Robert S. Kaplan is Baker Foundation Professor at the Harvard Business School.

Kaplan joined the HBS faculty in 1984 after spending 16 years on the faculty of the business school at Carnegie-Mellon University, where he served as Dean from 1977 to 1983. Kaplan received a B.S. and M.S. in Electrical Engineering from M.I.T., and a Ph.D. in Operations Research from Cornell University.

Kaplan has a research, teaching, and consulting focus on linking cost and performance management systems to strategy implementation and operational excellence. He has been a co-developer of both activity-based costing and the Balanced Scorecard. He has authored or co-authored 14 books, 17 Harvard Business Review articles, and more than 120 other papers.

In 2006, Kaplan was elected to the Accounting Hall of Fame, and received the Lifetime Contribution Award from the Management Accounting Section of the American Accounting Association (AAA). Kaplan received the Outstanding Accounting Educator Award in 1988 from the AAA, the 1994 CIMA Award from the Chartered Institute of Management Accountants (UK) for “Outstanding Contributions to the Accountancy Profession,” and the 2001 Distinguished Service Award from the Institute of Management Accountants (IMA) for contributions to the practice and academic community.

David P. Norton is co-author of *The Balanced Scorecard: Translating Strategy into Action*. He is also co-author of *The Strategy-Focused Organization: How Balanced Scorecard Companies Thrive in the New Business Environment* and *Strategy Maps: Converting Intangible Assets into Tangible Outcomes*. He is co-founder and president of Palladium Group. Prior to his career at Palladium, Dr Norton co-founded and served as president and CEO of Balanced Scorecard Collaborative. He was also president of Renaissance Solutions, Inc., a Balanced Scorecard consulting firm, and co-founder and president of Nolan, Norton & Company.

Kaplan & Norton’s forthcoming book is called *The Execution Premium: Linking Strategy to Operations for Competitive Advantage*. Drawing on extensive research and detailed case studies from a broad array of industries, *The Execution Premium* presents a systematic and proven framework for achieving the financial results promised by your strategy.
Q: Hello and welcome. Can you tell us about the philosophy behind your forthcoming book The Execution Premium: Linking Strategy to Operations for Competitive Advantage?

Kaplan & Norton:

Most companies, in implementing the strategy management system based on the Balanced Scorecard followed a sequence we described in our second book, The Strategy-Focused Organization. They start with Principle 1, mobilize the executive team, followed quickly by Principle 2, translate the strategy into a strategy map of linked strategic objectives with an accompanying Balanced Scorecard of measures and targets, and Principle 3, align the organization through linked scorecards across business and support units. Principle 4, motivate and align employees required redesign of some key human resource systems, while Principle 5, make strategy a continual process, required the redesign of various planning, budgeting and control systems.

“...It is important for management to meet to address short-term operational problems. But it is also important for senior managers to meet to discuss their progress in strategy implementation.”

Typically, the implementation of Principles 4 and 5 did not start until the programme was one or more years down the road. In fact, we found that companies were able to get breakthrough results just by implementing Principles 1, 2 and 3 in their entirety and performing a few basic activities in Principle 4, such as a programme to communicate strategy to employees, and, following one practice in Principle 5, instituting a new management meeting to review strategy. This limited approach produced results until the leader who had introduced the programme departed. The message was clear; a strong leader using the tools of Principles 1, 2 and 3 could mobilize, focus and align the organization to achieve excellent performance. However, because the new approaches had not been embedded in the ongoing management systems of the organization (Principle 5), the performance was often not sustained. We had not yet found a way to embed the ongoing management of strategy into the organization’s way of doing business.

Through continued and intensive engagement with private and public sector enterprises in North America and Europe, we eventually identified all the key processes required to implement Principle 5, make strategy a continual process. The Execution Premium reports on these findings. In the book, we describe how companies can establish strong linkages from strategy to operations so that employees’ everyday operational activities will support strategic objectives. We introduce a new framework for management review meetings that solve short-term problems and monitor the improvement of key operational processes, from the meetings that review and improve strategy execution.

While we set out, in writing this book, to document the best practices for SFO Principle 5, we ended up with a self-contained and comprehensive management system that links strategy and operations by integrating the contributions from our four earlier books, and those of many other recent management innovations, including strategy development, operational management and improvement, activity-based costing, business intelligence, and analytics. The closed-loop management system described in this book represents the “end-state” that enterprises can aspire to reach for connecting excellence in operational execution to strategic priorities and vision.

