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A SUBSIDIARY OF A MULTINATIONAL COMPANY.

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MANAGING THE PERFORMANCE LOCALLY THE BALANCED SCORECARD OF SEW EURODRIVE ITALIA, A SUBSIDIARY OF A MULTINATIONAL COMPANY

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Abstract

This paper focuses on the issues of design and implementation of a performance management system, based on the Balanced Scorecard (BSC) methodology, in the Italian subsidiary of a multinational company: Sew Eurodrive. It discusses why the BSC has been embraced by the subsidiary, how the global strategy of the company has been translated in local actions by the subsidiary through the BSC, how the BSC has been developed, what results have been achieved by its implementation and use and how the first release has been refreshed after the first year of use.

Introduction

Company overview
Sew Eurodrive, the multinational company (the company), is a global leading producer in drive engineering technology. It yields a revenue of about 1.2 billion Euro, with approximately 10,000 employees. Sew Eurodrive has 11 production plants and 58 assembly plants in 44 countries. Company headquarters are in Bruchsal, Germany.
Sew Eurodrive Italia, the Italian subsidiary (the subsidiary), is located near Milan. It generates a revenue of about 60 million Euro, with a workforce of 140 employees/workers and 14 managers. The subsidiary has an assembly plant and 6 branch offices spread across the country.

The strategy
The global strategy of the company was a clear strategy of expansion, developed along three directions:

- enhancing leadership in key product technology: the geared motor
- offering customized solutions tailored to meet specific requirements of existing customers
- attracting potential new customers with high performance integrated solutions: geared motors, electronic drive systems and service

The Italian subsidiary had to adapt this strategy to the local market needs and demands.
The goal the Italian subsidiary wanted to achieve was to make a big leap in revenue in the next five years, maintaining operating margin and profit at the desired levels. The subsidiary formulated a strategy to enhance its position in the local market, acting in two directions:

- promoting new integrated solutions developed by the company to broaden the market space
- gain market share from the competition, through a more aggressive price policy

The aim was to differentiate SEW from competition. A characteristic of Italian market is the strong presence of local vendors that play in the competitive context by offering products with a good price/performance ratio.

A first point of differentiation could be to offer better logistic support and better product quality: short and reliable delivery time, wider product range with lower number of rejected parts.
Thanks to the wide product range and the competence of sales staff, one more point of differentiation could be to provide customers with a complete solution including a high level of consultancy offered by the sales organization.
SEW serves the OEM market, but often end-users, the OEM's customers, can influence the choice of components. A significant part of SEW business is driven by end-users requirements. End-users can be very big and well known companies in different markets: beverage (Coca Cola, Heineken), automotive (Chrysler, BMW, Volkswagen, Kia), logistic (airports) SEW is very well accepted from end users because of the reliability of its products and the effectiveness of local service and support provided worldwide. Low operating and maintenance costs make SEW very appealing for all the end-users that look at medium and long term benefits of their choice.
On the contrary , OEM are more price sensitive, because they are focused on keeping their costs low. Therefore they prefer cheaper components, because they do not care too much of long term savings.
One of the challenges was to convince OEM to buy SEW products and solutions even when there was not any specific request from end-users.
Due to the importance of end-users as decision makers, the company decided also to set up some initiatives for them, getting in touch with them directly to show them the long term advantages of SEW solutions and offer maintenance contracts and special prices on spare parts.

Why the Balanced Scorecard?

The Italian subsidiary was started 35 years ago, and, for long time, the management was very stable. In year 2003 a total new generation of management was established due to the retirement of the old executive team.
The new Managing Director hired new production manager, sales manager, financial manager, marketing manager to replace the old staff.
After a short period, the new top management realized to have two main needs:

- enhancing the efficiency and the effectiveness of the organization introducing new tools, ERP, BSC, CRM, to improve operational and sales processes and manage the performance of the company
- building up a new mentality of teamwork for the new staff and a culture of collaboration throughout the whole organization.

