



# Integrated Business Planning

*Taking Strategic Planning to the Competitive Edge*



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## The evolution of strategy

Strategy has become one of the most widely used, and misused, terms in business. Some leaders believe that strategy is the only way to compete in today's complex and fluid business environment; while others recognize the value of strategy but think strategic planning is dead.

To understand the evolution of strategy we must return to the fifth century where Greek military commanders known as Stratigos used formal strategic plans to win wars by focusing on individual battles. Stratigoi [ρ] typically served on administrative councils and were responsible for all aspects of war including recruitment, training, planning and of course, battlefield tactics.

Strategy, as defined by Liddell Hart in his book titled *Strategy*, is 'The art of distributing and applying military means to fulfill the ends of policy.'<sup>1</sup>

Strategy, as defined and applied by Grecian military and political leaders, was easily adapted for the business world by simply replacing the term 'military' with 'resources.'

Harvard Business School was one of the first institutions to introduce strategic planning methodologies for the business world. In the early 1920s Harvard introduced the Harvard Policy Model. In this formal model, strategy is defined by *a pattern of purposes and policies defining the company and its business.*

'The annual strategy review and planning process is like some primitive tribal ritual: there is a lot of dancing, waving of feathers, and beating of drums. No one is exactly sure why we do it, but there is an almost mystical hope that something good will come out of it.'

- Anonymous Corporate Executive

This was the accepted definition until the late 1950s when strategic planning turned from organizational policy and structure toward the management of risk, industry growth, and market share. Business recognized this approach to strategic planning as the portfolio model.<sup>2</sup> While management professor George Steiner, believed by many to be the father of strategic planning, boiled the essence of corporate strategy into the simple question, 'What should the organization be doing?'<sup>3</sup>

<sup>2</sup> H. Mintzberg, *The Rise and Fall of Strategic Planning* (New York: The Free Press, 1994)  
Note: Mintzberg refers to the Harvard Policy Model as the 'Design School Model.'

<sup>3</sup> Steiner, George A., *Strategic Planning*, (New York: Simon and Schuster, 1979).

Today, strategic planning remains a critical initiative for most companies' top brass. However, the impact or results from strategic planning is waning. In fact, many management gurus have come to the conclusion that strategic planning is nothing more than an exercise in futility.

While the concept of strategic planning still seems to have merit, the successful application of it has all but vanished. This is not surprising as most companies develop a strategic plan then revisit that plan on an annual basis. Globalization and emerging channels, combined with unprecedented change and generic uncertainty, is rendering the strategic plan to a static muscle that only gets flexed during the annual board meeting.

In a survey by the McKinsey Global Institute on Strategic Planning, one executive stated, 'The annual strategy review and planning process is like some primitive tribal ritual: there is a lot of dancing, waving of feathers, and beating of drums. No one is exactly sure why we do it, but there is an almost mystical hope that something good will come out of it.'<sup>4</sup>

While strategic planning may be under the gun, it can still help direct companies and improve

<sup>4</sup> McKinsey Global Institute, *Improving Strategic Planning*, Survey, 2006.

<sup>1</sup> Hart, B.H. Liddell. *Strategy*. (Meridian, 1991).

earnings provided the planning process:

- Captures the current situation or landscape in an accurate manner
- Uses forward-looking scenarios to determine the economic impact and risks from alternate investment choices
- Establishes the metrics and objectives that link the ultimate path chosen to operational planning and execution
- Effectively and efficiently identifies new market developments and recommends the best course of action

When done well, strategy planning can be a competitive advantage. According to Richard Rumelt, Professor of Strategy at UCLA's Anderson School of Management:

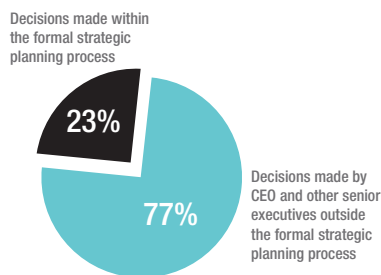
*'A good strategy, in turn, is one that is responsive to change and builds, builds upon, and stretches the resources that yield competitive advantage.'*<sup>5</sup>

However corporate executives, business unit leaders and dedicated planning managers, know all too well that strategic planning does not drive a company's critical decision making process.

