

Today's Webinar Presentation

Managing Success: Mapping Strategy, Leadership, Culture and Control System

Presented by

*G. Brint Ryan College of Business
at the University of North Texas*

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Introductions



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MANAGING
SUCCESS
through
effective
management
control systems

Govind S. Iyer

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Agenda

- Management Control System
- Levers of control
- Organizational design
- Human behavior
- Responsibility accounting
- Managing Innovation
- Performance measurement
- Strategies and Control Systems
- Management Compensation

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Management Control Systems

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Definition

- Management control is the process by which managers *influence* other members of the organization to *implement the organization's strategies*.

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Alternative Definition

- Management Control Systems are the formal information-based routines and procedures managers use to maintain or alter patterns in organizational activities.

• Robert Simons

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Goal Congruence

- Good management control systems influence behavior in a *goal congruent* manner.
- Individual achievements lead to meeting of organizational goals.

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Goal Congruence Agency Theory

- Principals hire agents to make decisions for them and act on their behalf.
- Losses may arise because of
 - Agency issues
 - Incompetence
- Costs arise because of
 - Monitoring
 - Goal alignment
 - Contracting

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Agency Cost

- Monitoring and motivating performance
 - Delegating decision rights
 - Multiple measures of performance
 - Linking compensation to outcomes

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Important Questions

- What decisions should be assigned to the agent?
- What is the agent accountable for?
- How do we measure performance?
- What are the intended and the unintended consequences of our control system?

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Informal control systems

- Societal Norms
- Organizational culture
- Management Style

While formal management control systems are the focus of this course, realize that informal control systems **MUST** be considered in designing a formal system.

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Poll #1

- In my organization the role of culture in managing and measuring performance is
 - a) *Low*
 - b) *Medium*
 - c) *High*

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Levers of Control

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Levers of control

- Belief Systems
 - Credos, mission statements. *Core Values*.
 - *Rewards*
- Interactive Control Systems
 - Organizational Learning. Analysis of strategic uncertainties
 - *Experimentation*

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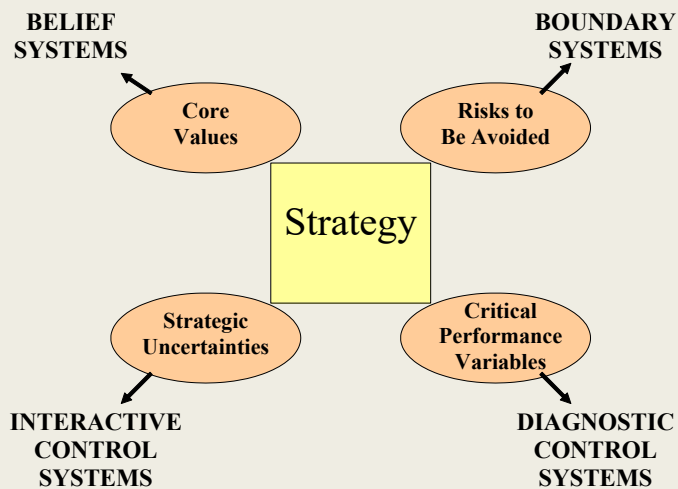
Levers of Control

- Boundary Systems
 - Limits and rules. Minimum standards.
 - *Sanctions*
- Diagnostic Control Systems
 - Formal feedback systems, preset standards, variances, analysis of critical performance variables.
 - *Periodic Reporting*

