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Think Functionally, Act Strategically

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BY DENIZ CAGLAR, NAMIT KAPOOR,
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What should the role of the corporate support function be in business strategy? Until recently, the answer was relatively straightforward. System-wide, service-oriented functions existed to carry out the many specialized tasks that every corporation needs to have done. Human resources (HR) recruited employees, managed benefits transactions, and oversaw evaluation and promotion practices. Information technology (IT) ran and helped support the company's computer systems. Finance carried out all processes related to accounts, debts, and taxes. Learning and organizational development offered training programs tagged to the skills the company needed. Legal vetted contracts and managed issues related to compliance. And so on.

Though much has been written over the years about the strategic importance of HR, IT, finance, and other support functions, in most companies their roles

have been primarily transactional. They fulfilled day-to-day needs, met legal and regulatory requirements, accommodated requests from business units, and put out the inevitable fires that erupted when there was a conflict or urgency. When functional leaders were asked to make improvements, it meant doing the same things more efficiently and at a greater cost savings.

Recently, however, there has been a leap in expectations. Over the past few years, CEOs, business unit leaders, and functional leaders themselves have been asking support functions to deliver more value to the organization at large. Instead of balancing services among all business units equally, or striving to be best in class in everything, support functions such as HR, IT, and finance are asked to be “fit for purpose”: more closely aligned to the enterprise strategy. Functions that are more directly related to individual brands and busi-

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ness units—which may include operations, sourcing, marketing, sales, and R&D—have also been affected, though not always in the same way as their counterparts at corporate headquarters. This leap is occurring for several reasons.

First, market environments and patterns have become less stable, and competitive intensity has increased. Many companies—facing changes in customer demand, the emergence of innovative new competitors from around the world, and greater macroeconomic uncertainty—are raising expectations accordingly. Today's functions must provide a far more complex set of activities and expertise than they ever had to manage in the past. For example, IT must design systems that mine “big data” to support real-time consumer offers that change on the fly; HR must recruit a broad range of people from around the world and design flexible career tracks to match their diversity.

There is also a new opportunity to raise the return on discretionary investment. Over the past decade, through outsourcing and process improvement, many functions have become more efficient in performing their day-to-day activities. Therefore, the resources dedicated to routine, transactional tasks—managing HR benefits, dispensing IT equipment, resolving finance discrepancies, maintaining mailing lists, and so on—have been dropping. Such tasks now consume perhaps 35 percent of staff time, whereas they once consumed 70 percent. This development enables functional leaders to allocate more time, attention, and money to discretionary activities, the strategic tasks that can make an organization more competitive.

In addition, the pressure to execute flawlessly is increasing. Most functional departments have made great

strides in maximizing efficiency and improving operations. But they usually still have a lot of room for improvement, forcing many functional leaders to look for new paths to operational excellence and greater value, usually while reducing costs.

Finally, many companies have become aware of the power of distinctive capabilities, that is, the advantage held by companies that do only a few things in the market, but do them exceptionally well. Amazon's success is based on its skill with online user interfaces, logistics, and technology. Coca-Cola's success depends on its prowess in beverage creation, brand proposition, and global consumer insight. Hyundai gained its enviable foothold in the U.S. automobile market through stylish car design and marketing combined with disciplined quality improvement (*see “Hyundai's Capabilities Play,” by William J. Holstein, s+b, Spring 2013*). Functional leaders face the difficult challenge of supporting these complex new capabilities while not compromising what they already do.

For all these reasons, the role of corporate staff functions is expanding in many companies. These businesses are investing more in their global corporate staff, and are deploying functions such as marketing, R&D, and sourcing across all the business units in the enterprise. Corporate functions already have a more prominent seat at the strategy table than they used to, and are increasingly influential in setting and executing the corporate capabilities agenda.