More than 70% of strategic plans are nothing more than budgets rolling up and down the organization. According to Rumelt:

*'Most corporate strategic plans have little to do with strategy. They are simply three-year rolling resource budgets and some sort of market share projection. Calling this strategic planning creates false expectations that the exercise will somehow produce a coherent strategy.'*

#### How Important Decisions are Made



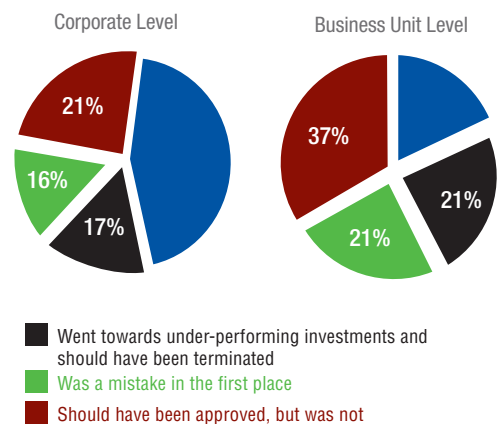
The McKinsey survey validated these statements and assumptions indicating that a mere 23% of a company's important strategic decisions are made within the formal strategy planning process. In other words, nearly 80% of a company's most important decisions are made either by the CEO or by small groups of senior executives, outside the formal planning process.<sup>6</sup>

McKinsey reports that despite CEO involvement and focusing on the proper areas or factors, resource allocation remains sub-optimal.

Non-integrated, disparate planning systems force executives and managers to make decisions using incomplete information and poor analytics, which causes resource allocation to remain sub-optimal.

Corporate executives report that 17% of the capital invested by their companies went towards underperforming investments that should be terminated. Another 16% of their investments were a mistake to have been financed in the first place. Even worse, another 21% of capital should have been approved, but was not.

#### Resource Allocation



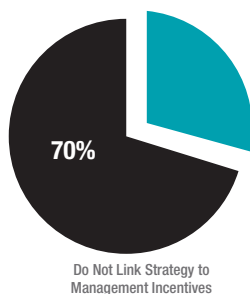
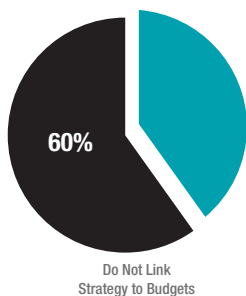
<sup>5</sup> Richard Rumelt, Professor, Anderson School of Management, University of California, Los Angeles

<sup>6</sup> McKinsey Global Institute, Improving Strategic Planning, Survey, 2006.

Drill deeper into the organization and the numbers worsen. At the business unit level, investments and capex are even more disappointing with 21% of the existing investments calling for termination; another 21% falling into the ‘should have never been approved’ category; while an astonishing 37% should have been approved but were not.

### Strategy and operational disconnects

A disjointed decision making process creates excessive costs and restricts an organization’s ability to identify, much less capitalize on, hidden or emerging opportunities.



After surveying 143 large companies, the Balanced Scorecard Collaborative/ Palladium, determined that 60% of the organizations do not link strategy with budgets. And for those that do, connectivity is limited to financials only.<sup>7</sup>

Additionally, 70% do not link management incentives to the attainment of strategic goals and objectives.

Planning managers and senior management are keenly aware of these ‘disconnects’ and are actively adopting new processes and investments in planning and business intelligence systems.

Management and academic ‘gurus,’ as well as several consulting firms, have proposed new methodologies to improve the planning process, including the Balanced Scorecard, Strategy Focused Organization, the Beyond Budgeting movement, and others. While these methodologies offer advanced processes and organizational model alternatives, they do not solve the real issue –integration.

<sup>7</sup> ‘Integrate and Conquer: River Logic’s Enterprise Optimizer Augments Balanced Scorecard System.’ The Palladium Group. 2007

Even with the support of the latest planning systems, fancy scorecards and so-called predictive analytics, planning executives and senior management still fail to make optimal choices as decisions become increasingly complex and require faster turnaround.

Planning systems are not integrated. This lack of integration restricts insight and understanding at the enterprise level. Therefore managers cannot evaluate strategic alternatives objectively, nor can they effectively allocate resources. Without understanding the company’s collective performance drivers, managers cannot determine priorities and economic ‘trade-offs.’