Q: You quote one executive as saying “We have no time for strategy. If we miss our quarterly numbers we might cease to exist. For us, the long term is the short term.” How commonplace is this attitude within the business world today?

Kaplan & Norton:

We think it is common for several reasons. First, many companies still operate under the gun of Wall Street pressure for quarterly results. Since they use only financial measures to report their performance to analysts and shareholders, they don’t have a credible way of communicating their progress in enhancing customer relationships, improvement in critical processes, and aligning their employees’ motivations and competencies to strategic objectives. Thus, management meetings can become obsessed with meeting Wall Street’s short-term financial targets.

Second, those companies that have not yet implemented a management system based on their strategy rely mainly on the budget system for setting the agenda for periodic management meetings. By its very nature, the budget is short-term oriented and management spends the bulk of its time together trying to understand reported cost overruns and revenue shortfalls and developing action plans for coping with the problems.

Don’t misunderstand us. It is important for management to meet to address short-term operational problems. But it is also important for senior managers to meet to discuss their progress in strategy implementation. These are very different meetings, with different agendas and, usually, with different participants attending. We hope that having a management system anchored firmly in strategy will enable a new type of management meeting to occur, at which managers can debate and devise solutions to emerging problems in strategy execution.

Q: You state that breakdowns in a company’s management system - not managers’ lack of ability or effort - are what cause a company’s underperformance. Can you elaborate on this?

Kaplan & Norton:
In part, the breakdown, more the gap, in a management system is caused by the proliferation of diverse tools for strategy formulation and operational improvement that have been introduced during the past 30 years. Strategy development starts with tools such as mission, values, and vision (MVV) statements, along with external competitive, economic, and environmental analyses, which are summarized into statements of company strengths, weaknesses, opportunities, and threats (abbreviated as SWOT). Strategy formulation methodologies include Michael Porter’s Five Forces and Competitive Positioning Framework, the Resource-Based View of strategy, core competencies, disruptive strategies, and Blue Ocean Strategies. Companies also use scenario planning, dynamic simulations, and war-gaming to test the robustness of their strategies.

Strategy maps and Balanced Scorecards help companies translate, communicate, and measure their strategies. Some companies use the “catchball” component of the Japanese hoshin kanri policy-deployment process to cascade high-level strategic objectives to specific goals and targets for operating departments, followed by MBO systems to set goals for individual employees. Companies also employ TQM methodologies – six sigma, kaizen, and assessment methodologies from the Malcolm Baldrige and EFQM award programmes – to promote continuous improvements in the efficiency and responsiveness of their operating processes. For radical process improvements, they deploy re-engineering approaches.

Business intelligence software offers a myriad of tools to support strategy planning and the design of customized dashboards to facilitate operational improvement programmes. Companies use sophisticated analytic tools to review the performance of their strategies, including customer relationship management software and analytic modelling to capture and profile customer behaviour. Activity-based costing is used to assess product and customer profitability, key indicators of strategy success.

It is good that companies now have a large number of strategic and operational tools to choose from, but they still lack a theory or framework to guide the successful integration of the many tools. Companies struggle with the question of how to make these various strategy planning and operational improvement tools work together in a coherent system. The implementation of the tools is ad hoc, with little interchange and coordination. As a consequence, the tools don’t work coherently to drive results through the organization. Much of what we advocate is common sense; it’s a system that connects the dots among all a company’s myriad current tools and methodologies so that they can all be focused on an overarching goal: successful execution of a company’s strategy.

Q: Staggeringly, statistics indicate that 60-80 per cent of companies fall short of the success predicted from new strategies. From your research, what have you found to be the key reasons for this?

Kaplan & Norton:

First, the company’s leadership may not have clearly articulated the strategy and communicated it to the entire organization. Strategy cannot be implemented by the senior executive team. It requires that middle managers and front-line and service employees embed the strategy in their day-to-day activities. If middle managers and employees are not aware of or do not understand the strategy, they can’t possibly help in its execution.

Second, the company may not have thought through the need to integrate business and support units to the corporate strategy. Thus it never gets to realize the potential synergies from operating multiple units within the same corporate structure.

Third, companies often don’t allocate sufficient resources to initiatives and projects that are critical for developing the capabilities for strategy execution. Such strategic spending gets starved or subordinated to short-term operational concerns.

“Companies often don’t allocate sufficient resources to initiatives and projects that are critical for developing the capabilities for strategy execution.”

