

Creating value with performance management

Coloplast

Case Study | Anders Olesen, Partner, CFO Services





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CREATING VALUE WITH PERFORMANCE MANAGEMENT

By Anders Olesen
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Coloplast has achieved great success with their performance management method, which has much in common with Basico's general Performance Model; see fig. 1.

In the previous issue of Content, we described our Performance Model, which is practical and useful when helping companies translate strategy into action. You will find a more detailed description of the model in the September 2018 issue of Content.

The overall purpose is to create the foundation for unleashing/realising the company's full potential. In our view, it is actually more about enabling performance than about managing performance. The prerequisite for this is a holistic and coherent management model, which results in the desired behaviour throughout the company.

Background

Coloplast has been on a fantastic journey over the recent ten years. When the company embarked on this journey, its performance was rather poor compared to that of its competitors. Today, Coloplast ranks

among the world's best performing and most valuable medico companies. Not least because of the company's efficiency and earnings performance, which is exceptional and the highest within their industry.

The purpose of Coloplast's impressive journey has constantly been to become the world's best performing medico company, and in this respect focus on performance management was decisive.

The company's finance department was already familiar with the Beyond Budgeting principles,

and the leadership change ten years ago became a welcome occasion to put them to the test. This combination turned out to be extremely beneficial for Coloplast's development.

In 2009, Anders Lønning-Skovgaard was Director of Performance Management in the finance department. It was thus natural for him to assume a key role in the ensuing transformation. Anders led the project team that, over the following twelve months, implemented a totally new planning model referred to as: "Turning Ambition into Action".

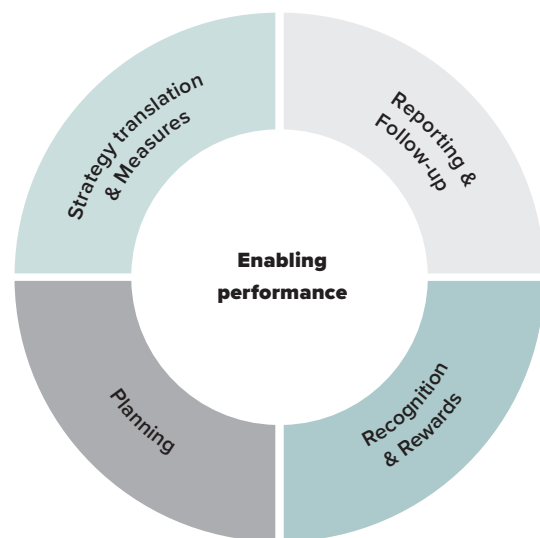


FIGURE 1: BASICO'S PERFORMANCE MODEL

This is how we lead in Coloplast



FIGURE 2: THIS IS HOW WE LEAD IN COLOPLAST, SOURCE: COLOPLAST

Already then, Coloplast was – together with Basico – active in the Beyond Budgeting network, and right from the start we have followed Coloplast’s Beyond Budgeting journey with great interest. Under the headline “No more budgets”, Content featured an article on the beginning of their journey in June 2010.

Coloplast’s management model

“Our management model is focused on value creation. This is at the core of our way of managing. And this is reflected in our processes and tools, which have been developed to support our leadership principles and overall strategy. This connection is extremely important for our ability to execute effectively”, says Anders Lonning-Skovgaard.

Coloplast’s management model has much in common with Basico’s Performance Model (figure 1), and in the following we will describe this briefly.

In general, the purpose of the model is to create value by ensuring coherence between strategy and action.

Strategy translation and measures

On the basis of the company’s mission, vision and values, Coloplast has developed a strategic plan with a three-to-five-year horizon at Group level and for each business area. These plans are prepared on a relatively high level (i.e. with limited details). They outline the direction and ambition level, and they contain the most important priorities and activities. Ambitions are high and help create a winning mentality.

Based on the strategic plan, Coloplast develops one-year plans, which they refer to as their Agenda. These plans contain the most significant activities within each of the strategic areas: innovation, customers, efficiency and leadership.

The Agenda helps translate the overall strategy into specific activities. It is an important internal communication tool as it helps employees focus on what to do next in order to create value in the longer term.

For each of the strategic goals and activities, the KPIs have been defined that are best at answering the important questions: “Are we moving in the right direction?”, “Is the customer satisfied?”, “Are we doing the right thing?”, “Are we making progress?”, and “Are we moving fast enough?”.

In this connection, Coloplast uses forward-looking KPIs (leading indicators) and non-financial measures such as number of new patients.

