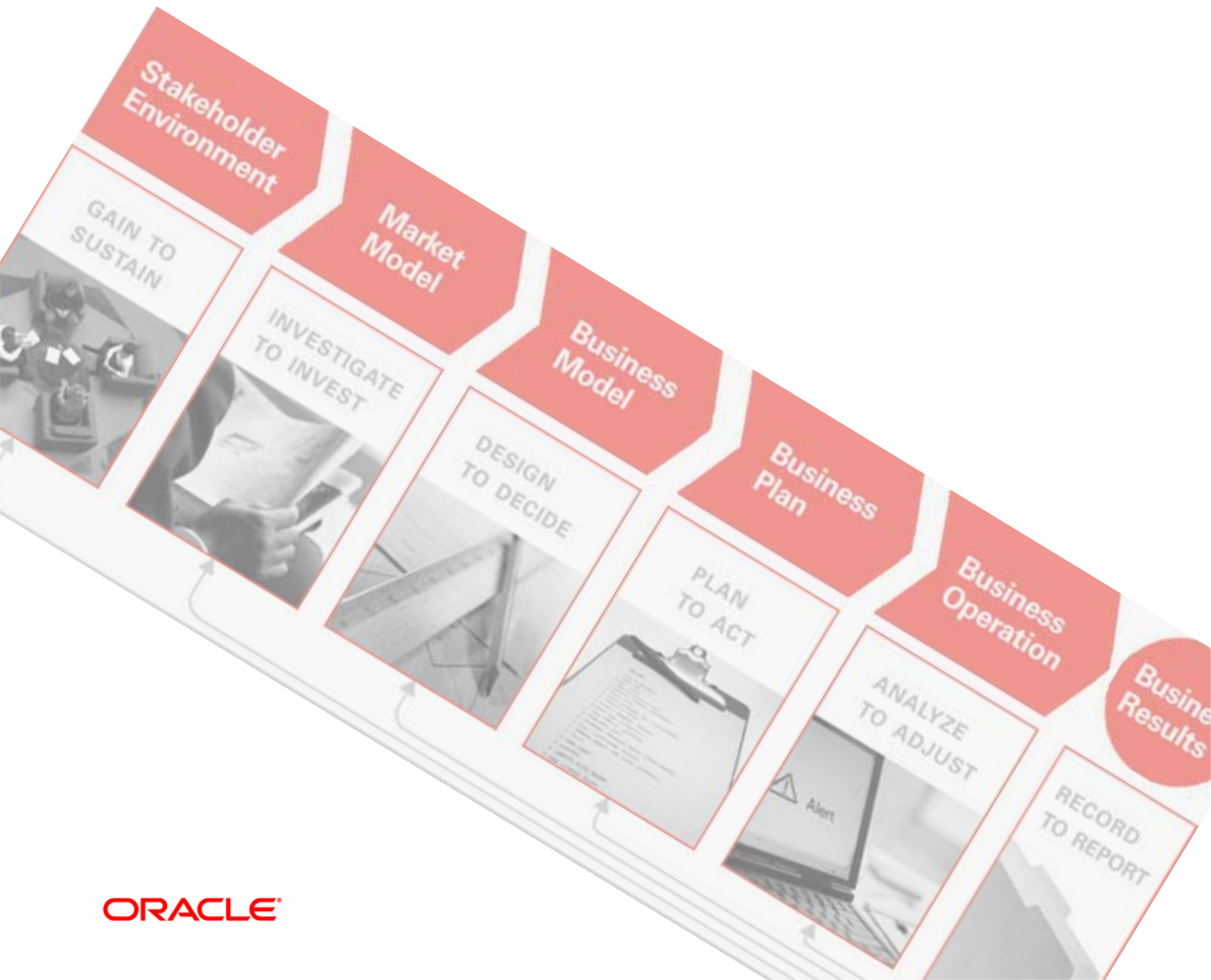


# Journal of Management Excellence

## Introducing Management Excellence

*An Oracle BI and EPM Publication*  
*Issue 1, June 2008*



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## Letter from the Editor



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The *Journal of Management Excellence* is a new quarterly publication from Oracle's Global Business Unit (GBU) for Business Intelligence and Enterprise Performance Management. The journal focuses on thought leadership—that is, everything we, our partners, our customers, and academia do in order to improve a general understanding of performance management and how to move our field of expertise forward. We don't concentrate on products and technology (although I can imagine we would discuss technology trends in general). Instead we focus on what we would like to achieve with performance management: creating management excellence.

The theme of the first issue of the journal is therefore obvious: introducing management excellence. Most business people would be familiar with the concept of operational excellence, but it turns out this is not enough anymore to make a strategic difference. Competitive advantage is no longer achieved by just eliminating cost while improving quality and increasing speed. Competitive advantage comes from being smart, agile, and aligned.

Creating management excellence is the goal of performance management. It has many angles, so the journal will have many topics to address. Although the editorial calendar for the coming quarters is still flexible, themes that come to mind are sustainability, how to organize for performance management, performance management methodologies, and creating business value, etc.

In the GBU, we have always believed in having deep domain expertise. Although I didn't calculate this precisely, a rough estimate shows there must be between 500 and 1,000 man-years of dedicated performance management experience in our team. As impressive as this is, experience only grows by learning. And that is what we would like to achieve with this journal: connecting customers, partners, academia, and Oracle in order to learn from each other.

Our ambition is high. We would like you to not only read the journal, but find it so interesting that you keep it. And send it to all people you think are interested too. Even better, we hope that the content of the journal triggers you to contribute. If you submit an article for the journal, we'll make it worth your while, and compensate you for the effort and time with an appropriate gift. Contact us at [epmgbu\\_ww@oracle.com](mailto:epmgbu_ww@oracle.com).