Fourth, companies continue to use the financial reporting and budget system as their primary management system. These systems allocate resources and report based on past performance but don’t help monitor and guide companies for future performance. Without a management system focused explicitly on strategy execution, companies will have considerable difficulty gaining clarity about the strategy, communicating the strategy, allocating resources for the strategy, reporting and learning about the strategy, and incentivizing managers and employees for successful strategy execution.

Q: Can you briefly describe what you mean by a “closed-loop” management system?

Kaplan & Norton:

We have formulated the architecture, shown in Figure 1, for a comprehensive and integrated management system that links strategy formulation and planning with operational execution. The system has six major stages.

Stage 1: Managers develop the strategy using the strategy tools described in a preceding section.

Stage 2: The organization plans the strategy using tools such as strategy maps and Balanced Scorecards.

Stage 3: Once the high-level strategy map and Balanced Scorecard have been articulated, managers align the organization with the strategy by cascading linked strategy maps and Balanced Scorecards to all organizational units. They align employees through a formal communication
process and link employees’ personal objectives and incentives to strategic objectives.

Stage 4: With all organizational units and employees aligned with the strategy, managers can now plan operations using tools such as quality and process management, re-engineering, process dashboards, rolling forecasts, activity-based costing, resource capacity planning, and dynamic budgeting.

“A distinguishing feature of the comprehensive management system is its explicit link between long-term strategy and daily operations.”

Stage 5: As the strategy and operational plans are executed, the enterprise monitors and learns about problems, barriers, and challenges. This process integrates information about operations and strategy in a carefully designed structure of management review meetings.

Stage 6: Managers use internal operational data and new external environmental and competitive data to test and adapt the strategy, launching another loop around the integrated strategy planning and operational execution system.

Q: What is the difference between a mission statement and a vision statement? Do these items have real practical value in business?

Kaplan & Norton:

Before formulating a strategy, managers need to agree on the company’s purpose (mission), the internal compass that will guide its actions (values), and its aspiration for future results (vision). The organization’s mission and values typically remain stable over time. The vision, although not as stable as the mission and values, is often constant during an organization’s three- to five-year strategic plan. Despite their stability, most organizations should begin their annual strategy development process by reviewing and reaffirming their mission, values, and vision statements. One chief executive officer stated, “The executive team must constantly remind itself of the foundations for what we are doing.”

The mission statement

A mission statement is a brief statement (typically one or two sentences) that defines why the organization exists. The mission should describe the fundamental purpose of the entity, especially what it provides to customers and clients (or, for public-sector and non-profit entities, citizens and beneficiaries). The mission statement should inform executives and employees about the overall goal they have come together to pursue.

For example, Google’s mission statement is remarkably brief yet powerful and understandable: “Organize the world’s information and make it universally accessible and useful.”

The values statement

Companies also should have a values statement (often called its core values). These describe the attitude, behaviour, and character that the company wants to follow. Whole Foods, on its corporate Web page, describes the importance of its core values better than we can express:

“The...core values reflect what is truly important to us as an organization. These are not values that change from time to time, situation to situation, or person to person, but rather they are the underpinning of our company culture. Many people feel Whole Foods is an exciting company of which to be a part and a very special place to work. These core values are the primary reasons for this feeling, and they transcend our size and our growth rate. By maintaining these core values, regardless of how large a company Whole Foods becomes, we can preserve what has always been special about our company. These core values are the soul of our company.”

The vision statement

Different from either mission or values is the vision statement. This defines the mid- to long-term (three- to ten-year) goals of the organization. It should be market oriented and should express – often in visionary terms – how the enterprise wants to be perceived by the world. The vision statement should contain three elements: a stretch target that is a discontinuity from the company’s present position, a time horizon over which the stretch target will be achieved, and the definition of the niche in which the company intends to operate and win.

The vision of Cigna Property and Casualty, an insurance company we worked with in the 1990s, was “to be a top-quartile specialist within five years.” Though short, this vision statement contains the three vital components:

Stretch goal: To be in the top quartile in profitability (at the time, Cigna P&C was at the bottom of the fourth quartile)

Definition of niche: To be a specialist, and not a general-purpose, underwriter, as it had been

Time horizon: Five years

The vision statement for a non-profit or government organization should define a stretch goal that relates to its mission. In 1961, US President John F. Kennedy offered one of the most famous and effective public sector vision statements when he declared that the US space programme would “land a man on the moon and return him safely to earth before the end of the decade.” In addition to the vision’s inspirational power, it described a clear measure of success and a specific time horizon.
Setting a stretch target and a specific time frame for achieving it in the vision statement is one of the most important roles of leadership.