Reporting & follow-up

“We focus on the relatively few key figures that say something about our ability to create value.

Great efforts have been made to secure the quality of these data, which means that we now have meaningful and value-creating discussions when we report and follow up on these key figures. Our reporting and follow-up is consistent across business areas, regions and functions”, says Anders Lonning-Skovgaard.

Especially, the high data quality, the standardization of reporting formats as well as the manner in which business reviews are made have contributed to increased insights and a much higher process quality and efficiency. ▶

CONTACT US

How do you get started?

We hope that this article, which illustrates the value of a coherent management model, has inspired you to explore the potential in your company. If so, we recommend that you seek assistance for your journey.

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"We have truly achieved one set of numbers, and it is of utmost importance with such transparency in our data", says Anders Lonning-Skovgaard.

What is also interesting is that their reporting focuses on the development of realized data; i.e. they focus on trend analysis of key measures. Contrary to many other companies, Coloplast makes almost no variance analyses since it is a lengthy and (in most cases) worthless exercise.

Planning

When Coloplast introduced its new management model, the company wanted to avoid the many negative side-effects related to the traditional annual budget process.

"Our budgets were not coherent with our strategy, they resulted in wrong and undesired behavior, we spent oceans of time making them, and, on top of that, they were useless a few months into the accounting period", Anders

Lonning-Skovgaard explains and continues: "There is a risk of traditional budgeting taking place locally, in parallel with and in addition to the established processes on group level. We are aware of this and are constantly striving to streamline these."

A core element of Coloplast's model was to replace the annual budget by processes that were far more efficient and designed to solve the specific challenges.

In this connection, Coloplast chose to follow the general recommendation from the Beyond Budgeting network: For each of the budget purposes (ref. figure 3: Ambition, Forecast, Capital Allocation and Incentives), Coloplast established a new and separate process.

"This method increased the quality of our work substantially, and at the same time, we avoided the problems associated with the annual budget", says Anders Lonning-Skovgaard.

Membership of Beyond Budgeting Round Table

Anders Lonning-Skovgaard:

"We have been a member of BBRT since the start of our journey in 2009. Initially, this provided us with important inspiration for developing our new management model. It is still very useful to be a member of BBRT. For example, we urge new employees to attend BBRT meetings since it gives them a good network and a better understanding of our management model."

Now, Coloplast prepares quarterly rolling forecasts that cover the following five quarters. Their forecasts contain far fewer details than previously, and it has increased agility and provided a far better overview than before.

The new Capital Allocation process, in particular, has increased agility and contributed to improved decision-making. "It has been one of the most important contributions to our value creation. We have an investment committee that meets monthly and evaluates the

investment proposals received. Investments are accepted or rejected depending on their contribution to our strategic agenda, the potential for value creation, alternatives, as well as whether sufficient cash flow is available. The absence of annual budgets and pre-allocated investment pools increases our ability to quickly allocate our resources to where they create most value", stresses Anders Lonning-Skovgaard.

With regards to the balance of the external financial guidance, Anders Lonning-Skovgaard

