from the competition; i.e. competitive advantages that are difficult for others to replicate. Too often companies make decisions that undermine their sustainability – cutting costs in areas like research, marketing, and product development or embracing strategies that are easy for competitors to duplicate. Sustainability is more about making "value" decisions that are right for all stakeholders over the long run and carefully observing trends and changes in the marketplace, giving the company insights into how it can outlast the competition.

Comprehending the IT Challenge

For too long, finance has misunderstood and failed to comprehend the true costs and resources required for many IT (information technology) projects. Issues such as migration and integration are simply pushed off to the IT Department to handle. The two functions (finance and IT) struggle against one another. Additionally, finance does not define its role in relation to IT and vice versa; i.e. there needs to be a marriage of strategies. Likewise, some IT projects continue unabated with no supporting value analysis, leading to unacceptable ROI's (Return on Investment). According to Gardner Group, 51% of all IT projects go over-budget by more than 200%.

Since IT is a significant part of a company's strategy and a major driver for best practices, Finance needs to fully grasp the role and strategies of IT. One good starting point is to find solutions that fit with both (Finance and IT) strategies. A fully integrated and seamless end-to-end suite for running the business may provide a solution that fits well with both Finance and IT. For example, many organizations are fragmented with different business units and departments each running their own applications. The end result is a desperate mix of applications and platforms, contributing to enormous bottlenecks in information flow, redundant activities, increased costs, less control over data, and paralysis for the organization when it is forced to change its business model or scale up due to growth. And to compound matters, with each new release of an application, the migration difficulties grow making the IT challenge increasingly difficult.

Desperate Applications and Systems:

Human Resources => PeopleSoft
Financials => SAP
Budgeting => Microsoft Excel
Inventory => Microsoft Access
Customer Relations Management => Siebel
Supply Chain Management => i2
Business Intelligence => Cognos
Web Services => BAE Systems
Directories => Novell
Portals => Plumtree

Suppose we could take this entire mess and put it into one single platform where scalability and integration were built into a single suite of products. Instead of a patchwork of desperate solutions where everyone is doing their own thing, we pull every part of the business together into one system and put a single IT strategy in place that works for everyone. Additionally, we no longer view Enterprise Resource Planning as another IT project, it is now viewed as a rapid business transformation project for removing the enormous disparities that are strangling the company.

What throws a monkey wrench into this whole equation is when management initiates a project that creates disparity, such as a merger and acquisition or a reengineering project. And at the same time, Finance has failed to fully grasp the true costs of desperate systems and how it impacts negatively on the company. Therefore, the Non-IT parts of the business need to comprehend the IT Challenge of trying to turn apples into oranges because of disparity. Turning apples into oranges is not how data should be managed and from an IT perspective, the management of data is how the company gains its competitive advantage.

Now that we understand the disparity issue and its ramifications, let's discuss another common issue confronting almost every IT project – time. In his book Good to Great, author Jim Collins examined all Fortune 500 companies and found that a mere 11 could be classified as "great." One of the most significant drivers for moving a company into the "great" category was time. Great companies took their time, showing high levels of persistence and patience with major initiatives such as IT projects. Contrast this to most companies where there is a mad rush to put some quick solution or patch in place that buys a little more time. Great companies are careful and prudent in making sure technology really fits with the values, strategies, and competencies of the organization over the long run and not the short run.

Collins also points out that great companies use technology (such as Enterprise Resource Planning) to accelerate transformation and not to reinvent the company. IT projects are viewed as complementary to the strategies of the organization and not the essence of the strategy itself. The core values (leadership, customer relationships, innovative products, strategic partners, etc.) that drive the organization have little to do with technology. They have more to do with people and processes with technology as an enhancer or tool to assist with execution.

"The good-to-great companies never began their transitions with pioneering technology, for the simple reason that you cannot make good use of technology until you know which technologies are relevant." – Good to Great by Jim Collins

In conclusion, it's high time for Finance and other management functions to fully understand the real costs associated with desperate systems. Moving to one fully integrated suite of products may not please different departments, but it will have profound positive impacts on improving efficiencies and saving costs on an enterprise wide basis. Finally, don't forget that "great" companies have never viewed technology as the roadmap to reinventing the company. And great companies have always allowed "time" to work in their favor by giving people the flexibility to revisit the entire life cycle of IT – working through continuous iterations until IT really begins to work and mesh with value creation for the organization.

Leveraging Knowledge Management

It is ironic that so many companies have an abundance of knowledge, but fail to use it for managing the business. Knowledge is a critical resource that warrants much more attention. If we are serious about managing knowledge, then we need to embrace the concepts associated with knowledge management.

