Beware of Performance Management Pitfalls

Smart companies avoid basic mistakes in implementation

White Paper

sponsored by

COGNOS®

VENTANA RESEARCH

Aligning Business and IT to Improve Performance

Ventana Research Headquarters
1900 South Norfolk Street, Suite 280
San Mateo, CA 94403
info@ventanaresearch.com
(650) 931-0880

Ventana Research Europe
2nd floor, Berkeley Square House
Berkeley Square, W1J 6BD London
europe@ventanaresearch.com
44 (0) 20 7887 6012

Table of Contents

Two Common Mistakes

Performance management is the strategy and sets of methodologies and processes that an organization uses to direct its employees, partners, suppliers and customers to achieve a common set of goals and objectives. Companies manage performance through various mechanisms, including planning, budgeting, scorecarding, querying and reporting results and variances. Each of these activities involves making data collected by transaction systems available in a context and format that transforms the data into actionable business information. Ventana Research believes all performance management initiatives must address an interrelated set of people, process, information and technology issues. This paper focuses on the latter two, but people and process are critically important in shaping decisions about what information is needed and the technology for managing it.

In setting up performance management systems, two mistakes are particularly common. One is choosing the wrong software to do the job, and the other is not having enough of the right information.

The two problems can be interrelated. Often, both arise when the process of designing the system begins with some piece of technology (such as a specific application) as a "given." A project that starts with a choice of software likely will fail, or at least fall short of its potential. Force-fitting a technology into the specific situation of a company and its users usually is a mistake. You end up making people and processes adapt to the way the software functions; as a result, the processes may no longer function smoothly, and the people may resist using the new solution. While it is good business practice to make use of existing information technology assets, it is better not to use them for the wrong purpose simply because they have already been purchased.

The second mistake is selecting (or allowing a project to proceed being confined to) too narrow a range of information used for performance management. Our research study, "Financial Reporting and Consolidation," found that a majority of people in finance and business roles are satisfied with the high-level numbers they receive regarding past results. Yet they also feel they are not getting a complete picture. They told us they want more guidance on how well they are performing to objectives, more forward-looking indicators and more information about external factors (such as competitors' results).

Successful performance management initiatives usually result in a broader set of information being available to employees than they have had in the past, and being provided sooner and in more relevant context. In contrast, simply finding a more efficient way to deliver the same information is like paving a cow path. It may yield some incremental improvement, but it will not enhance individual efforts sufficiently to boost the organization's competitiveness. It misses an opportunity to use available technology to empower everyone who uses it to make better

decisions sooner and more consistently, and to improve the company's agility in responding to change.

One source of both problems is confusion about the roles that enterprise resource planning (ERP), business intelligence (BI) and other enterprise software play in enabling companies to plan and set objectives and then to measure and assess results. To put it simply, designing an effective performance management system means using the right applications and the right data.

Transactions and Business Intelligence

ERP is one of several major types of transaction recording systems widely used by larger corporations. (Others include customer relationship management [CRM] and supply chain management [SCM].) Not long after companies began to deploy ERP systems, they discovered a major problem. Although ERP software did a great job of collecting accounting and other data while managing record-keeping activities (such as creating purchase orders, booking sales and purchasing inventory), it didn't help companies transform this data into actionable business information. This shortcoming gave rise to business intelligence systems.

Business intelligence, broadly speaking, is information that people need and use to accomplish the work they do. For this reason, it must be complete, timely and relevant. Business intelligence software is designed to do things transaction systems by themselves do not do well. It gathers, stores, accesses and analyzes data collected by the transaction systems so people can understand situations better and make better decisions quickly. The BI category includes software that performs analysis, creates reports and manages performance.

Companies use different types of software to sift through and understand results. Analytical applications handle repetitive analyses. Some of the numbers and ratios produced by these analyses take the same form in all companies (such as year-over-year comparisons), but some are unique to specific types of businesses or industries (same store sales, inventory turnover, the "combined ratio" for insurance companies and so on), and still others may be unique to how one company runs its business. One-time ad-hoc analyses are done to answer specific questions or better understand the root cause of some result.

Reporting also can be divided into repetitive (sometimes termed "production") reporting and ad-hoc reporting. Production reports inform employees of specific results (such as sales and balance sheet information) or deliver periodic analyses (for example, actual versus budget). Companies create ad-hoc reports to follow up on specific analyses or collecting a set of information. Until a few years ago, almost all reports were printed on paper. Now companies have many options on how to deliver this information. Some use portals to aggregate information onto Web pages (sometimes in a highly personalized format), others use e-mail or another form of communication.

Why Performance Management Matters

One of the evolutionary roots of performance management can be found in the expanded capabilities delivered to corporate management by BI systems. In this sense, performance management is a way of using information technology systematically to improve business results. With that technology in place, companies implement performance management systems to increase their nimbleness and responsiveness by giving people the right information as soon as possible and in the right context. This enables good managers to make better decisions sooner. Performance management also aims to elevate the capabilities of people in the organization by focusing their attention on ways to improve their personal performance. That feedback and information about the state of the business helps people do their jobs more effectively.