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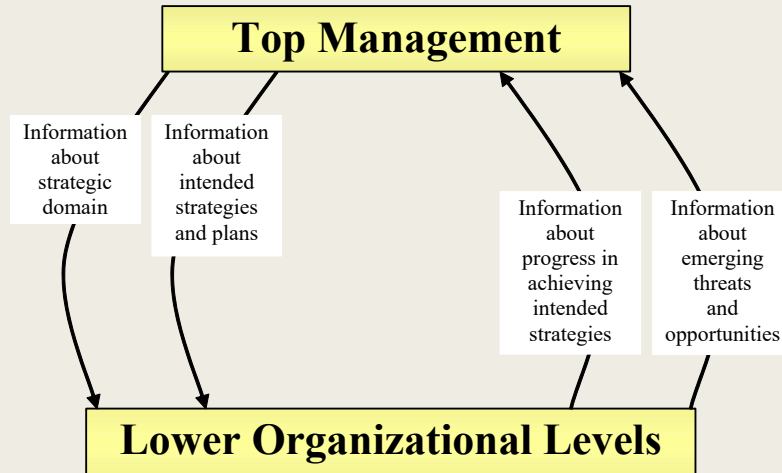
Levers of control



Simons, 1995, *Levers of Control*, Boston: Harvard Business School Press, p. 7

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Information Needs



Simons, 1995, *Levers of Control*, Boston: Harvard Business School Press, p. 6

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Organizational design

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Organizational elements

- Mission - Vision
- Organizational goals
 - *Financial goals*
 - For profit v. not for profit
 - ROE v. cost effectiveness?
 - Efficiency v. effectiveness?
 - *Strategic goals*
 - How to achieve financial goals
 - Cost leadership v. differentiation?
 - Both?

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Strategy formulation

- Deliberate strategies
 - *Traditional SWOT*
- Emerging strategies
 - *Based on real, on the ground experiences*
 - *Learning not SWOT*
 - *May become deliberative strategy later*

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Corporate v. Business unit strategy

- Corporate strategy
 - *Where should the company compete*
 - *Single industry versus related diversified versus unrelated diversified*
- Business unit strategy
 - *How to compete in the industry*
 - *Porter's five forces?*

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Mechanistic v. Organic MCS

Mechanistic	Organic
Motivation through pay	Motivation through contributing to goals
Specialized, defined responsibilities	Cooperation, teamwork and interaction
Hierarchic communication	Horizontal communication
Formal and tight	Informal and loose
Supervision	Encouragement
Internal focus	External focus
Narrow cost and productivity measures for evaluation	Broader and mainly non-financial measures for learning
Planning and budgeting	Flexibility and creativeness
Technology and routines	People and culture

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Poll #2

- The management control system in my organization is predominantly
 - a) *Mechanistic*
 - b) *Organic*

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Human behavior

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Principles

- Principle 1: Management control systems should motivate managers and employees
 - *Managers and employees should be motivated by the goals that they are asked to achieve*
 - *Managers and employees should be motivated by the rewards they may get from their efforts*

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Principles

- Principle 2: Management control systems should consider managerial and employee abilities and inabilities
 - *Managers and employees should be encouraged to learn and innovate*
 - *Managers and employees' tacit knowledge should be cherished*

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Principles

- Principle 3: Management control systems should support a healthy, social and ethical environment
 - *Culture matters (a lot) for management control system design and use*

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DNA element	Economic	Psychological	Sociologiaal
Control is about	Agency	Behavior	Groups
Control serves	Contracting	Motivation	Power, identity
Key control issue	Indicators to measure value creation	System to motivate managers	Enable individuals
Model of man	Self-interested in utility maximizer	Social creature with various needs	Culturally raised an educated team member
Focus	Superior manager's controls	Manager's behavioral patterns	Manager's identity, values and norms
Control practice	Measure and reward	Motivate	Congruence of identity values and norms
Motivation	Utility function	Complex (economic + psych)	Group needs