There is no a history of performance management in the subsidiary because the previous management team relied only on a few financial measures and the subjective judgment of the former Managing Director, without any sort of performance system put in place.
The BSC has been adopted by the subsidiary in the attempt to address this lack and with the purpose of driving focus and alignment on both the new global strategy and the local change agenda throughout the organization from top to bottom. The alignment with the new strategy was considered a top priority for the subsidiary. In fact, despite clear messages in this direction, most of the local sales force continued to think in terms of products rather than solutions and most of the efforts to execute the new strategy failed to deliver what expected.
At the beginning, the idea was to put in place a few initiatives to change that behaviour and monitor the results, but the subsidiary needed something more than a set of financial measures to track expected performance improvements. Besides, in order to define these initiatives the subsidiary had to find out key performance drivers and highlight the cause and

effect relationships that link these drivers with financial outcomes. The BSC was considered the best methodology to make it happen.
As it did not exist a global BSC for the whole multinational company, the local BSC could not be developed through a cascading process from it. The challenge was to develop a BSC tailored for the local competitive context and, in the meantime, consistent with the global strategy of the company.

The subsidiary Scorecard

Team and agenda

The new Managing Director engaged a consultant to facilitate the design and the implementation of the Balanced Scorecard. The first step was to arrange a meeting between the Managing Director and the consultant to set up the financial results to be achieved in the next 5 years, clarify the strategic directions endorsed by the Headquarters in Germany and perform an initial assessment to establish the baseline of the project.
Then they decide to actively engage all the 14 managers in the Balanced Scorecard project from the beginning. People involved in the project team reacted in a extremely positive way to this approach because they felt to be like the "founders" of a new organization.
Design and implementation lasted about 3 months. The project started with a 2-days training course on the Balanced Scorecard in order to introduce the foundations of this methodology and educate participants in using it. After this session about theory, 4 practical sessions were organized to design the BSC of the company: the first to built the strategy map, the second to select indicators (KPI) and review the map, the third to agree about initiatives to be implemented to support objectives, the fourth to set up targets, review indicators and initiatives and consolidate the whole scorecard. In between these meetings, a lot of homework kept the participants focused on what they needed to do next to build the scorecard . This approach was used to be ready with the scorecard in a short time and test and refine it on the field.
During the design and implementation period, many tests and many changes occurred. All managers gave their personal contribution to successfully build an effective Balanced Scorecard for the company, working in collaboration with their colleagues. They shared experiences and ideas with colleagues, made proposals about objectives and KPI, explaining each other why and how a specific KPI should be selected and used, compared their opinions about actions to be taken and discussed about different scenarios in order to attain to a shared vision of what the company could be and identify a common set of objectives, indicators and initiatives. The most difficult task was to define targets. If for indicators like revenue and profitability it was relatively easy to set targets, for many others, the lack of historical data did not allow to set up relevant targets. They were used just to understand and monitor progress. In the meantime initiatives were identified to support processes and develop intangible assets. Targets and initiatives are two key components of the "agreement on performance". It is crucial that they are considered together.
The complete scorecard and the concepts behind it were presented to the whole sales force organization during a global meeting at the beginning of the year. Furthermore, the top management illustrated to each department and to each branch office the strategy to emphasize the importance of managing the performance with this tool.
According to the management requests, the IT team of the subsidiary worked to develop a software application dedicated to collecting data and reporting measures. The system was based on Intranet technology to provide all managers with the possibility of monitoring performance progress and strategy execution and sharing information with their staff.
In-house development was considered the fastest, easiest and more effective solution to be ready to support performance management in daily execution with a software application.

The first scorecard

The Balanced Scorecard architecture adopted by the subsidiary was the traditional one (Kaplan and Norton, 1992) arranged in four perspectives: financial, customer, internal processes, learning and growth. At the beginning the project team contemplated adding a further perspective to take into account the relationship with corporate headquarters in Germany. Analyzing more deeply the impact of this relationship on business, the team considered it not so strong, complex and articulated, to justify one more perspective. So this hypothesis was put aside and a specific objective in the internal processes perspective was defined to stress, anyhow, the strategic importance of that relationship.

Financial outcomes were not particularly different from those of any other profit-driven company. The main focus was on accelerating revenue growth while maintaining profitability, a goal to be achieved by improving the "quality" of revenue, a strategic objective, and keeping the subsidiary costs under control, a strategic constraint.

Three financial outcomes were identified in the financial perspective.

- Achieve a revenue of ( ) in ( ) years, while maintaining a profitability of ( )
- Increase value of customers portfolio while maintaining the profitability
- Reduce customers handling costs

It is interesting to point out that the expected profit was considered more a constraint to be satisfied in pursuing the desired revenue growth than a specific goal to be achieved. In other words the subsidiary did not pursue the growth of the local profitability.

A measure of profitability has been added as a compensating metric to balance the revenue one because if only revenue is used as a financial measure, then profit could be compromised by sales force taking shorts cuts. Revenue and profit measures needed to be combined to encourage the appropriate sales force behaviours and avoid getting undesirable results (Neely et al, 2003).