Performance management provides a methodology with which management can set objectives within business units and across a corporation, ensuring that these objectives are consistent with corporate strategy and will increase the organization's ability to achieve these goals. By ensuring more timely, accurate and precise communication of results, plans and objectives, it helps coordinate corporate activities better and to make sure that fewer things fall between the cracks.

A variety of technology elements support performance management efforts. They include:

- dashboards and scorecards
- planning and budgeting
- production reports
- ad-hoc reports
- business analysis
- ad-hoc queries and analysis.

Note that while ERP is a vital source of data for performance management, it is not on this list. Ventana Research has concluded that ERP systems have played a limited role in helping companies implement new performance management initiatives. Our recently completed research study "ERP Innovation," sponsored in part by Cognos (which surveyed 588 companies, each with more than 1,000 employees), found ERP was not the preferred software choice for implementing performance management. The study showed more companies implemented innovations related to performance management as well as planning, budgeting and forecasting using some software other than ERP. The likely reason is that transaction systems are designed to collect information systematically and efficiently but not to analyze it. BI software allows companies to make better use of that information.

Different Systems, Complementary Roles

Transaction recording systems and business intelligence software play two different but complementary roles in supporting performance management. Successful performance management initiatives use both types.

Until the 1990s, companies used dedicated software to automate each part of their record-keeping. As a result, these applications proliferated into an unwieldy mess. Then, when ERP systems first were deployed, they consolidated a range of business functions – financials, manufacturing, inventory and supply chain management, for example – that had been handled by disparate systems.

Combining these elements produces several benefits. It eliminates the need for multiple user interfaces, makes it easier to integrate processes for greater efficiency and responsiveness, cuts maintenance costs and allows more end-to-end process standardization. It also ensures that data is collected in a consistent fashion. For all of these reasons, it makes sense to collect in a single system the information created in the course of managing business activities.

Indeed, the value of centralizing proved to be so great that many companies mandated that their ERP system be used "for everything." Most succeeded in reducing the amount of transactional fragmentation in their core accounting, purchasing and materials management functions. Yet dozens of isolated, single-purpose applications remain. In fact, our recent research study found that almost two-thirds (62 percent) of companies with more than 10,000 employees and nearly half of those with between 1,000 and 9,999 employees continue to use legacy finance applications that could be replaced by their ERP system.

Half of these survey respondents said the reason their company had not replaced a legacy system was that doing so was not important enough, another one-fifth said it would not be cost-effective, and a further one-fifth stated the existing software worked well enough. That companies continue to maintain legacy applications demonstrates that in practice many believe there are sound technical and business reasons for not using ERP for everything.

This feeling is especially pervasive when it comes to performance management, business intelligence and analytics. There is a fundamental difference between systems optimized to collect information and those designed to help people use it effectively.

Transaction systems focus on faithfully recording the past by following set procedures. They are designed to manage repetitive tasks – sales, purchase orders, customer records, releases from inventory – and hence rarely are changed. Also, the processes that transaction systems manage can be defined in detail because a limited group of people in a specific role (or a sequence of roles) uses them.

The purpose of a performance management system is to anticipate the future and adapt to the needs of individual users. Performance management processes thus often evolve ad hoc. Business processes that record transactions are fundamentally different from performance management activities such as planning, querying or exploring data, or creating and using scorecards. One of those differences is that performance management systems are available to a variety of users in different roles who use the information for many purposes.

The point here is that benefits that accrue from using a single system to record a range of transactions do not apply to performance management. While transaction systems strive to centralize as much as possible (because of the value of collecting data in a consistent fashion and enabling business process execution across traditional business silos, to name two reasons), BI systems recognize that in any large company, the data needed to make business decisions – which is far more varied in content and format than transaction data – is collected in multiple systems. Making that data accessible in a consistent, reliable fashion is a challenge performance management must overcome to succeed.

Information from Multiple Sources

Although vendors have expanded the range of business processes ERP systems manage and information they extract from these processes, these systems do not have it all. This is another reason why starting with the assumption that a single transaction system can manage performance will blunt the effectiveness of any performance management initiative.

Peter Drucker, one of the most influential business thinkers of the past century, said, “You cannot manage what you cannot measure,” and offered as well its corollary, “What gets measured gets done.” Indeed, today’s interest in performance management stems in part from the fact that the expansion of the scope of transaction systems over the past decade has given companies many more things they can measure easily and in greater detail. Accounting information became the focus of what was measured because only it was collected systematically. Today, however, companies can collect a plethora of useful information. Unfortunately, many do not collect all that they could and do not always use what they have.

Increasingly, organizations need information from more than just financial records, especially for performance management purposes. The Balanced Scorecard movement began as an effort to mediate between financial and other objectives in setting performance goals. It argued that focusing on accounting data alone could be harmful to a company’s long-term prospects and sought to use performance goals instead to evaluate how well an organization or an individual performed. That goal has not yet been fully realized.