Non-integrated systems and inadequate planning and analysis capabilities force managers to make decisions without understanding the complete picture. In place of information, management is forced to use well-educated guesses and assumptions. And results from assumption-based activities can be devastating as each manager makes different assumptions.

#### A Case In Point

General George A. Custer decided to lead his troops into battle ahead of what his official orders called for. Without information about the size of his enemy or the terrain of Little Bighorn, he was forced to make assumptions; Assumptions that led to the demise of 210 soldiers in one of the worst military fiascos in the history of the United States Army.

## Over-extended assumptions

Planning assumptions tend to be over simplified and based on inaccurate understanding of the current situation. Managers, because their source of information is limited to historical data and events, fail to translate their organizational knowledge into accurate and insightful, forward-looking scenarios. Assumptions should only be made where facts are not available, such as future demand, competitor reactions, availability, future cost of talent, future input materials, etc. All else should be facts that help map the economic impact of assumptions made under different investment alternatives. Too many companies today make assumptions about costs, customer profitability, demand fulfillment capacity, cash flow and impact on balance sheet. In addition to repeatedly poor decision making, this overload of assumptions also prevents adequate linkage between strategy and execution.

Remember, General Custer had a solid strategy that called for segmenting his troops into three groups, then attacking his enemy on three sides simultaneously. But without real facts, strategy – no matter how insightful or brilliant will fail.

## When you assume

As noted in the McKinsey survey on resource allocation, assumptions are frequently over stated. Optimistic assumptions range from time and project completion rates, to sales impact, expected costs and production requirements.

RiverLogic and its partners have found instances where minor assumptions had a major impact on the company or project – in many cases erroneous assumptions led to incorrect answers that were as much as 200% off the mark.

Most assumptions can be traced back to one of the following:

- Failure to properly account for changes in input or energy costs
- Understanding marginal pricing and marketing implications of capturing additional growth, and its impact on profitability
- Understanding the behavior of costs, especially how fixed costs moved up or down with volumes of different product families
- Assuming or neglecting to properly evaluate impact on working capital
- Ignoring important constraints and penalties such as Wall Street's expectations, emission credit requirements and tax rates

## Interdependent relationships

After identifying the company's true performance drivers and variables, replacing assumptions with facts, and then comparing forward-looking scenarios, the manager or planner must turn to relationships.

While each functional silo is often disconnected at the strategic level, these disparate groups are indeed connected at the execution level. Therefore managers must account for the interdependencies across multiple initiatives when evaluating the impact of alternative strategic paths. While this integrated approach to planning is essential, it is not yet a common practice. According to McKinsey, 85% of the companies surveyed do not evaluate opportunities as dynamic, integrated portfolios.

Most strategies include elements for marketing, sales, finance, production and human resources. While these components may be independent, the actions in one area will have an impact on the enterprise, thereby influencing the value of any given strategy. Missing the impact across interdependent strategic initiatives often causes management to miss important nuances and can cause embarrassing and costly mistakes.

## The level playing field

Strategic alternatives are frequently compared to one another using different parameters and criteria. As a result, the quality of insight is marred and the decision making process is exposed to external, non-related factors including personal agendas, personalities, politics – even luck. For example, a billion dollar technology company wanted to close one of its production facilities that produced duplicate or similar product lines. Management, after evaluating each location, elected to close its west coast facility in order to reduce its average unit cost.

Months later only a portion of the anticipated savings was realized. The error occurred due to analyst bias. In other words, assumptions were used in place of facts and analysis. And when comparing the two facilities, different assumptions were made regarding the management of the remaining volumes. In one option the reallocation of production was fairly optimal from a financial standpoint, while the other was not. These assumptions were dependent on the subjective decisions of the analyst calculating the plan in place of analyzing production allocations and product mix rationalization. Consequently the company, comparing apples to oranges, failed to reduce unit cost through consolidation.

## A case in point

After completing their strategic review and planning process, the executive team of a multi-billion dollar technology company developed a strategy driven by four key initiatives:

1. Grow profitable product lines and services
2. Maintaining cash flow from so-called 'cash cow' products and clients
3. Reduce sales and marketing costs by cutting unprofitable products and channel partners, re-engineering sales roles and increasing the direct, online component
4. Consolidate and offshore elements of the supply chain

Additionally, these key initiatives were to be implemented while managing acceptable levels of risk, and avoiding disruptive events such as channel partner defections, supply disruptions, and significant changes in inventory.