In the customer perspective objectives were selected to balance customers satisfaction with their contribution to short and long term company success (Neely et al., 2003).

Four objectives were selected in this perspective:

- increase the value of the company's offer as perceived by customer
- increase the product mix per customer
- attract new customers
- enhance brand recognition

It should be noted that objectives identified in the customer perspective were not intended to highlight specific aspects of the value proposition but rather focus on how the value proposition is perceived, "valued" by customers and how they contribute to the subsidiary success.

This is a more "deterministic" approach to the customer perspective than those described in other Balanced Scorecard case studies. (Kaplan and Norton, 2004, Niven, 2005, Olve et al., 1999, Olve et al., 2003)

This light-approach has been thought to make the strategy map development easier for managers approaching this methodology for the first time. Besides it simplifies the development of subsequent updates of the scorecard because objectives in both financial and customers perspectives are left as they are, while the ways they are pursued change and evolve over time.

As Michael Porter pointed out (Porter, 1996), companies build their winning value proposition through processes they perform: "*Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value*".

In the internal processes perspective, the subsidiary selected objectives to differentiate its activities from those of its competitors and create the conditions for a long term growth. A strength and weakness analysis was conducted to identify issues and establish processes the subsidiary had to improved to better execute its strategy.

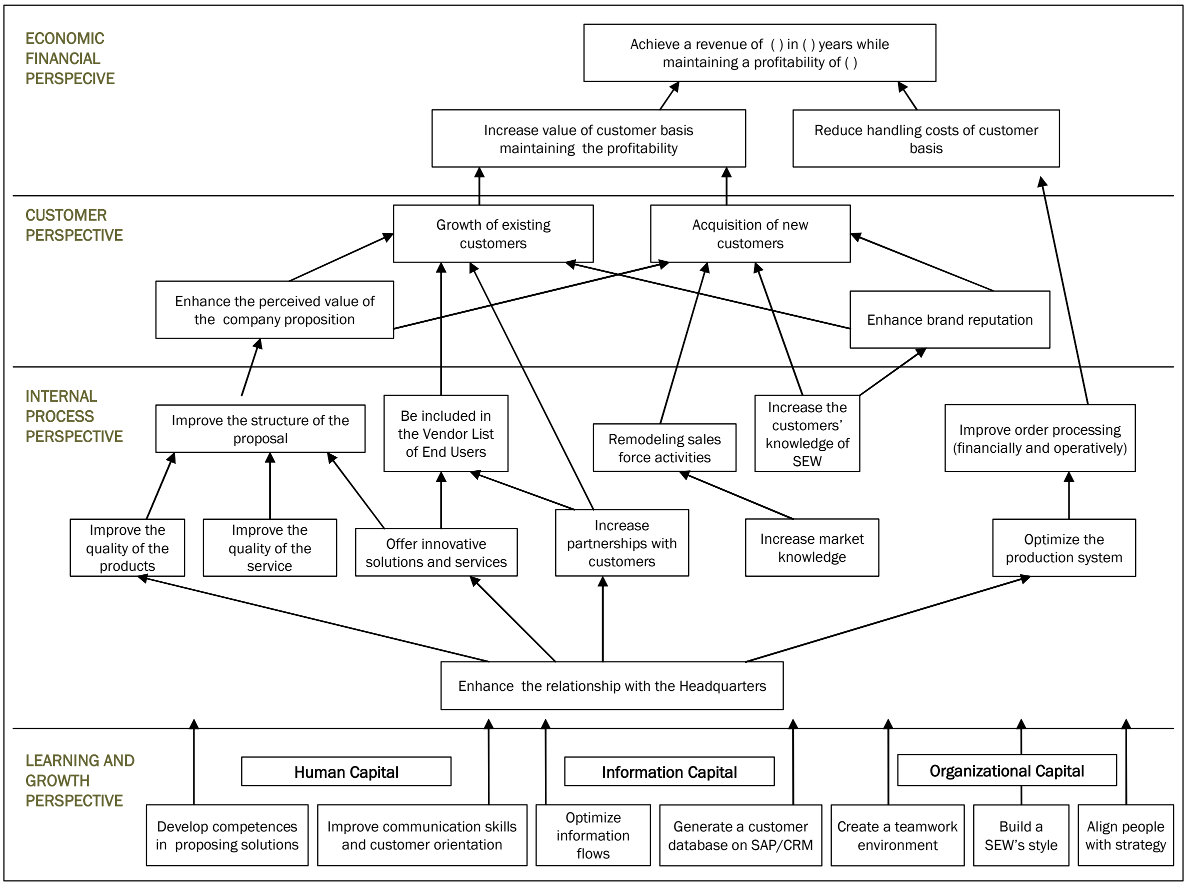

Figure 1 – 2005 strategy map

The subsidiary already controlled its costs quite well. So focus in building the strategy map was on executing a strategy of growth, not on keeping costs further under control. Well designed, organized and executed sales processes, on one hand, and partnering with customers to design tailored solutions, on the other hand, were considered the key elements to deliver the customer value necessary for sustained business success. The subsidiary wanted to maintain its product leadership in the Italian market and, in the meantime, improving customer intimacy.

Twelve objectives were identified in the internal processes perspective. One of them was to "enhance the relationship with the Headquarters in Germany". Too often, multinational companies consider their subsidiaries more as distributors than parts of the same organization. The Italian subsidiary wanted to move from such a sort of vendor-distributor relationship to a true and robust partnership between different parts of the same organization. To track the achievement of this objective, the team chose two indicators:

- number of customize solution jointly developed by the subsidiary and the company
- delivery time of products released in Germany for Italian customers

In the learning and growth perspective efforts were oriented to achieve the following objectives:

- educating employees on a customer-centric approach to business (human capital)
- improving sales force knowledge and skills on selling integrated solutions (human capital)

- facilitating the internal flow of information (information capital)
- introducing a CRM (information capital)
- creating an organizational climate oriented to improve collaboration among sales force, product specialists and solution designers (organization capital)
- creating a company's style (organization capital)
- aligning people with strategy (organization capital)

The strategy map of the first balanced scorecard built at the end of the year 2004 for year 2005 is shown in Figure 1.

The update