"Businesses, especially large ones, have little choice but to become information-based. To remain competitive, maybe even to survive, businesses will have to convert themselves into organizations of knowledge specialist." – The Coming of the New Organization by Peter F. Drucker

Knowledge Management is the process of pulling together people, systems and tools so that an enterprise wide structure is in place for efficient and effective decision making. Unfortunately, many companies view knowledge management as an IT project, trying to move information from one location to another. Although technology does play a role, knowledge management is more about understanding the resource and knowing how to leverage it for growing the business. And yes, technology (such as enterprise portals) is often deployed to help leverage knowledge. However, it may be more important to focus on the information itself – knowing how to classify it and analyze it before you give everyone access to it.

A much better approach to knowledge management is to clearly understand the intellectual assets of the business. This can include simple things like getting more out of databases (a common repository of information) or looking at strategic issues like properly identifying intellectual assets and understanding how they impact the business. The goal is to put the "whole brain" of the organization to work, getting all parts of the body connected and working together for driving performance. This usually requires some form of gap analysis – looking for gaps in your knowledge assets, building knowledge to fill in these gaps, and making sure you are using the knowledge that you currently have.

"Ultimately, intellectual assets have become more important than any other because only by means of knowledge can companies differentiate their work from their competitors."
- The Wealth of Knowledge by Thomas A. Stewart

As author Peter Senge points out in his book The Fifth Discipline, learning organizations are always expanding their knowledge, finding new ways of creating knowledge, moving it seamlessly throughout the organization and transforming it so that people have insights into what they need to do. This requires a knowledge infrastructure, comprised of numerous components such as databases, libraries, internal experts, research centers, outside information brokers, and other knowledge-based sources for plugging the knowledge gaps within the organization. It also requires measuring and managing the value of knowledge so that it truly fits within the organization. Many companies have created Chief Knowledge Officers or Chief Learning Officers to help propel this process.

Leveraging knowledge management requires much more than moving the stuff around through Lotus Notes. It's about having a culture and infrastructure that supports the knowledge needs of the organization. This requires strong leadership, unlearning of old ways, an openness to new possibilities, promotion of learning, and very seamless communication on an enterprise wide level. This also requires a willingness to learn from others regardless of who they are; i.e. you must be willing to face the truth if you expect to leverage knowledge. In essence, knowledge management is about finding the best ways of running the business. And in order to accomplish this, you must be willing to learn and use your newfound knowledge in new ways for managing the organization. If a company isn't managing its knowledge, then it isn't managing its business.

"All healthy organizations generate and use knowledge. As organizations interact with their environments, they absorb information, turn it into knowledge, and take action based on it in combination with their experiences, values, and internal rules. They sense and respond. Without knowledge, an organization could not organize itself; it would be unable to maintain itself as a functioning enterprise."

Working Knowledge: How Organizations Manage What They Know by Thomas H. Davenport and Laurence Prusak

Elevating the HR Function (Part 1 of 2)

Organizational capabilities are developed primarily through the development of human resources. Despite the enormous importance of human resources, many organizations treat the HR (Human Resource) Function as just another administrative function with high overhead costs. As a result, the HR Function is often targeted for outsourcing and downsizing; crippling it from its real potential for value-creation within the organization.

Instead of viewing HR as a necessary administrative function, it's high time for all organizations to recognize that the real challenge for Human Resource Management is to lead the way on several strategic fronts - development of formal systems for creating a "learning" organization, effective deployment of human resources for maximum return to the company, and enhancing the competencies of the workforce. Senior Management should take a much broader and strategic view of the HR Function, using it to maintain or create new competitive advantages for the organization. Ultimately, the HR Function should be a major strategic player in how the organization executes its overall strategic plan.

"It has become increasingly clear that human resources (HR) in the future must operate strategically – not as the current 'partner in business', but as a business in and of itself. There are a number of critical reasons to move in this direction, not the least of which is that it may be the only way HR can take control of its own future."
- <u>Tomorrow's HR Management</u>, Edited by Dave Ulrick, Michael R. Losey, and Gerry Lake

In order for HR Management to become more strategic, it will have to reduce the administrative, paperwork that holds HR back. For example, things like virtual services - having employees doing their own training through e-learning or changing their benefits on-line will be the wave of the future, allowing HR to move away from pushing paper and doing more consultation type work.