Each of these strategic mandates produced several projects and initiatives. To address the product mix and cash cow mandates (items 1 and 2 above) management reviewed its historical data to determine unit contribution margins and the requirements for maintaining minimum revenues. Next, the team drew an arbitrary line across the product mix to isolate the cash cow product groups.

The team, after making the appropriate adjustments, witnessed a significant decline in cash generated from these products. Management, using 'backward-looking' information, discovered that a few of the cash cow products were negatively impacted by initiatives undertaken in other parts of the organization. These competing initiatives included channel partner composition, sales force restructuring, and changes in the supply chain.

If the team had a better understanding of how these interdependent relationships impacted the enterprise they would have selected different products. But because their model failed to consider market conditions and the financial ramifications of their choices, they missed significant growth opportunities. Specifically, the management team did not consider determining cash cow product lines after implementing the other key initiatives. An integrated model would have determined the optimal portfolio of initiatives. In this case, after implementing the required supply chain improvements and cost reductions, the team found a completely different mix of cash cow products.

Not properly understanding these interdependencies is why most capital expenditure proposals fall below expectations despite meeting the company's minimum ROI requirements.

This example, a classic case of 'you don't know what you don't know,' illustrates the need for broader understanding and insight across the enterprise. By understanding these interdependencies, managers can dynamically evaluate each initiative independently, as well as a portfolio of strategic, enterprise-level, investments.

Operating on an uneven playing field often opens the door to other subjective influences in the forms of management personalities and organizational politics – each contributing to the inefficient allocation of resources.

According to McKinsey, when corporate executives and business unit heads were asked to define what best explains the approval of the company's least successful project, 45% indicated it was because 'a senior leader advocated the project.'

Similarly, 51% of corporate executives and 63% of business unit heads believe executives in their companies form alliances with peers, or lobby someone more senior to push through their capex proposals.

Even worse, 31% of corporate executives and 35% of business unit heads believe executives hide,

restrict or misrepresent facts to get their projects approved. In addition to these challenges senior executives and strategic planners must address a number of obstacles including the process itself; increasing complexity; faster decision cycles; failure to link strategy to performance; backward-looking tactics, and the most important factor – the inability to determine financial outcomes for each scenario or plan.

### Integrated Business Planning

UCLA professor, Richard Rumelt, says:

*'Strategic thinking is essentially a substitute for having clear connections between the positions we take and their economic outcomes.'*

### Gartner

The technology analyst firm, defines Integrated Business Planning as: *A set of systems, processes, and competencies that forms the strategic alignment and modeling capability that is missing from the traditional operationally focused sales and operations planning (S&OP) processes. IBP links corporate performance management to S&OP, with capability for strategic and financial modeling and analytics.*

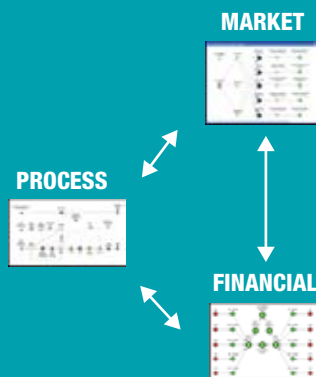
*- Hype Cycle for Business Intelligence and Performance Management, 2007*

To increase the impact of the strategic planning process, company executives and planning managers must identify and accurately quantify the economic impact of strategic alternatives. Each potential strategic measure or action must consider market, process and financial dynamics, and how these dynamics impact the organization as a whole. This is the essence of Integrated Business Planning.

Integrated Business Planning (IBP), by leveraging the organization's information assets, enables corporate executives, business unit heads and planning managers to evaluate alternatives based on the economic impact of each consideration.

## Implementing Integrated Business Planning Turns Strategic Planning into a Competitive Edge

- Higher, more profitable revenues
- Improved return on invested capital
- Quantified, more accurate risk management
- Flexibility to react to new situations and opportunities
- Stronger organizational alignment with company strategy



IBP provides for effective strategy development, and then links the strategy to operational planning and budgeting. Companies that take the knowledge and capabilities obtained during the strategic planning process and channel it to operational planning, gain a significant competitive advantage.