Together, these changes give functional leaders a mandate to think and operate more strategically than they did in the past. They are rewarded less for providing a service bureau that fills all requests, and more for their effectiveness and discernment, for emphasizing

the activities that differentiate a company in the market, and for finding less expensive or more comprehensive ways to deliver the rest. They are also being asked to focus, for the first time, on resolving function-related conflicts among different parts of the larger organization (for example, conflicts over incompatible IT systems or redundant talent initiatives). Every function, local or global, should define its role in light of the overall capability agenda, and how it can be fit for purpose in driving that agenda—instead of thinking first about how to fulfill its functional excellence agenda.

Consider, for example, the story of the finance staff at a large North American consumer packaged goods company. For years, they had focused on a single dimension of their role: as the “cost police” for the business units, processing transactions, tracking expenses, and holding down costs, even when it meant constraining growth. Then, in the wake of the Great Recession, the CEO asked the chief financial officer to cut finance’s operating costs by 20 percent.

The CFO and his direct reports met to consider the measures. Staff members were already stretched thin, and this would stretch everyone further, possibly past the breaking point. The mood around the table was glum. Then the CFO said, “If we’re going to do this, we’ll do it in a way that delivers more value to the business—not less.”

Over the next few weeks, the CFO and the top finance team met one-on-one with the managers of some of the largest business units to talk about finance’s operating model and where the department’s help was most valued. These conversations, which had never before been conducted in that company, led to a quiet reorganization. In some areas—such as due diligence for

acquisitions and postmerger integration—the finance team increased investments. For consultative cost management, they designed a leaner operating model, incorporating new metrics for effectiveness and value delivery. They also outsourced routine and transactional activities such as standard financial reporting. Perhaps the most important change was in the reorganization of the financial planning and analysis staff. Under the old structure, these staff members had been embedded in business units around the world; they replaced this structure with a centralized staffing model, reinforced by service-level agreements with the heads of all the business units. This gave the finance team a higher level of accountability for local results than they had had before, while gaining efficiencies and cost savings. The top leaders of the finance function took on more of an advisory role, consulting with business unit leaders on key decisions—such as where they should channel their investments for growth and how to manage and control costs. That had the beneficial side effect of helping business units plan ahead, reducing some of the urgent last-minute calls that drain every functional group.

Within six months, the new system had freed up more than 20 percent of the finance function’s budget—and a fair amount of executive attention. This was particularly helpful in making and integrating acquisitions; the success rate for “onboarding” new enterprises grew visibly. Because finance now managed business unit costs more actively, the cash available for reinvestment was identified more accurately. The function’s new agenda provided the company with a clearer picture of the return on investments; it helped the company overcome its ingrained reluctance to share information

and services across business unit boundaries. In short, finance now played the kind of strategic advisory role that made a significant contribution to the company's top line as well as to its bottom line.

Choices and Commitments

If you are a leader in a corporate function, you may have a similar story to tell. The changes in your role may feel challenging or unfamiliar at times, but they represent a golden opportunity for you and everyone in your senior team and department. For years, you may have sought more opportunities to bring your specialty to bear, not just in day-to-day services, but in defining and developing the company's distinctive edge. Now, the chance is finally here. In fact, in many industries, it's become an imperative.

To be sure, you still have to manage your own house. Transactional tasks remain; businesses continue to demand service. You are still judged on your operational effectiveness and efficiency. Senior management may send mixed signals; it isn't always clear how to resolve conflicts between the day-to-day needs of individual businesses and the long-range, in-depth efforts needed to build distinctive capabilities. Many things that you would like to see improved, including some highly important cross-functional initiatives, are outside your control or jurisdiction, yet seem to require your involvement and influence. Moreover, if your enterprise (like most) is struggling with incoherence—not quite able to settle on an overarching direction that is appropriate for all its products, services, and priorities—then the function you lead will undoubtedly struggle as well. Different businesses will make contradictory demands of you, you won't be able to fulfill them all, and you

won't always know how to bring them together. Managing these types of situations requires a high level of leadership skill.

How, then, can you take on this new strategic role, maximizing your effectiveness, without being torn into pieces? You can accomplish it only by changing the way your function conducts business, overcoming the inertia of embedded habits and practices, and putting strategic activities first, before the usual long list of critical tasks and service requests. That is the purpose of the new functional agenda.