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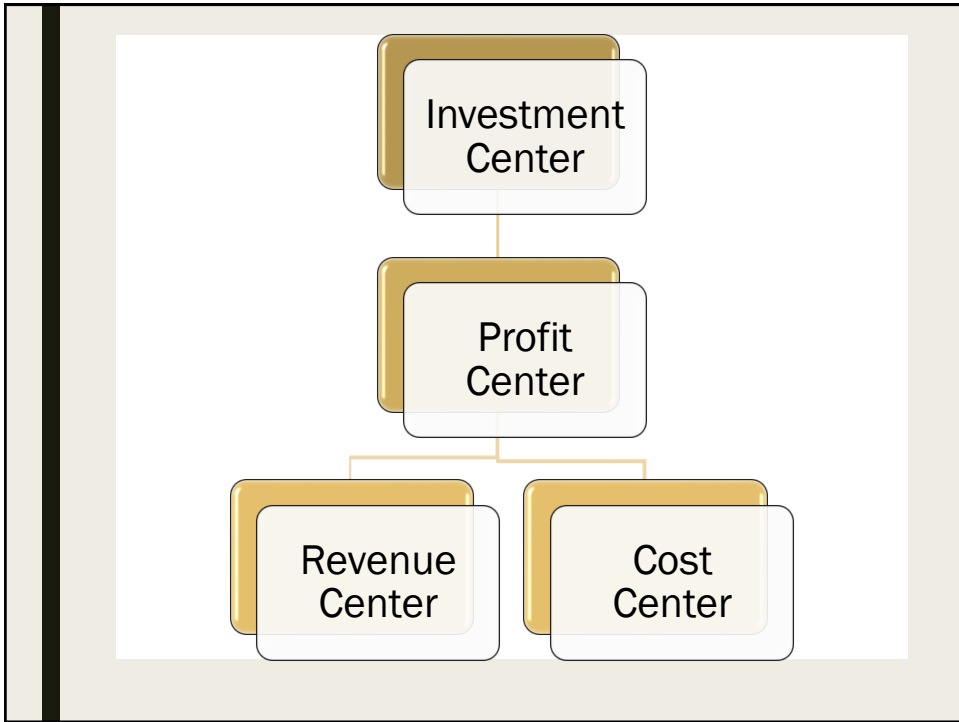
Poll #3

- The human behavior model underlying the control system in my organization is
 - a) *Economic*
 - b) *Psychological*
 - c) *Sociological*

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Responsibility accounting

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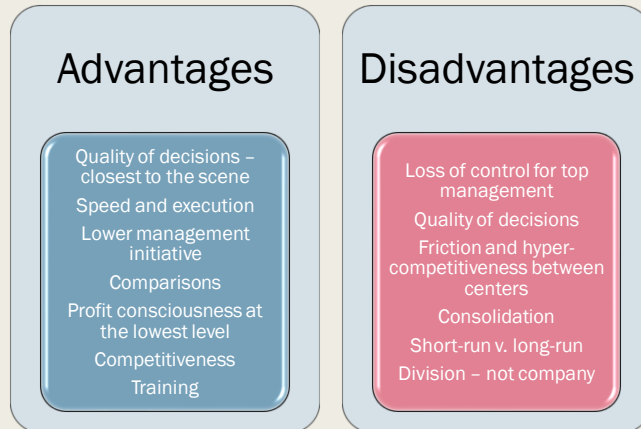
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Objectives and performance measures

Cost center	Revenue Center	Profit Center	Investment Center
<ul style="list-style-type: none"> • Cost • Minimize cost 	<ul style="list-style-type: none"> • Revenue • Maximize revenue 	<ul style="list-style-type: none"> • Revenue • Cost • Profit • Maximize profit 	<ul style="list-style-type: none"> • Revenue • Cost • Profit • Assets employed • Maximize ?