Several factors are forcing change on the HR Function:
New technologies (such as on-line time sheets)
Competitive forces
Organizational changes (such as changes in management, strategy, etc.)
Increased pressure on HR to deliver services at lowest costs
New challenges on HR to address strategic outcomes that impact the business

These factors and more will drive a major transformation in how HR will work. According to Ernst and Young, today's HR will contrast sharply with tomorrow's HR:

Today's HR Function	Tomorrow's HR Function
70% transaction processing 30% strategic initiatives	30% transaction processing, 70% strategic initiatives

“The reason I think that strategic planning is important is simple. I have worked directly or through associate for more than five hundred companies in the thirty-two years that I have been a personnel consultant. Approximately two hundred of these companies were my direct accounts, so I knew them very well. Every one of these companies engaged in real strategic thinking and strategic planning as a core part of the style of managing has been successful by every measure of enterprise performance as long as they managed in that manner. Every company I have known for more than ten years that has shunned strategic activities in their management processes has failed and is no longer in business. That’s pretty compelling evidence for me.”
- Strategic Planning for Human Resource Management by Robert E. Sibson

If HR is to become strategic, then senior management outside HR must become more open-minded, accepting the critical role of HR in driving organizational performance. Once this new “strategic” imperative is accepted by management, then ideas will flow from HR. For example, many people in HR have good ideas, but they are rarely given serious consideration and commitment from senior level management. Even when HR attempts to launch a major strategic program, HR must go it alone with very tepid support from outside the HR Function. Ironically, many other non-operating functions such as finance and marketing have reinvented themselves into high-level decision support centers, using technology and processes for intelligent, strategic type decision making. It seems the re-invention wave never reached the HR Function, relegating HR to its typical role of administrative tasks – compensation, benefits, pensions, and basic personnel management. Therefore, senior management and HR need to form a strong partnership in making the move to strategic HR management.

“Your firm’s human capital is a form of wealth that will create more wealth. When you enhance the value of your people, you enhance the value of your firm. A person’s value as a human asset stems directly from how his or her knowledge, experience, skills, and competencies match the job in which that person works.”
Valuing People: How Human Capital Can Be Your Strongest Asset by Lisa M. Aldisert

In order to jump-start the strategic process, HR can embark on several “value-based” practices, such as team building, cross-functional development, linking pay to performance, and assessing individual performance. Even the most fundamental issues can be a good source for HR programs – things like effective communication throughout the entire organization. HR can test, monitor and improve various channels of communication, establishing standard guidelines and “best practices” for information sharing.

One compelling argument for making HR more strategic has to do with core competencies. The HR Function needs to place more emphasis on those things related to capabilities and competencies, helping the entire organization reshape itself so it can meet future expectations and demands. If HR fails to address this critical issue, then HR runs the risk of strangling and impeding the development of HR Capital.

HR will need to embrace a much deeper and broader purpose, reaching into new areas such as expanding the knowledge workers and improving the relationships between employees, managers, and customers. Part II of this article will outline more specific initiatives for making HR highly strategic.

"As more organizations have recognized the importance of human capital and knowledge management with respect to competitive success, it is reasonable to expect that HR professionals would be at the forefront of organizational leadership. Yet, to the contrary, the importance of activities performed by HRM units seems to be losing ground in a majority of organizations, while other functional areas (for example, information technology, operations, finance) gain greater and greater influence. It is essential for firms to recognize that people, rather than technologies or process, are best able to sense and make judgments that put structure around the inevitable disorder that results from these forces. Therefore, the knowledge economy, more than any previous market trend, places a premium on human talents. Consequently, the management of a firm's HR, more broadly defined than ever before, will be pivotal in determining the ultimate success or failure of the organization."
- <u>Human Resource Management in the Knowledge Economy</u> by Mark L. Lengnick-Hall and Cynthia A. Lengnick-Hall

Elevating the HR Function (Part 2 of 2)

Part I of this article addressed the issue of elevating the HR Function into a more strategic type function, as opposed to an administrative type function. Part 2 of this article will describe several strategic ideas for moving HR into the strategic function it must become.

In Part I, we mentioned the importance of HR as it relates to core competencies. Organization's need to maintain and build their core competencies since this is the source of competitive advantages in the marketplace. Core competencies have a lot to do with recruiting and retaining the best people. Obviously, HR should play a lead role in this mandate. However, we do not want to stop here since there are numerous other strategic issues related to HR.