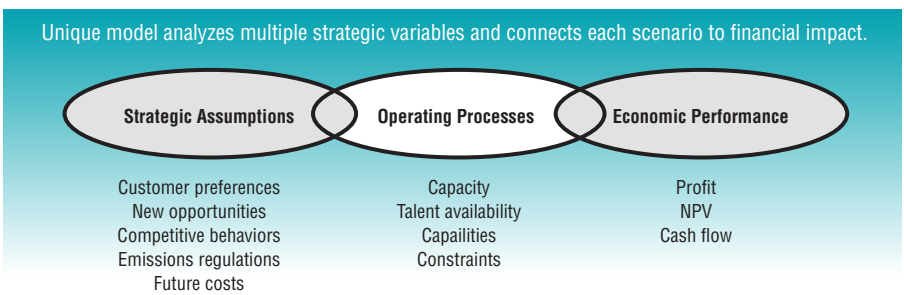
## Implementing IBP

There are 4 key steps to establishing an Integrated Business Planning capability.

1. A realistic and holistic model of the business that maximizes FACTS and minimizes ASSUMPTIONS
2. Support for multiple views that enable multi-variable planning
3. Advanced modeling capabilities with fast development of scenarios and analysis of output
4. Consider multiple levels of complexity and data over multiple timelines to support integrated strategic, financial and operational planning processes

### 1. A realistic, holistic model of the business

The core driver of Integrated Business Planning is an enterprise strategy model that accurately and realistically represents the company's situation on a past and 'forward-looking' basis. The model is unique because its analyses consider key



## Maximize FACTS and minimize ASSUMPTIONS

1. Consider all relevant factors in evaluating scenarios
2. Evaluate multiple variables simultaneously
3. Accurately represent interdependencies

strategic variables including demand expectations, pricing and elasticity, competitor behavior, emissions regulations, future input and labor costs. Next IBP maps these to key operating processes (capacity, capabilities, constraints), and economic performance (profit, NPV, cash flow) simultaneously and realistically to find the best decision under each scenario evaluated. Scenarios can then be segmented and analyzed by customer, product portfolio, network redesign, long-term recruiting and capacity, and mergers and acquisitions.

IBP enables managers to accurately project the financial outcomes of potential actions or plans, prior to execution. Another key advantage is the insight and discovery revealed during the process. Most IBP early adopters have significantly altered and optimized their business processes as a result of their integrated planning efforts.

The IBP holistic model provides 3 capabilities that reposition strategic planning as a competitive advantage.

Integrated Business Planning:

- A. Considers all relevant factors
- B. Simultaneously evaluates multiple variables
- C. Accurately represents interdependencies

### A. Consider all relevant factors

Core processes, costs behavior, constraints and financials are accurately represented at the right level of detail to replace previously made, high-level assumptions. This enables company managers to focus more of their time on structuring and analyzing strategic alternatives and the corresponding variables.

### B. Evaluate multiple variables simultaneously

This is a key short coming in relational, process, and spreadsheet-based models, which only solve for one or two problems. The model should enable management to consider multiple uncertain variables and to solve for many outcomes simultaneously.

### C. Accurately represent interdependencies

Strategic initiatives are rarely independent of each other. Therefore the model should enable users to model and quantify the impact of multiple strategic initiatives conducted simultaneously. This enables management to evaluate strategic initiatives as a dynamic portfolio versus strategic ‘one-offs.’

### 2. One set of facts; multiple views

The core Integrated Business Planning model enables corporate executives, business unit heads and planning managers to make strategic and financial planning decisions with the most accurate projection of economic impact; while simultaneously understanding the impact of their individual metrics.

Achieving this requires everyone to sing from the same song book. At the same time, executives, business unit heads and their planning analysts must be able to run their own scenarios to establish base projections, assess new ideas and evaluate different strategies. The model should provide the means for analyzing these scenarios within each group, while still providing the most accurate economic impact to the company. Additionally, this must be accomplished without disrupting the official strategic plan. Models that are under consideration but not yet blended into the company’s formal strategic plan are considered ‘unofficial.’

Once new ideas are accepted as potentially-viable strategies they can

be included in the latest strategy planning model and maintained by the corporate planning and strategy team. This team is also responsible for alerting management each time the latest, unofficial planning model is updated to enable assessment of strategic initiatives as parts of the enterprise’s dynamic portfolio.