Q: In planning operations you state that the goal is to align near-term process improvements with long-term strategic priorities. Can you tell us a bit more about this?

Kaplan & Norton:

A distinguishing feature of the comprehensive management system is its explicit link between long-term strategy and daily operations. Companies need to align their process improvement activities with strategic priorities. Also, funding for resources to operate the business must be consistent with the strategic plan. During the operational planning process, managers address the following two key questions:

1. Which business process improvements are most critical for executing the strategy? (Improve key processes)

The objectives in a strategy map’s process perspective represent how strategy gets executed. The map’s strategic themes originate in these key processes defined on the map. For example, a strategic theme to “grow through innovation” requires outstanding performance from the new product development process; a theme to “create heightened loyalty with targeted customers” requires greatly improved customer management processes. Some process improvements are designed to deliver the financial perspective’s cost reduction and productivity objectives, whereas others focus on excelling at regulatory and social objectives. Companies need to focus their total quality management, six sigma, and re-engineering programmes on enhancing the performance of those processes identified as critical for delivering the desired improvements in the strategy’s customer and financial objectives.

After identifying their critical processes for improvement, companies support their process management teams by creating customized dashboards consisting of key indicators of local process performance. The dashboards provide focus and feedback to employees’ process improvement efforts.

2. How do we link strategy with operating plans and budgets? (Develop the resource capacity plan)

The process improvement plans and the high-level strategic measures and targets on the Balanced Scorecard must be converted into an operating plan for the year. The operating plan has three components: a detailed sales forecast, a resource capacity plan, and budgets for operating expenses and capital expenditures.

Sales forecast

Companies need to translate their strategic plan’s revenue targets into a sales forecast. The beyond budgeting movement, mentioned earlier, advocates that companies continually respond to their dynamic environments by re-forecasting quarterly sales for five to six quarters into the future. Whether done annually or quarterly, any operating plan is launched from a sales forecast, a task facilitated by analytic approaches such as driver-based planning. Anticipating the need to derive a detailed operating plan, the sales forecast should incorporate the expected quantity, mix, and nature of individual sales orders, production runs, and transactions.

Resource capacity plan

Companies can use a time-driven activity-based costing (TDABC) model to translate detailed sales forecasts into estimates of the resource capacity required for the forecast periods. Activity-based costing has been widely promoted as a tool to measure the cost and profitability of processes, products, customers, channels, regions, and business units. But its “killer app” is for resource planning and budgeting. Because a TDABC model uses capacity drivers, typically time, to map resource expenses to the transactions, products, and customers handled by each process, such a model can easily translate the forecasts of sales and process improvements into the quantity of resources—people, equipment, and facilities—required to fulfill the plan.

“By separating the operational and strategy review meetings, companies avoid the pitfall of having short-term operational and tactical issues drive out discussions of strategy implementation and adaptation.”

Operating and capital budgets

Once managers have agreed on the quantity and mix of resources for a future period, they can easily calculate the financial implications (summarized in a financial profit plan) and operating and capital budgets. The company knows the cost of supplying each unit of resource. It multiplies the cost of each resource type by the quantity of resources it has authorized and thereby obtains the budgeted cost of supplying the resource capacity for the sales and operating plan. Most of the resource capacity represents personnel costs and would be included in the operating expense (OPEX) budget. Increases in equipment resource capacity would be reflected in the capital budget (CAPEX). The outputs from this process are operating and capital budgets that have been derived quickly and analytically from the sales and operating plan.

Because the company starts with detailed revenue forecasts and now has the resource costs associated with delivering these forecasts, simple subtraction yields a forecast and detailed profit-and-loss statement for each product, customer, channel, and region.
Q: Can you provide some brief guidelines for running successful strategy review meetings?