Like many other strategic exercises, converting to the new agenda begins with a statement of the value proposition: your company's chosen way to play in the market, how it intends to attract and hold customers. This is, of course, set at the enterprise level, but it is incumbent upon you as the functional leader to understand and articulate it in the context of your specialization. Will your company distinguish itself as an innovator, launching technologically sophisticated products and services? Will it be a value player, outpacing rivals through lower costs? Will it provide a compelling customer experience? Or will it forge some other way of delivering value?

In every successful company, the value proposition is closely linked to the firm's most critical capabilities: the things it has learned, over time, to do particularly well. Inevitably, functional leaders are involved in defining, building, and maintaining these capabilities. Thus, you need a clear understanding of the company's overall value proposition, of the capabilities required to fulfill it, and of the role your function plays. To start, divide all the capabilities that your function provides into three broad categories:

Being best in class in every process or activity simply isn't possible; no function has the funds or organizational stamina to be excellent at everything.

- **Basic business capabilities** are the capabilities needed to keep the company running. These services—which include payroll, employee benefits administration, and basic computing services—remain the responsibility of the functions. They are critical but non-differentiating. They should be tightly controlled for efficiency, and often automated, outsourced, or relegated to low-cost shared services, thus freeing up resources that functional leaders can redirect to differentiating capabilities (see *“Is Your Company Fit for Growth?”* by Deniz Caglar, Jaya Pandrangi, and John Plansky, s+b, Summer 2012).

- **Competitive necessities** are the “table stakes” that enable a company to compete in its industry. In many companies, these include logistics, sourcing, back-office processes, and integrated IT architecture. They are essential to survival and success, but they can often be managed for cost and efficiency, rather than for performance at a world-class level, or even at the same level as competitors.

- **Differentiating capabilities** provide a company with the distinctive advantage needed to outperform competitors. Most of these capabilities are cross-functional; they gain their power from the fact that different functional proficiencies fit together in ways that other companies cannot easily copy. For example, Procter & Gamble’s innovation capability, as chronicled during the years that A.G. Lafley was CEO, was not related solely to its R&D function. Financial reviews, product design and manufacturing, and immersive market research were closely involved. The Swiffer WetJet mop was developed when a launch team, in visit after visit to consumers’ homes, saw them struggling with conventional mops. Truly differentiating capabilities demand

(and deserve) a major share of investment and attention from every function that contributes to them.

As a functional leader, you must recognize which capabilities fall into which categories—and balance your resource investments accordingly. All three can be costly to build and maintain, and many functions have gotten used to spending more on competitive necessities and basic business capabilities than they should. Differentiating capabilities get shortchanged as a result, and when that happens a company can easily lose ground.

Being best in class in every process or activity within a given function simply isn’t possible, no matter how professionally satisfying; no function has the funds or organizational stamina to be excellent at everything. Instead, you need a clear sense of which category each activity falls into. There must be some activities in which being merely adequate is appropriate, where “good enough” is actually good enough.

This can be a very difficult path. Many people within your function, and in the business units you serve, will push back on the idea that their day-to-day capabilities need less investment. In the short run, you still need to tailor your approach to the individual priorities of every business, and to your organization’s culture. But in the long run, if you don’t have a clear and consistent idea of the right trade-offs and priorities, you will never muster the capital or attention you need to fulfill your strategic imperative.

Blueprint for an Operating Model

With a more conscious approach to channeling investment, the pressure to execute effectively has increased. A functional blueprint is a plan spelling out how to accomplish this: how you will deliver the most value to the

You may have to shift from a service bureau orientation, where your role is to fulfill every request, to a more strategic approach, where you sometimes have to say no.

Measuring Functional Performance

Every function's first priority should be to support the building and management of differentiating capabilities. Therefore, it is essential to define and measure explicitly just how much value each function is delivering. You can use four distinct indicators to assess this value.

1. Quantifiable impact. Measure all the function's activities against definable business outcomes that are aligned with the company's strategic priorities and tied to a specific time frame. A centralized consumer insights capability, for instance, might be measured by the reduction in the number of weeks required to develop

new products during the next 18 months.