Our market research and consulting work with corporations consistently show that there remains plenty of room to increase the scope of the

nonfinancial information organizations capture and could provide to employees. Our "ERP Innovation" study found that only about one company in 10 reports that its ERP system is delivering all or most of the nonfinancial information the company needs for performance management, and just under half say it delivers some of that nonfinancial information. We believe almost all organizations will find that, to be truly effective, their performance management initiatives will need to draw upon a range of enterprise systems, including custom applications. Our research finds a majority of companies could get more useful nonfinancial information from their ERP systems as well.

Another difficulty larger companies face is having not one ERP system but several. Our ERP research confirmed that large companies typically have a fragmented ERP environment: Only 23 percent of those with more than 10,000 employees have ERP systems from a single vendor; a higher percentage – 27 percent – have six or more. In companies with 5,000 to 9,999 employees, 32 percent have a single vendor, and 12 percent have 6 or more. "Doing everything in the ERP system" then begs the question, Which one?

Our research thus shows that larger companies typically must access information from a complex set of systems (a range of purchased and internally built enterprise applications as well as multiple ERP vendors' software). Generally, companies have found it best to stage the data outside of these transactions systems.

Performance management systems should make it as easy as possible to access reliable and consistent data quickly. In beginning an initiative, it is wise to identify the information needed to make it successful, then work backward to locate the sources of that data and finally determine the best ways to access it. If you start with a particular software product as a given, you will probably have to limit the kinds of information you can access – and, in the process, compromise the chances of success. Furthermore, the cost and complexity of making all needed information available using a system specified a priori could offset any of the savings it might offer.

Ensuring Success

Performance management and painting a house have one important thing in common: The quality of the results is largely determined by the prep work. Here are five steps Ventana Research recommends an organization take to get smooth results from a performance management initiative.

Build a cross-functional committee. It is imperative to involve all constituencies in the planning process from the start. Business requirements must be an important factor in establishing technology requirements, rather than allowing a predetermined set of technologies to define which business requirements can be met. Membership from both sides of the business/IT divide is essential: systems designed to make life easy for the IT group can fail to meet the needs of their business users;

conversely, business users may not understand how their requirements impact the cost and complexity of the application. Usually the gap between the two sides can be bridged by clear communications; this planning step should ensure that business and IT requirements are well-aligned. The communication process also will surface both unrealistic expectations and an inability to deliver necessary capabilities. If your performance management initiative has started with any "given" systems, make sure these will meet the requirements of all parts of the business.

Talk to other companies. One of the most important steps in preparing to implement a performance management initiative involves talking to people who have already done it. Vendor reference accounts are a good place to start but you also should try to network with members of user groups. Ask what has worked for them and, even more importantly, what mistakes they made. In the case of software selection, you are likely to find that even companies that make extensive use of their ERP systems' features and capabilities do not use them for performance management. Our recent ERP research study showed companies that had implemented performance management initiatives were likely to use software other than ERP for this purpose. If using your ERP system exclusively for your performance management initiative is a given, other companies' experience may provide convincing evidence that there is a better way.

Know what information you need. Performance management usually means breaking with the past. Deployment of different enterprise systems (most often ERP, CRM and SCM) that collect a broader range of information than accounting systems will give companies a more complete view of how they are doing. Also, it is likely that your information requirements and data types will evolve over the next several years, and your system will have to accommodate them. When choosing software, ask whether and to what extent it will be able to access, analyze and deliver information from this broad and still expanding data set.

Consider current and future requirements. Many performance management initiatives start small to minimize the risks associated with larger, more complex undertakings. Be sure that there is a roadmap for your company's longer-range performance management objectives and that the information requirements for these are reflected in your initial efforts.

Get support from senior executives. You will need to communicate the results of the cross-functional committee's deliberations to senior executives to ensure they understand what recommendations it makes and why. These discussions can be important if any of the givens for your performance management initiative came directly from or were influenced by one of these individuals. Using the results of specific business cases and reference calls can help tie the objectives to how real companies have achieved success and where they encountered challenges. Without senior-level sponsorship and understanding of the strategic importance of the effort, it will be almost impossible to get optimal results.

Performance management is still a new concept in many organizations. It promises superior ways to understand one's business, market and competitive position. But to realize these potential benefits, companies must prepare thoroughly and implement systems carefully. You should identify all sources of important information and make sure that your users can access them easily in consistent formats. Don't choose new software before addressing other issues or reflexively adopt systems that happen to be in-house already. Instead, make prospective vendors show that their products can meet your needs in ways that suit your processes and people. If done properly, your performance management initiative can deliver improvement across the business and help you stay in front of the competition.

About Ventana Research

Ventana Research is the leading Performance Management research and advisory services firm. By providing expert insight and detailed guidance, Ventana Research helps clients operate their companies more efficiently and effectively. We deliver these business improvements through a top-down approach that connects people, processes, information and technology. What makes Ventana Research different from other analyst firms is our focus on Performance Management for finance, operations and IT. This focus, plus research as a foundation and reach into a community of more than 2 million corporate executives through extensive media partnerships, allows Ventana Research to deliver a high-value, low-risk method for achieving optimal business performance. To learn how Ventana Research Performance Management workshops, assessments and advisory services can impact your bottom line, visit www.ventanaresearch.com.