Kaplan & Norton:

Companies need operational review meetings to examine departmental and functional performance and to address problems that have arisen or persist. They conduct strategy review meetings to discuss the indicators and initiatives from the unit’s Balanced Scorecard and assess the progress of and barriers to strategy execution. By separating the operational and strategy review meetings, companies avoid the pitfall of having short-term operational and tactical issues drive out discussions of strategy implementation and adaptation. The two meetings address different questions:

1. Are our operations under control? (hold operational review meetings)

Companies conduct operational review meetings to review short-term performance and respond to recently identified problems that need immediate attention. Operational review meetings correspond to the frequency with which data are generated on operations and the speed at which management wants to respond to sales and operating data as well as to the myriad other tactical issues that continually emerge. Many companies have weekly, twice-weekly, or even daily meetings to review operating dashboards of sales, bookings, and shipments and to solve short-term issues that have just arisen: complaints from important customers, late deliveries, defective production, a machine breakdown, a near-term cash shortfall, the extended absence of a key employee, or a newly identified sales opportunity. Operational review meetings are typically departmental and functional, bringing together the expertise and experience of employees to solve the issues of the day in departments such as sales, purchasing, logistics, finance, and operations. These meetings should be short, highly focused, data driven, and action oriented.

2. Are we executing our strategy well? (hold strategy review meetings)

Typically, companies schedule strategy review meetings monthly to bring together the leadership team to review the progress of the strategy. The leadership team discusses whether strategy execution is on track, detects where problems are occurring in the implementation, attempts to determine why the problems are occurring, recommends actions to correct the cause, and assigns responsibility for achieving the targeted performance. If one thinks of strategy and problem-solving through the lens of the plan-do-check-act (PDCA) cycle, strategy review meetings are the check and act portions of strategy execution.

Theme owners distribute data on the Balanced Scorecard’s measures and initiatives in advance of the meeting. The meeting time focuses on discussion and selection of action plans for the issues that have emerged since the last strategy review meeting. Because in-depth discussion of every BSC objective, measure, and initiative would require too much time at each monthly meeting, companies now organize their strategy review meetings by strategic themes, covering one or two in depth at each meeting. In this way, they enable each theme and objective to be examined and discussed carefully at least once per quarter.

Q: With regard to business strategy in general, Deloitte’s Michael E. Raynor states “tomorrow rarely looks like yesterday…the unpredictability of the future makes it very difficult to know what to learn from the past.” Would you agree with his statement?

Kaplan & Norton:

It’s surprising that a CEO of a major consulting firm seems unable to learn from the past. I would say that we have learned that leadership is extremely important for choosing and leading strategies, and is likely to remain so in the future. Also companies need strategic direction, not just make incremental improvement to their existing operations. And companies need processes and systems to communicate and execute their strategies.

These are the lessons we have learned from the past 20 years that we expect will continue to be operative into the future. We have learned a great deal from the past on how to design management systems that help an organization direct their business units and employees in a coherent direction into the future. As far as what strategies companies can choose for the future, we have learned a great deal about the characteristics of successful strategies, about creating differentiation that is difficult for competitors to emulate, and whose gains cannot be quickly and fully appropriated by suppliers, customers, or substitutes.

Q: Finally, which articles or books would you say have had the most impact on your professional outlook, and why?

Kaplan & Norton:

Clearly, we have been influenced by Michael Porter’s books and articles on strategy, and also the many other writers and schools of thought on strategy. We wanted to design a management system that would be robust for all these strategy approaches. We wanted to be responsive to Henry Mintzberg’s pioneering work on allowing strategies to emerge from within the enterprise. Chris Argyris’s work on double-loop learning influenced our thinking on the need to test and adapt the strategy at least annually. We have attempted to incorporate the insights of Michael Hammer’s work on re-engineering, and the many contributors to the total quality management movement in general. Bob Simons’ work on Levers of Control (HBS Press, 1995), helped us understand how to use the Balanced Scorecard as the core of an interactive system, not just as a diagnostic system.

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Alistair Craven (acraven@emeraldinsight.com) is Web Editorial Coordinator at Emerald Group Publishing Limited.
Figure 1: The Management System for Strategy Execution Links Strategic Planning and Operational Execution

1. **DEVELOP THE STRATEGY**
   - Mission, Values, Vision
   - Strategic Analysis
   - Strategy Formulation

2. **PLAN THE STRATEGY**
   - Strategy Map / Themes
   - Measures / Targets
   - Initiative Portfolios
   - Funding / Stratex

3. **ALIGN THE ORGANIZATION**
   - Business Units
   - Support Units
   - Employees

4. **PLAN OPERATIONS**
   - Key process improvement
   - Sales planning
   - Resource capacity plan
   - Budgeting

5. **TEST & ADAPT**
   - Profitability Analysis
   - Strategy Correlations
   - Emerging Strategies

6. **MONITOR & LEARN**
   - Strategy Reviews
   - Operating Reviews

- **Execution**
  - Process
  - Initiative