Risk Reduction Advice from a Legend

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Balanced Scorecard Co-Creator Dr. Robert Kaplan's New Ways to Improve Communications and Risk Management

By Joe Mullich

In formulating strategic plans, senior executives tend to overlook two key elements: effectively communicating those plans to the employees who must execute them, and factoring in what might go wrong with the plans.

So says Dr. Robert S Kaplan, "Baker Foundation Professor" at Harvard Business School and co-creator of the Balanced Scorecard, and co-author of many books-the most recent being *Execution Premium: Linking Strategy to Operations for Competitive Advantage.*

"You have to communicate the plans to employees seven times in seven ways" for them to understand those plans, he says. "At the end, they need to understand the organization's strategy and understand what they can do to contribute to the success of the strategy."

Dr. Kaplan points to Volkswagen Brazil, a half-century-old subsidiary of the carmaker, as a successful example of effective employee engagement, motivation, and communication when implementing a turnaround strategy. Volkswagen Brazil had suffered eight straight years of losses, falling from number one to number three in market share in the country.

"Their only strategy was cutting and downsizing," Dr. Kaplan says. "The unionized employees were alienated." To turn that around, "they needed to capture the hearts and minds of the people. They wanted a strategy of growth and innovation, and that starts with culture."

A new executive team was brought in to transform the company. The head of Human Resources, with the support of the CEO, led the project. The process started with a strategy map, a simple diagram of a company's core business strategies that typically lists a small number of interlinked items. Volkswagen Brazil developed a very simple strategy map, with the top two elements-customers and financials-shown in the colors of Brazil, a potent reminder in light of the country's recent World Cup success. To remind employees of the importance of the initiative, a strategy map was put on the wall in every single room of the company-and keep in mind Volkswagen Brazil is so large it has four manufacturing plants.

Volkswagen Brazil took other unusual steps to communicate strategy, including games that drove home the message. "They also created a robot called Giga, which looked like a Volkswagen Beetle," says Dr. Kaplan, adding that Giga went around and talked with the employees about strategy.

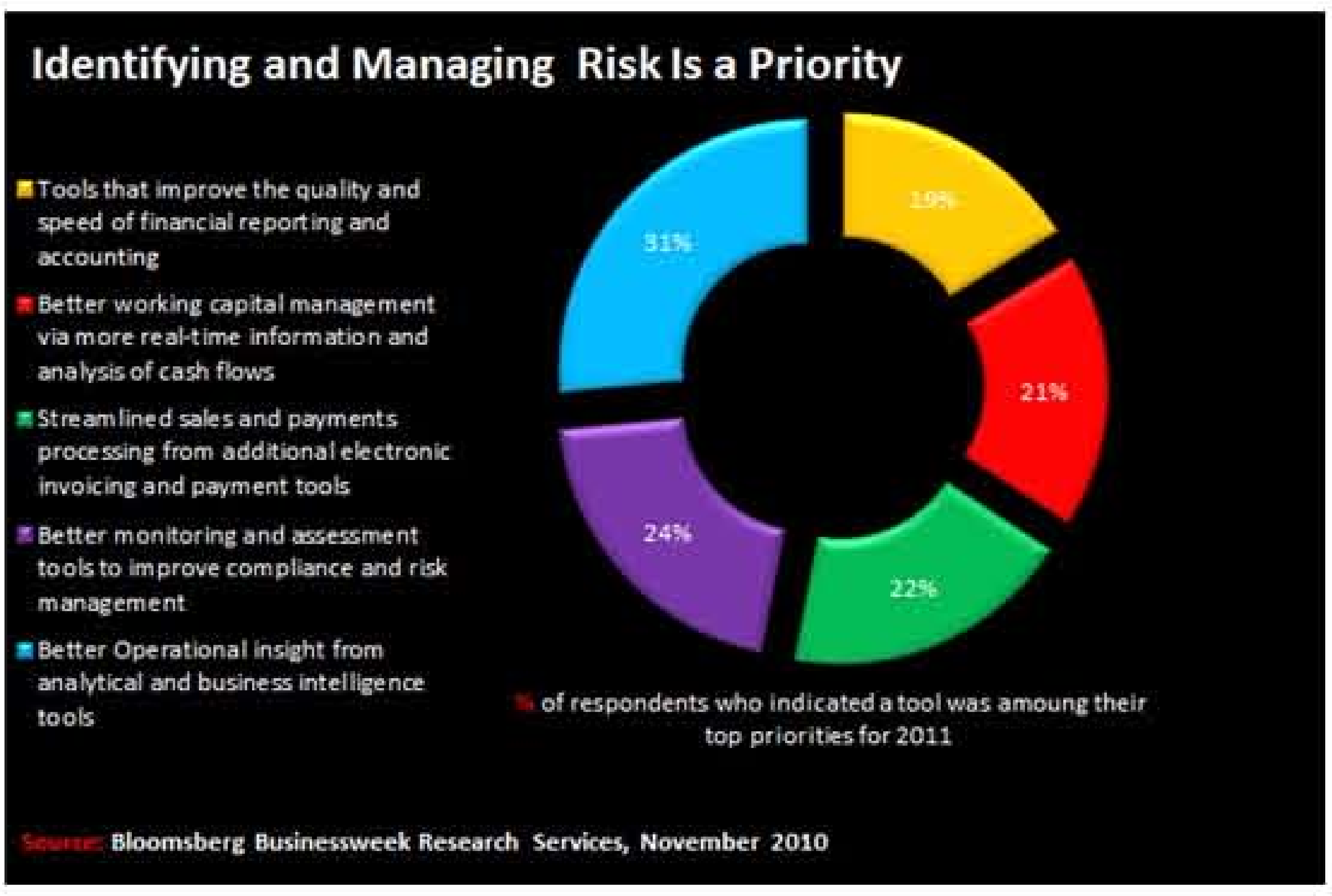
The results of clearly delineating and explaining the strategy had a staggering impact. Morale improved dramatically, and employee engagement soared. For example, the company's 22,000 employees contributed more than 13,000 suggestions. "I could see the improvements as I walked down the assembly line," Kaplan says. "There were ideas for new car development, but they also extended to suppliers and dealers."