Best regards, frank

## FROM OPERATIONAL EXCELLENCE TO MANAGEMENT EXCELLENCE<sup>1</sup>

Authors: Thomas Oestreich,  
Frank Buytendijk

In most organizations, business processes such as “order-to-cash,” “procure-to-pay,” “invest-to-retire,” or “develop-to-release” are very well defined. Many have invested millions in business process reengineering projects and implementations of business applications such as enterprise resource planning, customer relationship management, and supply chain management, in order to come to the point where the business processes are clearly understood by everyone and they are reliable, uniform, and predictable.

But what do we call the management process? When we ask this to customers and audiences all around the world, the answer is either silence, or a flurry of different activities and partial processes such as budgeting, financial reporting, resource management, and variance analysis, etc. The closest thing people mention to describe their management process is the PDCA-cycle (Plan, Do, Check, Adjust). This cycle is sometimes also called the planning and control cycle, or management cycle. Sometimes it involves more steps, but it is always based on this principle.

It is concerning, almost scary, that the management processes are not as clearly defined as business processes, as the competitive advantage that organizations can have is increasingly dependent on the management process, instead of business processes. Most organizations have done a terrific job in driving cost out of the process while optimizing the quality of the products and services they offer. Then again, *most* organizations have done that. Operational excellence is not a differentiator anymore; it has become a license to just play. For winning, more is needed. Organizations that make a difference are smart, agile and aligned.

*Smart.* There is no shortage of data about the market, or about your internal operations. The problem is that everyone has access to the same data. The question is how you interpret the data, and what you do with it. In *Competing on Analytics*,<sup>2</sup> Professor Thomas Davenport and Jeanne Harris describe how companies can make

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<sup>1</sup> In a different form, this article was also published in the *Journal of Performance Management*, Spring 2008.

<sup>2</sup> Thomas H. Davenport and Jeanne G. Harris (2007), *Competing on Analytics: The New Science of Winning*, Harvard Business School Press.

a strategic difference by continuously analyzing internal and external data and experimenting on how to improve business operations or customer contacts.

*Agile.* Almost every article or paper starts with stating “in today’s world, business is getting increasingly complex,” or “in today’s world, business pace is increasing at an amazing speed.” Although a cliché, it is true. Globalization has led to competition coming from different regions of the world. Think of the automotive industry, the IT industry, or the steel industry. Competition comes from adjacent markets, for instance cable TV companies competing with the classical telecommunications companies. New technology developments have changed business models. Internet-based applications allow mass customization; customers ordering products and services themselves, while specifying the configuration and options in a detailed way. The organizations most likely to succeed are the ones that are agile and can adapt.

*Aligned.* In *The Future of Work*,<sup>3</sup> Professor Thomas Malone mentions some evidence that despite all the mergers and acquisitions, the average size of organizations has been shrinking. This is mostly due to outsourcing and focusing on core competencies. In order to be successful, organizations throughout the value chain need close collaboration. Also, most innovation today comes from collaboration between companies. Think of Apple and Nike combining forces, offering jogging statistics on your iPod. Or think of competing airlines that form collaborating global alliances such as OneWorld, SkyTeam or Star Alliance. Strategic advantage comes from managing relationships rather than managing processes.

**Management makes the difference and  
EPM should be the enabler.**

Being smart, agile and aligned are not characteristics of operational excellence, but define what we call management excellence. Management makes the difference. And enterprise performance management (EPM) should be the enabler. Unfortunately, EPM traditionally focuses on the management- or PDCA-cycle, an inside-out approach. This was confirmed by a recent Cranfield University study that found organizations are too internally focused and did not use sufficient external information or benchmarking. Contrast this to management excellence, which is the art of reconciling outside-in and inside-out. In the words of Professor Rumelt,<sup>4</sup> substantially higher performance often starts from exploiting a change in the environment, and riding that change with quickness and skill. In other words, it’s about understanding the contributions and requirements of stakeholders (alignment), movements in markets (agility), and superior interpretation of data (being smart). Strategic guidance comes from outside, tells us what to *plan*, what to *do*, what to *check* and what to *adjust*. A better understanding of management

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<sup>3</sup>Thomas W. Malone (2004), *The Future of Work: How the New Order of Business Will Shape Your Organization, Your Management Style, and Your Life*, Harvard Business School Press.

<sup>4</sup>Dan P. Lovallo and Lenny T. Mendonca (2007), “Strategy's Strategist: An Interview with Richard Rumelt,” *McKinsey Quarterly*.

processes is needed. That is why we introduce our view on the management process: strategy-to-success.

## STRATEGY-TO-SUCCESS

The management process of strategy-to-success (S2S) is an extension of Porter's<sup>5</sup> concept defining the value chain across the business processes. Like every business process, the management process S2S consists of a number of steps: we need to understand our stakeholder environment, scan the market, strategize about our business model, manage our business plan, run our business operations, and provide feedback on all levels by measuring the business results (Figure 1).

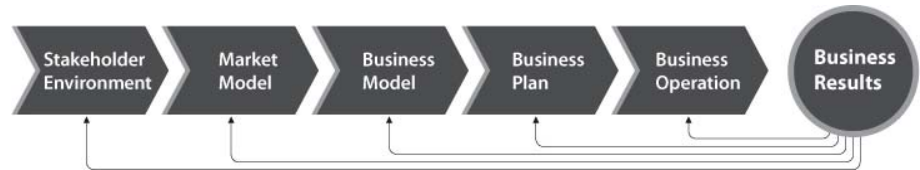


Figure 1: Strategy-to-Success: The Management Process Value Chain

### Stakeholder Environment

**Organizations operate in a network of different stakeholders, each having different requirements but also having different contributions.**

In our view, performance management is not a top-down exercise, translating your strategic goals into success factors, key performance indicators, and lastly improvement initiatives. Organizations operate in a network of different stakeholders. Each of those contributes to the performance of the organizations. Employees contribute labor, shareholders provide capital, suppliers and partners provide materials and services to design, build, and sell products, customers provide demand, society provides an infrastructure, and regulators ensure fair competition. We can only count on those contributions if we also acknowledge stakeholder requirements. We need to map those contributions and requirements and use that as the basis for a performance management strategy.