2. Clear drivers of value. Identify the sources of your function's greatest contributions to the enterprise. Improved demand management might depend, for example, on having sophisticated analytical tools that can provide streamlined access to data, greater scale, and the bundling of expertise. Metrics should establish the degree to which these tools exist and are used.

3. Cost-effectiveness. Continue to track the relationship between expenses and outcomes. Your function's contribution to the enterprise—measured through financial performance improvement in revenue or profit—must outweigh the cost of its activity.

4. Internal market validation. Seek out and incorporate feedback from your clients and constituents

within the company, to drive your function's effectiveness and efficiency wherever possible. This may include the use of charge-backs, service-level agreements, and make-versus-buy assessments (analysis of whether to build a capability in-house or outsource it).

Leading companies deploy rigorous processes and tools to ensure the alignment of ongoing and proposed functional activities and investments with the functional priorities and the operating model, and to ensure maximum value creation. Within the context of continuing pressure on support budgets, this helps functional leaders allocate their resources to the activities with the highest value.

organization as a whole, how you will work together with other functions to ensure the delivery of the greatest value, and how you will continually raise performance.

In developing the blueprint, you should rethink decision rights (who has final approval), processes, and tools. The way you measure performance should also be explicitly defined, both at the functional level and at the level of each function's specific activities (*see*

"Measuring Functional Performance," above). The blueprint defines a number of key elements that may have gone unexamined in the past. For example, you may revisit the roles and responsibilities in your organizational structure, along with existing patterns of centralization and decentralization. Differentiating capabilities tend to benefit from having global centers of excellence, or even an organizational structure designed around them

(see “Beyond Functions,” by Paul Leinwand and Cesare Mainardi, *s+b*, Spring 2013). Competitive necessities, which are requisite for every company in an industry, may naturally involve more decentralized operations—or, alternatively, may fit best in shared services. Many basic business capabilities can be outsourced.

Collaborate with business leaders and your counterparts in other functions to make these decisions. For example, a distinctive product development capability may require setting up common activities across IT, R&D, marketing, and sales. The marketing and sales functions will need to improve their market-sensing capabilities to understand what the customer wants, and R&D and product management will need to draw upon those insights in designing new features. IT will be called on to provide an underlying infrastructure to support knowledge transfer and collaboration. What conversations do you need to arrange, among which individuals, to ensure that these new systems and structures are in place?

Leading from Within

If you are a functional leader, your role is more challenging than ever before. You are a critical player in every aspect of capabilities: identifying them; designing the processes, tools, and practices that enable them; and executing the strategy through them. Your personal leadership qualities—your interpersonal skills and strategic insight—are a primary source of success not just for the function, but for the enterprise as a whole. In your most important work, on differentiating capabilities, you share authority with other functions and departments, instead of maintaining unilateral control. You need a level of credibility and integrity high enough

that you can counsel business unit leaders, even telling them hard truths—for example, that their priorities conflict with those of the overall enterprise.

As the company becomes more coherent, you may often be called on to help build or develop differentiating capabilities—and to help discard investments that no longer fit. That may mean shifting abruptly from a service bureau orientation, where your role is to fulfill every request, to a more strategic approach, where you help set and maintain priorities and sometimes have to say no. Even as its leaders espouse greater coherence, your organization may not move smoothly in that direction. Everybody tends to think that the number of projects should go down, starting with everyone else’s projects. In those organizations that embrace coherence, too much centralization can be a weakness; you will also have to guard against top-down rules and practices in your function that stifle creativity and make it hard to reach out to customers effectively.

A well-designed and well-executed functional agenda makes all this easier. Once you can establish an open, well-communicated set of priorities and an explicit, well-understood functional blueprint, you will not be operating alone. By putting these together and talking about them openly, you reinforce a higher degree of alignment between the corporate center, the local business leaders, and your own team. As you gain practice in saying no to multiple priorities, and focusing on the few most critical capabilities, you enhance your own ability to lead. When the company moves in the direction of a capabilities-driven strategy, and needs your function to take part wholeheartedly, you and your team will be ready. +

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