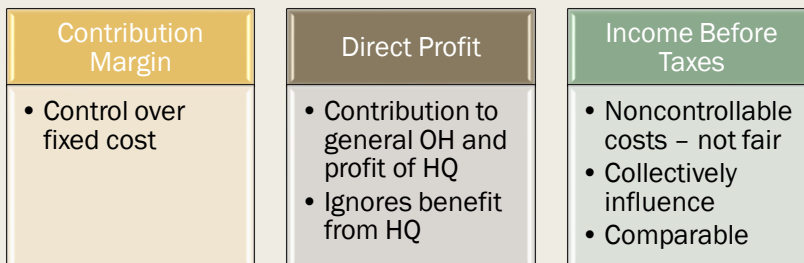
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Advantages and Disadvantages



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Measurement



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Poll #4

- The business unit I work in may be described as
 - *Cost or expense center*
 - *Revenue center*
 - *Profit center*
 - *Investment center*

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Matrix structure

- Functional v. Business unit
 - *Projects*
 - *Vertical and Horizontal*
 - *Reporting issues*
- Lean Management
 - *Resource efficiency v. Flow efficiency*
- Project management
 - *Waterfall v. Agile*

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Managing Innovation

(Adapted from "Ten rules for strategic innovators" Vijay Govindarajan and Chris Trimble.)

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Efficiency versus creativity

Efficiency

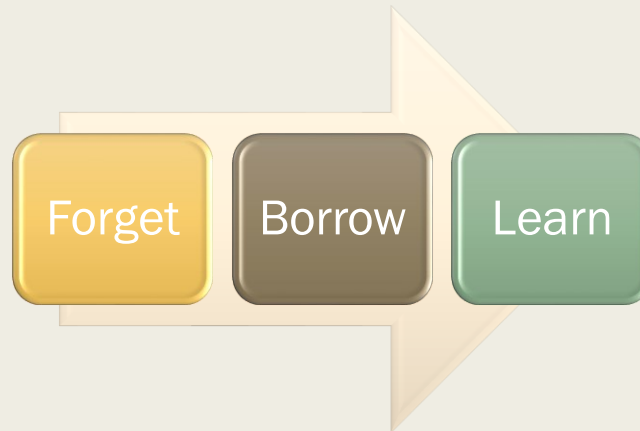
- Stick to your plan
- Exploit what you know
- Meet current customer needs
- Plan
- Demand accountability
- Impose structures, systems and processes

Creativity

- Think outside the box
- Explore what you don't know
- Anticipate future customer needs
- Let things happen
- Allow freedom and flexibility
- Encourage unstructured interaction

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Framework for Success



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Forget

- New company must forget existing company's success formula.
- During periods of stress, organization automatically reverts back to the old method.
- To be successful in forgetting, the organizational DNA for the new company must be different from the organizational DNA of the old company.

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Borrow

- New company has access to resources that independent start ups can only dream of.
- New company can get critical competitive advantage if it can borrow these resources.
- Too much and too close interaction will make it very difficult to forget.

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Learn

- New company must resolve critical unknowns in its business plan so that it can zero in on a working business model as quickly as possible.
- New company needs a much different planning process than the old company's – one that focuses on carefully resolving the disparities between predictions and outcomes and emphasizes learning over accountability.

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Three S and One C

DNA element	Indicative of	Existing company
Staff	Leadership style, staffing policies, competencies, promotion policies, career paths	Operational experts, internal promotions, known and established career paths.
Structure	Formal reporting structures, decision authority, information flows, task and process flows	

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Three S and One C

DNA element	Indicative of	Existing company
Systems	Planning, budgeting and control systems, evaluation criteria, incentive and compensation systems	Planning and budgeting are critical. Focus in on individual/unit/department accountability (as compared to plan). More fixed compensation.
Culture	Notions about behaviors that are valued, embedded business assumptions and decision biases	Business assumptions are deeply embedded in the organization and passed on from generation to generation. Risk averse

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Poll #5

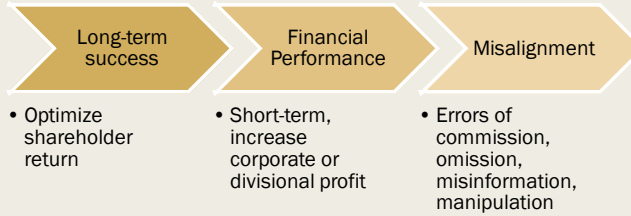
- My job function demands
 - a) *Efficiency*
 - b) *Creativity*