One of the most important trends for EPM for the coming years will be sustainable development reporting—collecting, analyzing, and sharing information about the impact of your business in terms of economic results, social responsibility, and environmental consequences. When stakeholder management is the starting point of performance management, corporate transparency will become much less of an issue.

### Market Model

Our external stakeholders ask not for our budget, but for our projections, forecasts, and guidance to the market. If you miss external trends that impact your business and do not take guidance, this has serious repercussions. Your stakeholders lose confidence in the capabilities of the management, the share price may be affected,

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<sup>5</sup> Michael E. Porter (1985), *Competitive Advantage: Creating and Sustaining Superior Performance*, The Free Press.

and ultimately the agencies lower your ratings, leading to an increase of the cost of capital. That's a pretty tangible business case.

Understanding market dynamics is the first crucial step in evaluating strategic alternatives and to define the right strategic goals. New products and services are introduced, new competitors enter the market, consumer behavior is changing, and business pace is increasing. Most organizations have all the external data to predict these trends, residing in their competitive intelligence (CI) functions. At the same time, internal information is readily available on resources and activities, within extensive business intelligence (BI) systems. However, rarely are CI and BI combined. The strategy-to-success process suggests combining these two functions.

### **Business Model**

**Scenario analysis is a key component of management excellence.**

Performance management started out as a discipline supporting strategic decision making. The systems involved were called decision support systems (DSS), often using what is now called OLAP databases to run what-if analyses.

There are many different strategic options that you have for shaping your organization and to identify the business model and the best stakeholders within this business model to maximize your success. Would you like to innovate and grow by introducing new products yourself, or should you find partners? If you need to downsize, do you divest a business unit or reduce capacity throughout the business? Which activities do we outsource, and which activities do we keep? These questions cannot be answered by calculating the return on investment, but by aligning them to what the market needs. Scenario analysis, popular in the 1970s and 1980s, reemerges as a strategic performance management initiative.

### **Business Plan**

**Taking an outside-in approach, which is the core of the strategy-to-success process, intuitively shows the importance of rolling forecasts.**

At this phase, we enter the more traditional view on performance management, using the PDCA-cycle. You set goals and create plans towards making those goals. Progress on the plan is closely monitored and differences are analyzed. Results are reported and new goals are aligned with the feedback. However, planning should not be an annual financial exercise that is later translated into operational activities. It should be more operational in nature, continuously balancing the needs of the market and stakeholders with the capacity of the internal resources and activities—translating into the (financial) goals of the business model phase.

This is why rolling forecasts are so important. Every change in the market or in internal capacity leads to a new operational forecast and financial prognosis. Variance analysis is not based on the budget, but is a relative comparison between the organization and the rest of the market.

### **Business Operations**

The “proof in the pudding” for every strategy is in the execution, in the business operations step. Insight, strategies, and plans need to be actionable and put into action. Execution should be closely monitored. But performance management

needs to do more than monitoring single processes. Performance management needs to overlay the various business domains, creating insight in causal relationships. For example, if the days-sales-outstanding (DSO) increases and the call center registers a spike of complaints, it might be because customers are unhappy, because they are not serviced well. This may be the result of a cost-saving initiative by paying suppliers later.

**Use standard metrics for operational measures. Standards allow benchmarking and there is no competitive value in creating your own definitions.**

A recent Economist Intelligence Unit (EIU) study found that organizations need more enterprise-level data; silo-information was identified as one of the main hurdles to success with performance management. To perform this cross-domain analysis, one of the main trends in performance management is to implement master data management, making sure all domains use the same product, customer, organization, and other reference tables. Many operational measures can be standardized; there is no competitive differentiation in your own definition of absenteeism or DSO. Standards allow you to benchmark your operational excellence.

### **Business Results**

**You can only get business results by putting plans into action—to link strategies all the way to business operations. Business results should provide feedback to all previous steps of the process.**

Every time we go through the strategy-to-success cycle, we need to learn from it. The S2S process is not complete without feedback. There should be performance indicators in place to provide that feedback to *every level* of the strategy-to-success process. Operational management needs real-time information, business planners need performance variance analysis, strategists need feedback on progress towards overall goals and on comparison to the overall market, and all stakeholders benefit from seeing how their contributions are recognized and requirements are met. Dashboards and scorecards are not for senior management alone, but are essential for all.

Strategy-to-Success Step	Call to Action
Stakeholder Environment	<ul style="list-style-type: none"> <li>• Focus on stakeholder performance indicators</li> <li>• Invest in sustainable development reporting</li> </ul>
Market Model	<ul style="list-style-type: none"> <li>• Integrate internal and external information</li> <li>• Merge business intelligence and competitive intelligence functions</li> </ul>
Business Model	<ul style="list-style-type: none"> <li>• Introduce scenario analysis</li> </ul>
Business Plan	<ul style="list-style-type: none"> <li>• Implement rolling forecasts</li> <li>• Connect operational planning and financial budgeting</li> <li>• Remain focused on variance analysis</li> </ul>
Business Operations	<ul style="list-style-type: none"> <li>• Introduce master data management</li> <li>• Focus on cross-domain analysis</li> <li>• Benchmark operational measures</li> </ul>
Business Results	<ul style="list-style-type: none"> <li>• Create performance indicators for all S2S steps</li> <li>• Use scorecards and dashboards to visualize performance</li> </ul>

**Table 1: Call to Action**

## CONSIDERATIONS

EPM is widely positioned as a management discipline of strategic importance. But how can it be strategic if it is a controlling activity in the back office? EPM should be closely connected to the business model. It should support strategic decision making, not just tactical management execution. It should support stakeholder management, not just provide internal management information. It should be part of your operations, and not just be finance oriented. All this needs to be done in concert. The shortest definition of EPM that we can come up with is “EPM aligns S2S.”