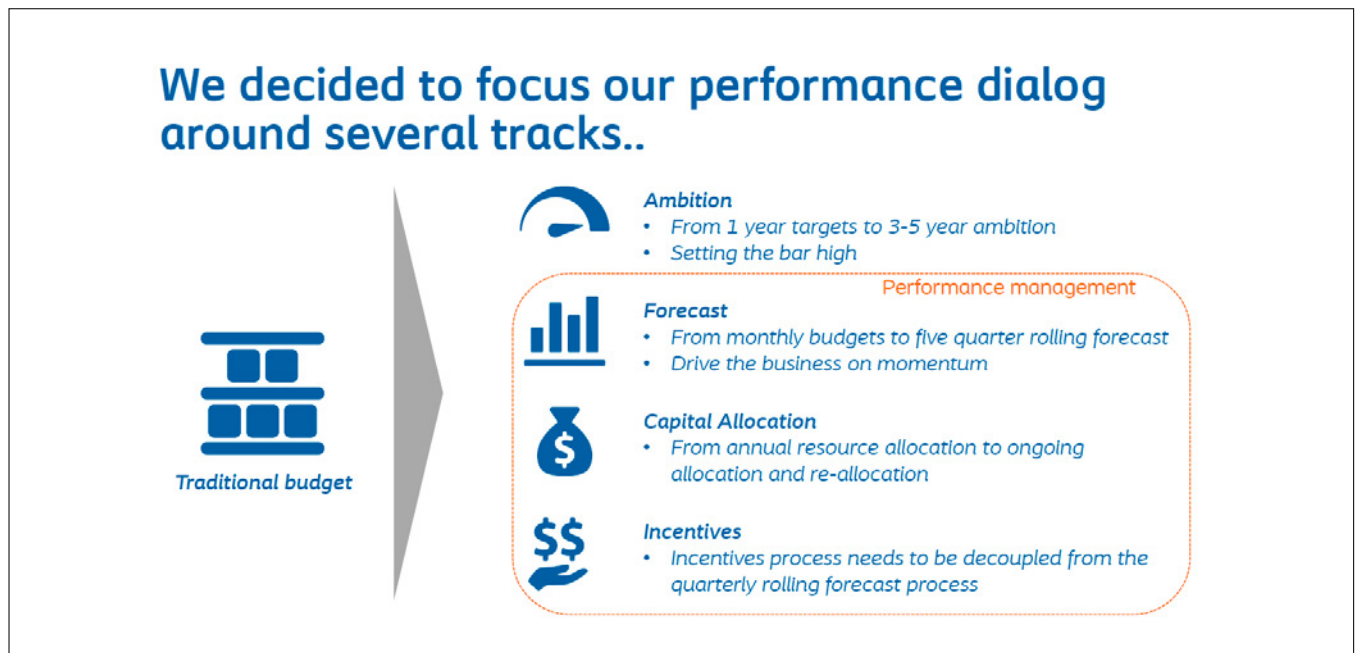


FIGURE 3: WE DECIDED TO FOCUS OUR PERFORMANCE DIALOGUE, SOURCE: COLOPLAST



Photo: Coloplast

CFO ANDERS LONNING-SKOVGAARD

Coloplast since 2006:

- Executive Vice President & CFO since 2014.
- Earlier: Chief Information Officer, Director of Performance Management and Finance Manager.
- Project manager for the implementation of Beyond Budgeting and a new management model.

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says that the secret is to remain focused on both short-term and long-term goals: "Sometimes you have to postpone an otherwise good, long-term investment in order to protect the guidance. It is an act of balance for management to safeguard the results and guidance in the short term without jeopardizing motivation. The aim is to work dynamically with the capital allocation to ensure that resources are continuously invested where the return is the highest; just as the resources should be re-allocated should investment cases develop contrary to expectations, and if new opportunities appear."

Recognition & rewards

Coloplast has also come far in this respect. Now, they have bonus systems that support the overall strategy and they have rooted out and abolished most individual bonus goals. The latter is an important, but often overlooked element: In brief, individual bonus goals will, more often than not, result in undesirable behaviour and constitute a considerable complexity (cost).

At Group and head office level, Coloplast only works with common goals, and elsewhere in the organization, it is now the general rule to establish common

(regional/local) goals.

"The challenge is that it takes time to get the right mind-set in place and to make people accept that they cannot affect their bonus directly", says Anders Lonning-Skovgaard.

This was the last field that Coloplast delved into when they introduced their new management model.

With the wisdom of hindsight, this should have been on the agenda earlier. The point is that the management model should be coherent at any time; this requires one to work with these areas in parallel rather than consecutively.

Next step

Coloplast has come far, but the company is constantly striving to optimise its model and processes.

One focus area is digitalisation: Coloplast uses Power BI extensively in order to support and improve the quality of their reporting and data analysis.

"We still spend too much time in our production and supply chain planning in too much detail, so this also has our attention", Anders Lonning-Skovgaard concludes. ■



Value creation in Coloplast

Coloplast's management model has had a dramatic impact on value creation. Since its introduction ten years ago, Coloplast has been one of the most successful and value creating of the listed companies in Denmark (Nasdaq Copenhagen)

- Turnover has doubled during the period. The market share has increased considerably in all major markets.
- Earnings (EBIT margin) have been at 30-34 per cent for several years. This is the highest – and approx. twice the median – in their industry.
- Coloplast's customer and patient satisfaction ranks at the top of the most recent Patient View Survey.
- Coloplast is one of the most innovative and forward-looking companies in this industry. Investments in R&D account for 4 per cent of turnover.
- As of January 2019, the market capitalization of Coloplast is DKK 127 billion, which is higher than that of far larger listed companies on Nasdaq Copenhagen.
- During the ten-year period, the shareholders have had an average annual return on investment (CAGR) of more than 25 per cent.

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