### 3. Advanced modeling capabilities

Advanced modeling enables companies to understand their best choices or alternatives from a complete universe of choices.

#### More insight

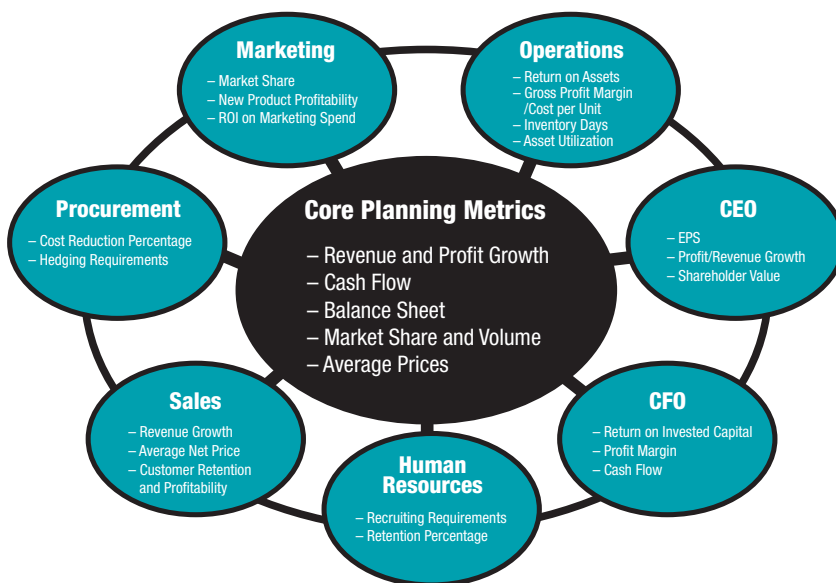
- What-if analysis
- Simulation/sensitivity analysis
- Optimization to any variable or objective function
- Infeasibility and “next best alternative”

#### More impact

- Full set of metrics and KPIs
- Resource allocation guidelines
- Alignment of targets and incentives

#### More flexibility

- Fast structuring and analysis of scenarios with multiple variables
- Easy to store, retrieve, analyze and share



#### 4. Support strategic, financial and operational planning processes

IBP provides the ability to model large scale, long-term decisions, as well as short term activities. IBP provides significant flexibility by providing scenarios using a number of options with varying levels of detail such as products, timeframes, workflows, access rights, etc. IBP can then link each scenario to the firm's strategic and operational planning activities.

Links between plans, budgets and forecasts are made via the guidelines, resources, metrics, targets and incentives defined in the strategic plan. Other links include:

- Explicit financial and operational guidelines from the strategic plans that define how the company competes. These include target markets, product introductions; process focus and objective functions (e.g., focus on cost vs. customer service, etc.)
- Resource allocation across strategic initiatives, business units and functions over time. This includes on-going maintenance funding, capital expenditures, market development and M&A resources
- Metrics, both financial and non-financial, include managerial business targets and may include minimum customer satisfaction,

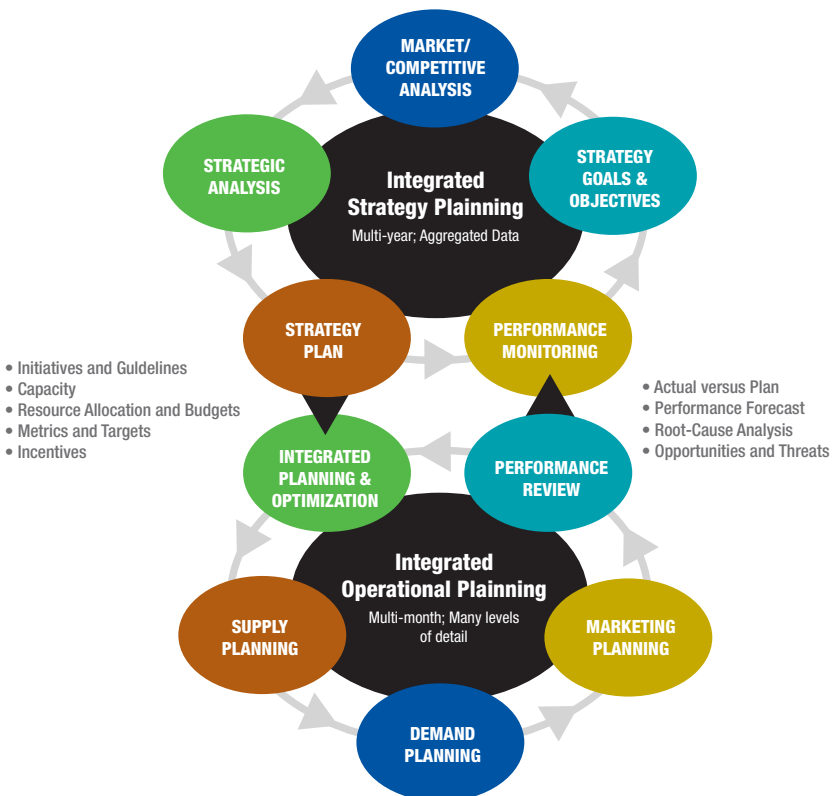
maximum risk exposure, and working capital constraints. Additionally, all critical metrics must tie to financials and be defined in terms of economic value