All models are wrong, but some are useful. The strategy-to-success model has its limitations too. Of course, it is possible that you discover during the business planning phase that the business model phase had some shortcoming and needs to be revisited. The market and business model phase may show that you need to rebalance stakeholder contributions and, for instance, create a new partner strategy.

**A strategy is only as good as its implementation and the quality of feedback**

But the strategy-to-success model is not meant to be linear and deterministic; it is meant to be heuristic. Each step is guided by the previous step, but managers should have deep knowledge of all steps at the same time. The S2S model needs to stress the outside-in approach, contrasting traditional performance management. It also stresses that results can only be booked by going through all the steps consecutively. A strategy is only as good as its implementation and the quality of feedback.

Lastly, maybe we've been too harsh on the PDCA-cycle. It may be too internally focused; the term "navel-gazing" may even apply. But you can't be smart, agile, and aligned if your own house is not in order. You must first be in control yourself before you take the outside-in approach. The PDCA-cycle is a good place to start improving today. But the focus should be on tomorrow, making a difference with your own strategy-to-success process.



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When Oracle acquired Hyperion, it was clear that this was a business-changing event. Business applications such as ERP and CRM are no longer separated from enterprise performance management (EPM) applications and business intelligence (BI) technologies. The groundbreaking research our team has been doing has uncovered many parallels between both business disciplines. I believe “management excellence” will become as impactful as “operational excellence.”

Consider the days before ERP and CRM systems. Order entry, accounts payable, accounts receivable, and the general ledger were all standalone applications typically written in COBOL. The operational inefficiency of these applications became the target of the ERP and CRM revolution. The success of ERP and CRM came from their ability to drive operational excellence based on two simple concepts:

- Take a systematic approach to the processing of transactions through modules operating on a common platform and provided by a single enterprise software vendor.
- Identify and refine the key business processes necessary to run the business.

The combination of well-defined business processes and a sound technology architecture to support them proved to be magic. EPM promotes management excellence based on two simple concepts that parallel ERP and CRM:

- Take a systematic approach to the management activities through modules operating on a common platform and provided by a single enterprise software vendor.
- Identify and refine the key management processes necessary to manage the business.

The first concept is once again based on sound technology strategy and best practices in systems engineering, while the second concept is truly a revelation as most businesses can’t readily identify their key management processes, such as “gain-to-sustain”, “investigate-to-invest” or “plan-to-act” to name a few.

The Hackett Group in their *Book of Numbers*<sup>TM</sup> Research Series has documented that the way forward for best-in-class organizations is to solidify their operational excellence through ERP and CRM, while differentiating with management excellence that is enabled by EPM.

# Putting Management Excellence into Practice



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## **HYPE OR REALITY?**

What drives the need for management excellence? Is it hype, or the result of an evolution of company requirements to stay on top of their business? More and more, the companies we talk with underline the need for being smart, agile, and aligned. Here are a few cases that illustrate how management excellence is already a given in many industries.

### **Being Smarter About the Business**

For Christophe Mialon, Accounting and Controlling Group Manager at Saur - global and major player in water utilities and in the waste management chain, serving over 20 million consumers in France and worldwide- being smarter is about sharing information, a core mission for Finance. "Our role at Saur is to produce relevant insight for the Group. Our challenge is to improve our controlling activity and achieve true Performance Management. Therefore, we will make our company smarter in its decision making process, by bringing relevant information and selected KPI's (Key Performance Indicators) in dashboards to all managers from both a financial and an operational stand point and by taking our controlling activities beyond finance."

At Stryker Endoscopy, a division of Stryker Corporation, a \$5 billion medical device and orthopedic manufacturer, being smarter with data is critical to operating business. "One of the main goals was to bring everybody under the same umbrella of data," explains Glenn Boelenheim, CFO, Stryker Endoscopy. "We had roughly 40 systems that were being utilized at Stryker Endoscopy and we narrowed that number down to about 25. But even the ones that exist now are all drawing from a common data source. Moving forward, we will focus on how we make that data more accessible to the users that need it, and make it more real-time for those users."

### **Nimble Response to Growth Opportunities or Risks**

For Jacques Ndongué, group controller and head of performance at Schneider Electric, a leader in energy management and automation, management excellence is something he is living and breathing everyday. Schneider's challenge is to remain agile and face each year's challenges, while generating productivity gains and ensuring service quality of the highest standards with the same staffing. For

Ndongué, performance management is critical. It enables him to manage the ever-increasing workload year after year. “At each new fiscal beginning, what we learned to master the year before becomes 75 percent of what awaits us; the other 25 percent is totally unknown and we have to be prepared to address it,” says Ndongué.

“Agility is engrained in Endoscopy’s performance,” explains Glenn Boelhenheim. “It permeates through our entire culture. We introduce new products and new versions of products every two to three years. So when you think about the back office and the finance side of things, we need to be equally fast. We close our books in two days. It allows us to have a view of our actual performance, our budget performance, and our projected performance.”

### The Many Faces of Alignment

#### Management Excellence:

- Better and broader understanding of the business
- Ability to react to new challenges or seize new opportunities
- Internal alignment as well as synchronization with external stakeholders’ feedback

Alignment starts by speaking the same language and sharing the same information. To achieve management excellence, every decision maker should use the same framework and align managers across the entire organization. How do you link your strategic goals to operational plans to execution, while empowering everyone to contribute to the success? This requires setting up solid management processes that are supported by robust technology.

“From operations to sales, R&D, or finance, alignment is a need and a request. Having an EPM solution aligned all along the company, makes us confident that we have the same information. If we go to market with this information, everyone can be sure that this information has been shared and discussed with all the counterparts involved,” says Ndongué.