"The evidence is unmistakable: HR's emerging strategic potential hinges on the increasingly central role of intangible assets and intellectual capital in today's economy. Sustained, superior business performance requires a firm to continually hone its competitive edge. Traditionally, this effort took the form of industry-level barrier to entry, patent protections, and governmental regulations. But technological change, rapid innovation, and deregulation have largely eliminated those barriers. Because enduring, superior performance now requires flexibility, innovation, and speed to market, competitive advantage today stems primarily from the internal resources and capabilities of individual organizations – including a firm's ability to develop and retain a capable and committed workforce."
<u>The HR Scorecard: Linking People, Strategy, and Performance</u> by Brian E. Becker, Mark A. Huselid, and Dave Ulrich

In his book, Strategic Planning for Human Resource Management, author Robert E. Sibson outlines several critical issues confronting the typical HR Manager:

Productivity improvement
Educational deficiency
Delegative Management
Fairness in the Workplace
Managing Differences
Fair Pay for Everyone
Chronic Labor Shortage
Impact of Technology
Employee Owners (entrepreneurship in the workplace)
Organizational Restructurings for Higher Performance

Each of these areas can represent a major strategic program for the HR Function. An absence of ideas is no excuse for making HR strategic. In his book The Human Equation: Building Profits by Putting People First, author Jeffrey Pfeffer describes seven dimensions that characterize how organizations produce profits through people:

Employment Security
Selective hiring of new personnel
Self-managed teams and decentralized decision making.
Comparatively high compensation contingent upon performance.
Extensive training
Reduced status distinctions and barriers (including dress codes, language, office arrangements, and wage differences).
Extensive sharing of information throughout the organization.

Once again, the sources for strategic initiatives are extremely significant. The obvious problem we will have is how do we address these issues within our typical HR Function. In order to elevate the HR Function so that it can meet these new demands, people within HR will require higher skill sets, including very strong technology type skills since many of the traditional HR services will be conducted through on-line service centers. Additionally, like most high quality functions, HR will need some "independence" from senior management, allowing the HR Function to pursue critical issues in an honest manner.

"The total transformation of Human Resources (HR) as a function has become both a business necessity and a strategic, value-adding opportunity. This transformation, which calls for a functionally fragmented, administrative cost center to a value-adding, integrated organization aligned with corporate business strategies, will not happen incrementally in most cases . . Instead, the true transformation of HR requires analysis and identification of opportunities for improvement in five interrelated areas that are the success drivers of effective HR, including the *people* in HR and their competencies; *processes* used to deliver HR products and services; the *culture* of the HR organization; its *structure* and the *technology* used."
- Web-Based Human Resources: The Technologies and Trends that are Transforming HR
Edited by Alfred J. Walker

All of these strategic issues can be overwhelming to any resource-strapped function. Consequently, HR will need to develop its own strategy for value-creation within the organization; otherwise HR will not adequately address many of these strategic issues and outside managers will continue to have their traditional bias view of HR. The HR Strategy will need to address the issue of how the organization will build its HR Capital (which expands the capabilities of the organization). This can cover a wide range of best practices – web based training, knowledge sharing, 360-degree evaluation processes, cross-functional teams, and so forth. As a minimum, the HR Function must have a strategy for protecting the core competencies of the organization. Next, the HR Function will need to develop strategies for building a knowledge-based workforce that can meet future challenges confronting the organization.

"If competitive success is achieved through people – if the workforce is, indeed, an increasingly important source of competitive advantage – then it is important to build a workforce that has the ability to achieve competitive success and that cannot be readily duplicated by others. Somewhat ironically, the recent trend toward using temporary help, part-time employees, and contract workers, particularly when such people are used in core activities, flies in the face of the changing basis of competitive success. This raises the questions of why these practices seem to be growing, what effects they have on the ability to achieve advantage through people, and what the implications are for organizations that might follow a different strategy."
- <u>Competitive Advantage through People: Unleashing the Power of the Workforce</u> by Jeffrey Pfeffer

In order for HR to be successful with its new strategic mandate, it will need to "in-source" to execute its strategy since its resources are way too limited. For example, direct involvement by IT (Information Technology) will be required to launch new technologies in the HR area. Additionally, HR may have to outsource some of the day-to-day administrative activities so HR can begin to address strategic issues.

In conclusion, some of the most significant performance issues confronting any organization are rooted in human resources. This is why the HR Function needs to become much more strategic. Moving HR into a strategic partnership with management is now mission-critical. There are a multitude of strategic issues for HR to pursue, ranging from making the organization more fluid for the sharing of knowledge to making sure all employees have the tools to provide outstanding customer service.

"In the closing years of the twentieth century, management has come to accept that people, not cash, buildings or equipment, are the critical differentiators of a business enterprise. As we move into the new millennium and find ourselves in a knowledge economy, it is undeniable that people are the profit lever. All the assets of an organization, other than people, are inert. They are passive resources that require human application to generate value. The key to sustaining a profitable company or a healthy economy is the productivity of the workforce, our human capital. In the American economy, where over half of the gross national product is allocated to the information sector, it is obvious that knowledgeable people are the driving force."
<u>The ROI of Human Capital</u> by Jac Fitz-enz