- Personnel incentives are directly connected to the achievement of targeted metrics within the strategy guidelines and resource specifications. This ensures behaviors, actions and rewards are aligned with the company's strategy

Best practice organizations use an expanded version of the Integrated Business Planning strategy model as the core planning driver for operational planning, S&OP (sales and operations planning) and financial budgeting and forecasting. These best practices enable companies

to simultaneously optimize operational plans, S&OP (or capacity planning in services) and financial planning initiatives for the best economic impact, while maintaining acceptable levels of risk. Key advantages include an accurate, holistic understanding of the economic impact from the plan. Other advantages include 'what-if' scenarios and simulations to optimize the entire set of decisions according to economic impact, while managing pertinent information for each department. This, in turn, drives organizational acceptance, guides behaviors and improves objectivity. This image below illustrates how Integrated Business Planning is connected at the strategic and operational planning levels.

**Strategy Planning Links to Operational Planning and Provides Platform for Continuous Improvement**



## A Case In Point

A well known, Fortune 1000 consumer packaged goods manufacturer has experienced significant growth over the past 10 years. In addition to exponential sales increases, the company's accelerated growth has increased the firm's operational complexities. While the company is proud of its continued growth, many senior executives have become frustrated by their inability to make 'big picture' decisions.

To address this issue and improve operational agility, the company deployed a fully integrated business planning capability that enables corporate executives, business unit heads and operational planning managers to conduct what-if analyses and identify the strategies and tactical

plans with the maximum economic impact.

Since deployment of the IBP solution, the company has improved its competitive position and realized a multi-million dollar improvement in profits. Additionally, several high-value strategic moves were discovered during the planning process. These insights, which were not possible with the company's legacy system, also strengthened the company's performance and delivered significant stakeholder value.

The company's vice president of planning indicated that his deployment of Integrated Business Planning has already delivered a return on investment in excess of 2,000%.



### Deployment guidelines

The following guidelines are helpful when evaluating Integrated Business Planning solutions. These guidelines apply to IBP applications used in strategic planning, operational planning, or a combination of the two.

The broader the solution deployed, including range of planning and number of users, the higher the value. Broad scope deployment maximizes company knowledge by using it to create relevant and meaningful insights derived through what-if questions, scenarios and simulations.

Applying the IBP solution to a wider set of problems will increase the value and impact of the solution exponentially.

The same is true for highly complex processes.

Although Integrated Business Planning can be applied at the enterprise level, it is not necessary to have an ERP system. IBP's holistic nature will use data from multiple, often new, sources, and will likely require some degree of data cleansing.

In terms of deployment timelines, most installations are accomplished in four to six months and deliver an ROI in less than twelve months. Most River Logic customers indicate an ROI of more than 1,000% within the first year.

For additional information on how to get more insight, more impact, more profit, in less time, contact

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### Separating fact from fiction

Integrated Business Planning is delivering a competitive advantage for innovative firms. IBP is here, now – delivering tangible value to its practitioners.

Moving forward, IBP is how businesses will address the increasing speed and complexity of their operations, while improving their position in the market place. IBP will continue to expand its reach as more and more progressive firms revamp their strategic planning efforts through effective integrated planning – And those that do will certainly outperform their competition by gaining more insight, more impact, and more profits – in less time.



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