For Boelhenheim, alignment also starts in the system. “Being aligned in the finance organization really means having a common data set for all of your reporting. All of our divisions, which are located in Israel, Puerto Rico, San Jose, and Dallas, feed their data into a common system and then it’s consolidated. Executives and directors can use that top-level information to make decisions and know that the dissemination of information will have the same meaning across our divisions.”

Finally, alignment has to be achieved with external stakeholders, including customers and suppliers, but also investors, regulators, and society at large. External alignment has been crucial for companies for decades. Back in the 1950s, Japanese companies understood the need to intensify collaboration with customers, suppliers, and investors in what they called *Keiretsu*. Today, one of the most interesting areas of external alignment is sustainability reporting.

Consider Metso Corporation, a global engineering and technology corporation serving customers in the pulp and paper industry. It has some 26,500 employees in 80 plants, and 275 sales and maintenance units in more than 50 countries. Metso’s customer industries are significant users of natural resources, so Metso has major indirect impacts on the environment through the solutions it supplies. Metso sees

optimizing its products and services for minimal environmental impact as a strong competitive differentiator, especially in developed markets.

Metso practices what it preaches and publishes an impressive sustainability report. It uses the Global Reporting Initiative's (GRI) three-dimensional approach of economic, social, and environmental responsibility. The company's challenge was to report on sustainable development activities across all of their sites, while streamlining the process of gathering environmental data. Metso uses its existing performance management processes and systems for this, in the financial area. Publishing financial data requires the same skills, processes, and technologies as publishing environmental data.

### **Information**

For Oracle President and Chief Financial Officer Safra Catz, exceptional management is needed to create an organization that is "built to last" in today's fast-paced economic environment. "It used to be that operational excellence was really enough, but it isn't anymore," Catz notes. "I'm hearing from customers that competition is really heating up at both the local and global levels, and so is the pressure to do more with less. Good managers have to make better decisions, and they have to better align themselves with their customers, employees, partners, and the community at large. You really have to differentiate yourself with being smarter, being more and more flexible, agile and able to really respond to your customers' needs more quickly."

"Oracle has always been about information," Catz continues. "And for years it was about automating clerks and putting data into systems. But the true goals, the high-value goals, are about enterprise performance management—making the information available and actionable for management teams so they can make changes when changes are needed, or stay the course when they are winning."



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Financial and management accounting are well-established disciplines. Every organization in business does it and multiple systems are in place to measure financial performance from different perspectives. Balance sheets, income statements, and cash flow statements are the basis to report financial performance. A multitude of ratios are applied to understand the returns delivered.

However, two unquestionably critical assets for any successful business are still largely invisible: the human capital asset and the information asset. With a few exceptions such as professional players in football clubs, for instance, human capital assets cannot be part of a balance sheet because it would violate accounting principles, such as the need to have exclusive control over the asset.

On the other hand, a growing body of academic studies proves that the premium in the market-to-book ratio, for instance, is an approximation for the return of human capital.

The asset information somehow faces the same fate. As much as human capital, it is mainly measured by the cost, and though it is difficult to quantify, the value or return on information.

In contrast to this lack of capabilities to adequately measure the returns of human capital and information, there is common sense that the combination of the right people and the right information can make all the difference in the performance of a business.

In principal we could say that there are two different loops with respect to financial performance. The first loop is traditional financial and management accounting, dealing with quantifiable assets, their utilization, and returns. The second loop is still an open one, dealing with “un-quantifiable” assets as discussed above.

Enterprise performance management aims to connect the two loops, though it is still has a way to go to close the second loop. But to understand the financial performance impact of human capital and information is increasingly important as both are key differentiators in the globalized network business of the 21st century.

# Creating a Passion for Performance



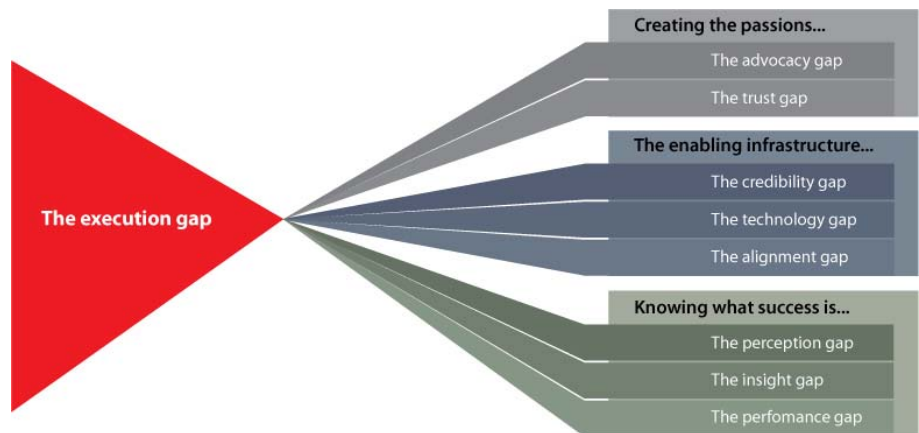
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In 2007, the Centre for Business Performance, Cranfield School of Management, Cranfield University and Oracle undertook a global study into the state of the art of enterprise performance management. During the analysis of the questionnaires from over 600 companies based in the UK, USA, China, Japan, and Australia, a number of common issues surfaced. These added up to what we have called the ‘execution gap’ that prevents organizations from achieving management excellence. This article is the first of three that examine the execution gap.

## THE EXECUTION GAP

From the study findings, eight individual gaps were recognized that contribute to the execution gap as shown in Figure 1.



**Figure 1: The Eight Gaps that Make Up the Execution Gap**

This article will focus on the first of the groups: creating the passion.