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Performance Measurement - Strategy maps and balanced scorecard

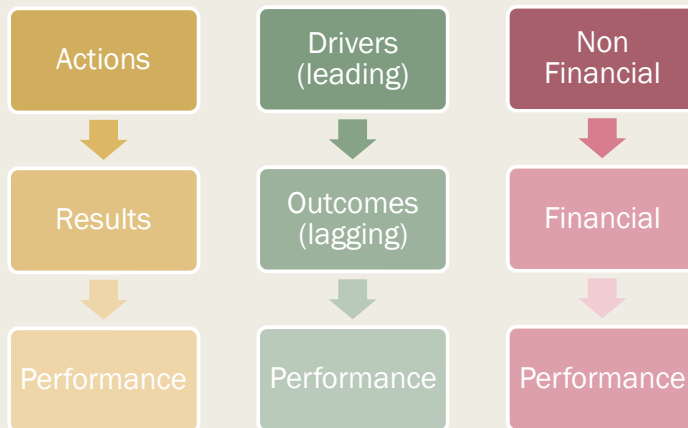
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Financial Performance



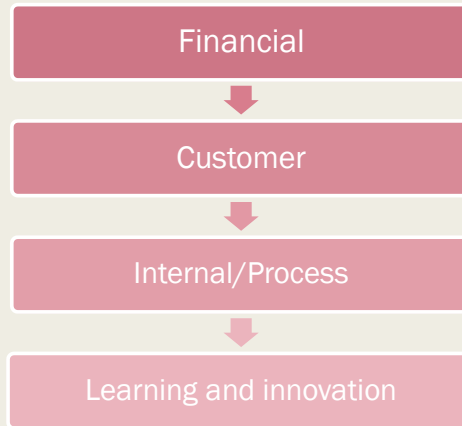
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Performance Measurement



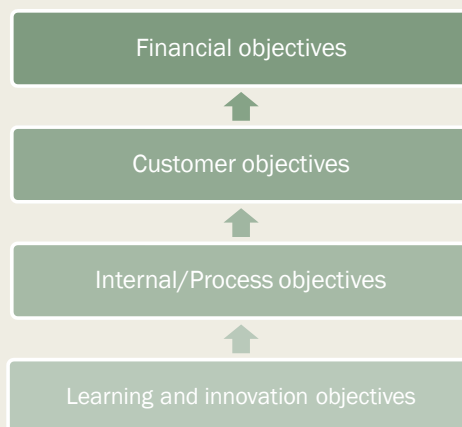
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Strategy Map



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Linkages



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Balanced Scorecard

Perspective	Objective	Measure	Current	Target
Financial				
	State goals (4 or 5)	Specific metrics	Current period value	Target value
Customer				
	State goals (4 or 5)	Specific metrics	Current period value	Target value
Internal/Process				
	State goals (4 or 5)	Specific metrics	Current period value	Target value
Learning and Innovation				
	State goals (4 or 5)	Specific metrics	Current period value	Target value

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Measurement using a BSC

Getting it right

- Measurement using BSC is meaningful only if the BSC is well constructed

How many measures?

- Too few measures may not capture what needs to be captured, while too many measures may dilute and distract the manager

Comparing employees

- It may be more difficult to compare employees, even more so when their BSCs contain different measures

Weighting and biases

- If the BSC does not contain any explicit weights, assigning implicit weights and distilling a single performance measure can be cognitively a difficult task

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Other systems

- SMART
 - *Specific Measurable Achievable Realistic Timely*

- OKR
 - *Objectives and Key Results*

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Poll #6

- My organization uses a “Balanced score card” for performance measurement and management
 - a) Yes
 - b) No

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Strategies and control systems

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Types of industries and control systems