After the initiative was launched, revenue grew from $6.7 billion to $9 billion in just two years. Volkswagen went from number three in market share back to number one. This type of success, Dr. Kaplan says, must be underpinned with accurate data that presents managers with a single version of the truth, allowing them to monitor how well their strategy is working.

"You want monthly management meetings for reviewing strategy, and you don't want to spend time on where the data came from and how it was measured, because that isn't the point. The data is supposed to trigger problem-solving discussions and mid-course corrections."

Dr. Kaplan says another key element of strategic planning-risk-is often overlooked, because most company cultures discount it and it is difficult to calculate. "It is the most difficult measurement I've ever encountered," he says. "Measurement is about what happened in the past, even leading indicators. Risk is about what may happen in the future, but may never happen."

Indeed, most companies are paying more attention to identifying and managing risks, according to a November 2010 survey by Bloomberg Businessweek Research Services. Better tools to monitor and assess risks ranked as the second highest operational priority for the 300+ companies that responded to the survey. Note that the percentage citing these types of tools as a top priority increased by four percentage points in one year.



Although most companies develop key performance indicators (KPIs), Dr. Kaplan says they should be linked with an emerging metric called key risk indicators (KRIs). British Petroleum (BP), for example, "followed a risky strategy, drilling in deep water more than a mile below the surface. That's OK," he says, "because-as they say-no risk, no reward. Where I second-guess them is if you are going to take a risky strategy, you need to beef up the risk [management] function."

As part of strategic planning, Kaplan encourages executives to study their strategy map and objectives and to think about what could go wrong, to create a complementary early warning strategy. For example, he says BP, knowing it was pursuing a risky strategy, could have installed or created sensors that provide an early warning if a pipe seal is failing.

"People don't want to think about what can go wrong," Dr. Kaplan says. "They get excited about what works. It's counter-cultural to think about what could go wrong."

For these reasons, Dr. Kaplan believes it is important to keep risk management a separate function from strategic management, rather than make risk a department within the Strategic Management Office. He sees value in maintaining "tension" between the strategy and risk functions. "If risk got inside the strategic function," Dr. Kaplan says, "it might become subservient to strategy-instead of the equal partner-which it should be."

For more insights from Dr. Robert S. Kaplan, **watch this video:**