### Why Passion?

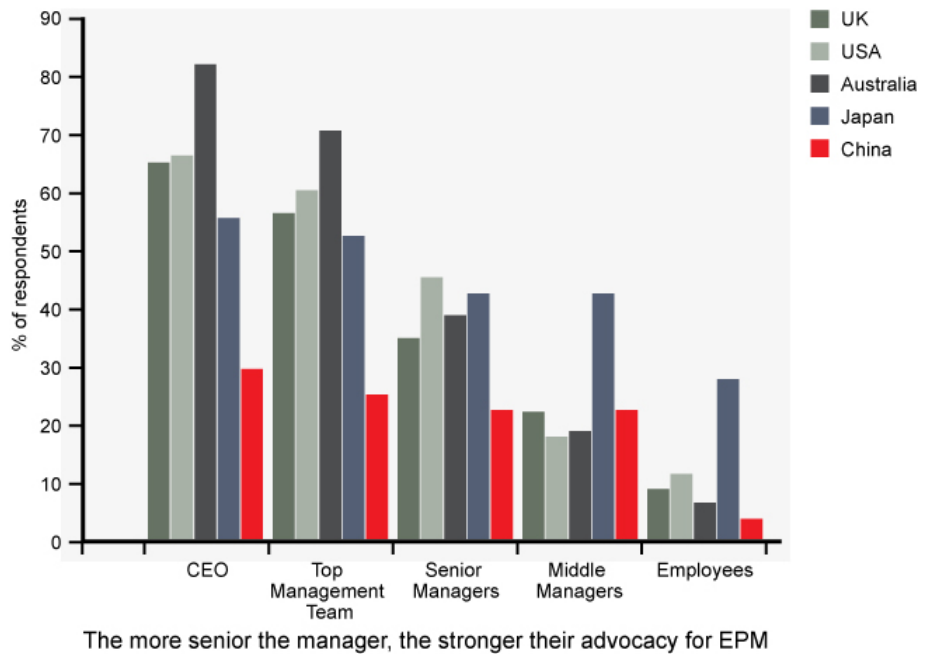
Because it is people that make enterprise performance management a success! In fact, management excellence touches everyone from the executive board to the most junior member of the workforce. Everyone has a part to play in making the company succeed in its goals.

A characteristic that we all recognize that sets great companies apart from the rest is what we describe as the “passion” for the company. Employees are proud to work there, customers are loyal to the brand, and the company is generally admired. In our study, we found that passion was stifled by the advocacy gap and the trust gap.

## THE ADVOCACY GAP

In the questionnaire we asked about the awareness, use, and acceptance of enterprise performance management at different levels within the company.

The results, as shown in Figure 2, were startling in their clarity and consistency. Most organizations have clear advocates for performance management on the higher levels within the organization, but on lower levels within the organization, there is a high proportion of people unaware of the initiatives, or they are aware but do not use the system. Advocacy falls dramatically the further down the organizational hierarchy.



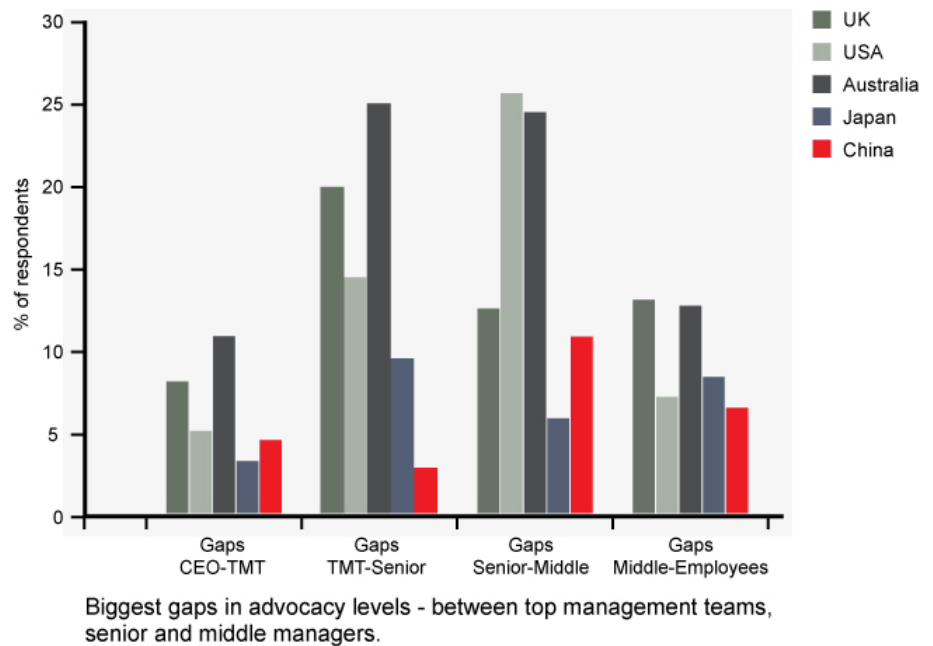
**Figure 2: The Advocacy Gap**

**EPM should be seen as a way of improving everyone's work.**

Senior management may lead the enterprise performance management charge, but the troops are not following willingly. In order for any organization to be focused and aligned, the advocacy gap must first be fixed. EPM should be seen as a way of improving everyone's work, instead of a top-down initiative to only support top management's goals.

## THE TRUST GAP

The decline in advocacy is compounded when we look at the differences and see huge gaps between top management teams and senior management, and senior management and middle management.



**Figure 3: The Trust Gap**

If senior management has issues in convincing their direct reports of adopting a certain management system, there must be an issue with trust between those groups. Otherwise lower levels of management would not hesitate subscribing to EPM as a means for management collaboration and control.

With these big differences at crucial management levels, it is clear why there is such a lack of interest in performance management at the employee level.

### What Should Companies Do to Create Passion?

The study revealed various strategies for organizations to create a passion for performance:

- Use analytic and predictive capabilities of software to understand what strategies do and don't work and what will and won't work in the future. Don't forget those who understand this best can often be those on the front line "doing," so use their expertise and knowledge in the analysis.
- Focus on strategic change through a completely integrated business planning approach—from strategic planning through financial planning to the detailed operational plans.
- Be aligned with one clear set of integrated goals and objectives, where cause and effect of departmental actions on the end result are known, so that the overall business is optimized.