Aspect	Single Industry	Unrelated Diversified
Organizational Structure	Functional	Holding company
Industry familiarity	High	Low
Functional background	Operating experience	Mainly finance
Decision making authority	Centralized	Decentralized
Corporate staff	High	Low
Internal promotions	High	Low
Lateral transfers	High	Low
Corporate culture	Strong	Weak

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Types of industries and control systems

Aspect	Single Industry	Unrelated Diversified
Strategic Planning	Vertical cum horizontal	Vertical only
Budgeting – relative control of BU manager	Low	High
Importance attached to meeting the budget	Low	Mainly finance
Transfer pricing importance	High	Low
Sourcing	Constrained	Arms length
Bonus calc	Financial and non financial	Mainly financial
Bonus based on	BU and corporate performance	BU performance
Bonus determination	Subjective	Formula based

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Types of strategies and control systems

Aspect	Build	Harvest
Importance of Strategic Planning	Relatively High	Relatively low
Formalization of capital expenditure decisions	Less formal DCF analysis, longer payback	More formal DCF analysis, shorter payback
Capital expenditure evaluation criteria	More emphasis on non financial data	More emphasis on financial data
Discount rates	Relatively low	Relatively high
Capital investment analysis	More subjective and qualitative	More objective and quantitative
Project approval limits at business unit level	Relatively high	Relatively Low

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Types of strategies and control systems

Aspect	Build	Harvest
Role of budget	Short term planning	Control tool
Influence of BU manager	High	Low
Revisions	Easy	Difficult
Frequency of informal reporting	Frequent on policy, less frequent on operations	Less frequent on policy, more frequent on operations
Frequency of feedback	Less often	More often
Control limit on periodic evaluation	High	Low
Importance to meeting the budget	Low	High
Output v. behavioral control	Behavior control	Output control

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Types of strategies and control systems

Aspect	Build	Harvest
% compensation as bonus	High	Low
Bonus criteria	Non financial	Financial
Bonus determination	More subjective	More formula based
Frequency of payment	Less Frequent	More Frequent

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Management Compensation

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Performance Measures



Rewards are better than punishment



Monetary rewards have diminishing returns



Senior management's actions regarding management control systems are extremely important



Feedback is essential – helps control outcome

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Performance Measures

Incentives are less effective as the time lag between action and feedback increases

Motivation is an inverted U curve – low when easily attainable and low when unattainable

Participatory budgeting creates greater motivation than imposed budgets

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Management Compensation

Salary – benefits – incentive compensation

Greater ratios of bonuses tended to have subsequent better financial performance.

Consultants are normally employed to assist in management compensation contracts.

Incentive bonuses must be approved by shareholders

Incentive plans can be short term or long term

Short-term – linked to current performance
– overriding criteria is to be competitive

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Issues to consider

- Performance of business unit managers based on comparing year to year performance.
- Performance of subordinate managers based on relative performance with each other.
- Forced ranking (bell curve like IE). For instance, 10% of the workforce in each department must be rated "lowest performers."
- Bonus only after achieving a minimum performance level
- Earned bonus paid over a period of time
- Stock or stock options vesting with the manager over a period of time

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Issues to consider

- Objective versus subjective performance measures
- Performance measures for merit rewards (compensation) and performance measure for promotion.
- Biases in performance measures - likeability, similarity to self, gender, marital status, looks, fixation on financial performance, loyalty, fear of being superseded etc.
- Motivational issues with group rewards versus individual rewards

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Issues to consider

- Role of performance measures - assessment, judgement, feedback?
- Role of performance-based compensation - motivation or reward?
- Effectiveness of different performance measures in different cultures.
- Role of psychological and social rewards, when are they appropriate?

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Issues to consider


- How do you motivate an already motivated workforce? When BSC targets are all already met or exceeded, how do you maintain motivation?
- Let us look at the flip side – the issue of managing during tough times. How do you increase (or at least maintain) employee motivation during such times?
- Are experiences from one company transferable to others?

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Final thoughts

- Final thoughts?
- Questions?
- Comments?

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thank you!

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