Perhaps most important of all, put learning above "monitoring and control" as the prime reason for enterprise performance management.

Put learning above "monitoring and control."

# The Rise of Uncertainty Risk Management



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## WHAT IS UNCERTAINTY RISK MANAGEMENT?

In many cases, strategic advantage comes from superior insight. It may be spotting a new trend or creating a “blue ocean market,” and making a strategic bet early in the game. A strategic bet also means you can lose—and there have been an equal number of cases where this has happened. The decisions that companies make that lead to high performance are the same decisions that lead to failure.<sup>1</sup>

Unfortunately, risk management is generally considered a separate discipline that is more connected to compliance, but risk management is as important to management excellence as performance management. Some speak of strategic risk management in combination with performance management, but strategic risk is not a clearly defined term. I prefer to use the term uncertainty risk management (URM), defined as managing uncertainty which has both a downside component as well as an upside opportunity element.

A paraphrase of Pat Leach is, “all of management’s value is derived from managing uncertainty.”<sup>2</sup> If there were no uncertainty, then we would be able to calculate exact values for future cash flows, making optimal decisions trivial. As a further refinement, when measuring uncertainty around key variables, it is essential to calibrate your assessment of that uncertainty.<sup>3</sup> Uncalibrated assessment will underestimate the uncertainty in a key variable, thereby understating the risk. Another key to URM is to clearly state the objective (e.g. maximize sequential quarterly total bookings) subject to what constraints (e.g. being cash flow positive).

URM applies at both the strategic as well as operational level. Operational URM is managing uncertainty in frequent, low impact transactions. Six Sigma projects are a good example of operational URM. Strategic URM is managing uncertainty at the business unit or corporate level. These are low volume, but high impact decisions. Examples include decisions about which businesses to acquire or divest; which drug leads or oil deposits to pursue. Matching the right capital structure to this optimized business portfolio is a key part of the process.

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<sup>1</sup> Michael Raynor (2007), *The Strategy Paradox*, Random House Publishing.

<sup>2</sup> Patrick Leach (2006), *Why Can't You Just Give Me the Number?*, Probabilistic Publishing.

<sup>3</sup> Douglas Hubbard (2007), *How to Measure Anything*, John Wiley & Sons.

## How Does URM Intersect with the Strategy-to-Success Management Value Chain Framework?

The strategy-to-success (S2S) management value chain framework is not limited to companies that have perfected their operational processes. Because essentially all companies are continuously working on improving their operational excellence, that is not a reason to defer implementation of S2S. With URM, companies are optimizing not only their deterministic futures, but their stochastic ones as well.

In fact, even leading organizations that optimize subject to uncertainty may just be lulling themselves with a false sense of security. Nassim Taleb makes this case strongly in *The Black Swan*.<sup>4</sup> Also, organizations with perfected processes may be the most in danger of disruption from more flexible innovators in adjacent markets.<sup>5</sup> With the emphasis on innovation in today's business dialogue, there is a real trade-off between highly refined operational efficiency and the flexibility to foster innovation. It is also important to match the organizational size and structure to the opportunity. Of necessity, new opportunities may start out small and would not be of interest or a fit into a large, well-run, operationally excellent company.<sup>6</sup>

While dashboards are great at giving a quick status on the key performance indicators (KPIs), it is URM that can determine which variables are actually key in the KPI. If your dashboard were to have just one or five key metrics, what would it (or they) be? How do you decide which of the hundreds of available variables you track on your dashboard? URM can provide a robust answer to that question.

Similar to the KPI context, in the PDCA-cycle (Plan, Do, Check, Adjust), uncertainty analysis is key to determine which projects should begin in the first place and put through the PDCA-cycle. If you have 400 possible projects with uncertain cash flows, timing, and demands for labor, how do you choose the optimal set of projects to undertake? Again, URM can provide a robust answer to this question.

Management excellence has three pillars: Being smart, agile and aligned. Smart means getting the most out of your data. URM is key to data analysis when data is expensive to acquire, incomplete, or inaccurate. This makes URM critical in just about every case. Agile means flexible. URM dramatically reduces the time-to-action by eliminating the need to gather more information in almost every case. By doing the math with uncertainty before gathering hard-to-get data, 95 times out of 100 the way forward will be clear.<sup>7</sup> In the rare cases where more information is necessary to make a better decision, then URM provides a very specific focus on just what information is necessary. There's no wasting time and money with URM on analysis paralysis. Aligned means collaboration. URM fosters collaboration both

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<sup>4</sup> Nassim Nicholas Taleb (2007), *The Black Swan*, Random House Publishing.

<sup>5</sup> Clayton Christensen and Michael Raynor (2003), *The Innovators Solution*, Harvard Business School Press.

<sup>6</sup> Christensen.

<sup>7</sup> Hubbard.

**Uncertainty risk management applies throughout the strategy-to-success framework.**

within the enterprise and across the industry and supply chains. For example, if the CFO's office has a global forecast for commodity prices, this best practice can be shared throughout the many business units. In Six Sigma case studies, it is essential to have quality throughout the supply chain.

URM applies throughout the S2S framework. Beginning with the stakeholder environment, URM provides insight into the relative impact of various stakeholder requirements and their tradeoffs before doing costly and time-consuming data analysis. Further, in the especially sensitive area of environmental impact, URM provides a credible estimate for the impact, timing, and cost of an enterprise's activities with respect to its environmental impact.

In the market model, URM increases the realism of your projections, thereby reducing the number of missed forecasts. This results in a direct increase in your organization's credibility. In a market model with limited data, high uncertainty, and many options, URM is an essential part of understanding the market dynamics.

In the business model, URM is the most realistic method for analyzing your strategic business options. Essentially 'what-ifs' on steroids, URM can show you not only the possibilities, but the probabilities of certain outcomes, depending on your data, uncertainties, alternatives, tradeoffs, and flexibility in execution.

In the business plan, URM fills the gap in the traditional PDCA-cycle between reporting results and aligning new goals with the feedback. After the reporting step and before action, comes analysis of alternatives. That analysis is best performed with URM to connect your data to your decisions.

In business operations, URM's analytics drive the answer to the causal questions. Of all the variables, which ones are driving the performance that we are seeing? This allows management to know what matters and to focus on what is most important. URM also helps drive standards and close the loop between analysis and actions. The output of URM is a set of decisions, not just charts. Charts are helpful for telling you where the issues are, but not what to do about them.

Finally, in business results, URM is helpful in understanding how often feedback should be given. Just like checking minute-to-minute stock price changes is not the best way to measure the trend of a security, nor may a 'more, sooner' approach to feedback provide the most useful information. URM can separate the signal from the noise in the feedback system.

Every organization has the same focus challenge: given all of my possible opportunities, yet having limited financial, technical, and human resources, where should I focus my efforts? URM provides a robust answer to that question based on your available data and the uncertainties in your business.



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### **ACCENTURE CENTER FOR HIGH PERFORMANCE BUSINESS**

*Competing on Analytics*, Tom Davenport and Jeanne G. Harris' bestseller is one of the most influential and widely read books on how firms develop a culture for "evidence-based decision making" and use BI and analytic tools to monitor and drive performance. For a quick introduction, or to even take a short quiz to find out where your company ranks as an "analytic competitor" check out the Accenture Information Management Services at:

[http://www.accenture.com/Global/Technology/Information\\_Mgmt/Information\\_Mgmt\\_Services/R\\_and\\_I/CompetingAnalyticsAIMS.htm](http://www.accenture.com/Global/Technology/Information_Mgmt/Information_Mgmt_Services/R_and_I/CompetingAnalyticsAIMS.htm)

### **THE NEW BPM: ENTERPRISE PERFORMANCE MANAGEMENT**

In the March 2008 issue of BPM Magazine, Andrew Pritchard, Oracle's senior director for EPM marketing, highlights the findings of a recent Oracle-sponsored Economist Intelligence Unit (EIU) study. Pritchard discusses the implications as ERP and EPM systems evolve into full-scale enterprise management systems. To read this timely and uniquely insightful article, visit:

<http://www.bpmmag.net/magazine/article.html?articleID=14976&pg=1>

### **ENTERPRISE 2.0**

Are you struggling to keep abreast of the latest developments around wikis, blogs, social networks, RSS, Twitter and mash-ups? Forrester recently stated that Web 2.0 technologies represent a fundamentally new way to connect with customers and prospects and harness the collaborative power of employees. Oracle and its recently acquired BEA Systems were two of the companies at the Enterprise 2.0 conference in Boston. To get a sense of where Enterprise 2.0 is going, visit Harvard Business School Professor Andrew McAfee's renowned blog, The Impact of Information Technology (IT) on Businesses and their Leaders, at:

<http://blog.hbs.edu/faculty/amcafee/>

### **PERSPECTIVES ON THE BALANCED SCORECARD**

The balanced scorecard is the most widely-used performance monitoring/management system by industry worldwide. To learn how firms are using scorecards to drive their performance, check out the recently published, Scorecard Best Practices: Design, Implementation and Evaluation. This book, by authors Raef Lawson, Denis Desroches, and Toby Hatch, explains the theories

behind scorecard tools and metrics, with real-world implementation examples and case studies. For more information, visit:

<http://eu.wiley.com/WileyCDA/WileyTitle/productCd-0470129468.html>

### **MANAGEMENT EXCELLENCE IN GOVERNMENT**

Management excellence also exists in the public sector. One US federal organization, the Department of the Interior, publicly details its goals, metrics, and progress in an annual “Performance and Accountability Report.” And, it is an agency with a massive scope and mandate. For instance, the DOI manages 68 percent of the oil and gas reserves in the US; it manages over 500 million acres of land, some one-fifth of all the land in the US; it provides 60 percent of all the water used by farmers in the US; and it oversees the protection of more than 1,200 “endangered species,” while also providing webcams of Old Faithful and the Grand Canyon. For an interesting perspective on “managing for excellence” in the United States, visit: <http://www.doi.gov/initiatives/management.html>

### **GLOBAL ENTERPRISE PERFORMANCE MANAGEMENT STUDY**

The Global Enterprise Performance Management Study – carried out by the Centre for Business Performance, Cranfield School of Management, Cranfield University and Oracle, is the largest global EPM study ever conducted. It discusses a total of nine gaps that organizations need to mind in becoming successful with EPM. The study can be downloaded at

<http://www.oracle.com/go/?&Src=5716090&Act=119&pcode=NA06070024C132>

### **ORACLE’S EPM SOLUTION SPACE**

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### **ABOUT ORACLE CORPORATION**

Oracle is the leader in Enterprise Performance Management (EPM), unifying Performance Management and Business Intelligence (BI), supporting a broad range of strategic, financial and operational management processes. Oracle provides a complete and integrated system for managing and optimizing enterprise-wide performance. This allows organizations to achieve a state of management excellence – being smart, agile and aligned – which provides competitive advantage and leverages their operational investments.

- **Smart** – Leverage market-leading products and technologies that address enterprise-wide requirements and drive new insights into your business
- **Agile** – Enable advanced integration that improves agility and lowers costs of ownership
- **Aligned** – Drive pervasive intelligence across the enterprise by linking strategic, financial and operational management processes

For more information, go to <http://www.oracle.com/epm>. Contact us with any comments or questions at [epmgbu\\_ww@oracle.com](mailto:epmgbu_ww@oracle.com).



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