The first year of use has been a period of adjustment in which to build familiarity with the system, teach people how to use measures to manage their performance and achieve the desired results, create consensus on this new way to "be in control" (Robson 2004) among the workforce, assess the effective relevance of objectives and measures included in the first scorecard, overcome barriers that a few salesmen raised to defend the level of comfort achieved in the past.

Interviewing managers e professionals about this first experience it looked like the performance management system was accepted and shared very quickly, apart from some rare and "physiological" exception.

Managers in the project team showed a sincere commitment to the scorecard and worked hard together to make the project succeed. The climate of collaboration, the shared knowledge and dialogue generated has been truly appreciated by executive that were afraid that some sort of internal competition would rise among managers.

The design, the implementation and the use of the scorecard increased the cohesion among managers and the will to share experiences, projects and information.

The scorecard was "internalized" by the subsidiary and, using it, people could evaluate, in the field, benefits (and disadvantages) of its adoption. The project team were aware that objectives and indicators in the first release were to many. They preferred testing all of them on the field to verify their relevance. The use highlighted the need to make a few changes to improve the effectiveness of the scorecard.

A 2-days meeting with the consultant was arranged to review and update the scorecard. In order to have a direct feedback from the front line, three new members were added to the review team: the two best salesmen of the subsidiary and a tech support person from one of the branch offices. The other members were the managers that drew the first release.

The new strategy map is shown in Figure 2. Some of the objectives has been left as they were, others either modified or removed. A few new objectives have been added in the new release. Thanks to the light-approach adopted, financial and customer perspectives has been left as they were in the first release. The team reviewed just the indicators selected to track the accomplishment of objectives included in these perspectives. In the second release they were reduced from 22 to 15. Still too many. They will be reduced further in the next release.

The map has been remodelled in the internal processes perspective. In addition to the objective "Enhance the relationship with Headquarters", four strategic themes were taken into account to focus on different groups of key processes.

The four strategic themes were:

- Enhance proposal development
- Empower sales force to get results
- Increase market visibility
- Improve financial and operational processes

These themes are linked to objectives in the customer perspective.

The team reviewed all the objectives included in the internal processes perspective of the previous map and make an analysis about their current relevance and their consistency with the strategic themes.
The review of the learning and growth perspective allowed to remove one objective from the information capital component and one from the organizational capital one. In particular the objective "align people with strategy" was removed because it was impossible to measure it in the subsidiary. What had been measured using the first release was not "how many people are aligned with the strategy", but "how many people the strategy was communicated to". This was not correct because instead of measuring an "effect" what was measures was on of its "causes"
In the second release of the scorecard, the total number of objectives decreased from 25 to 20 and the total number of indicators decreased from 62 to 50.

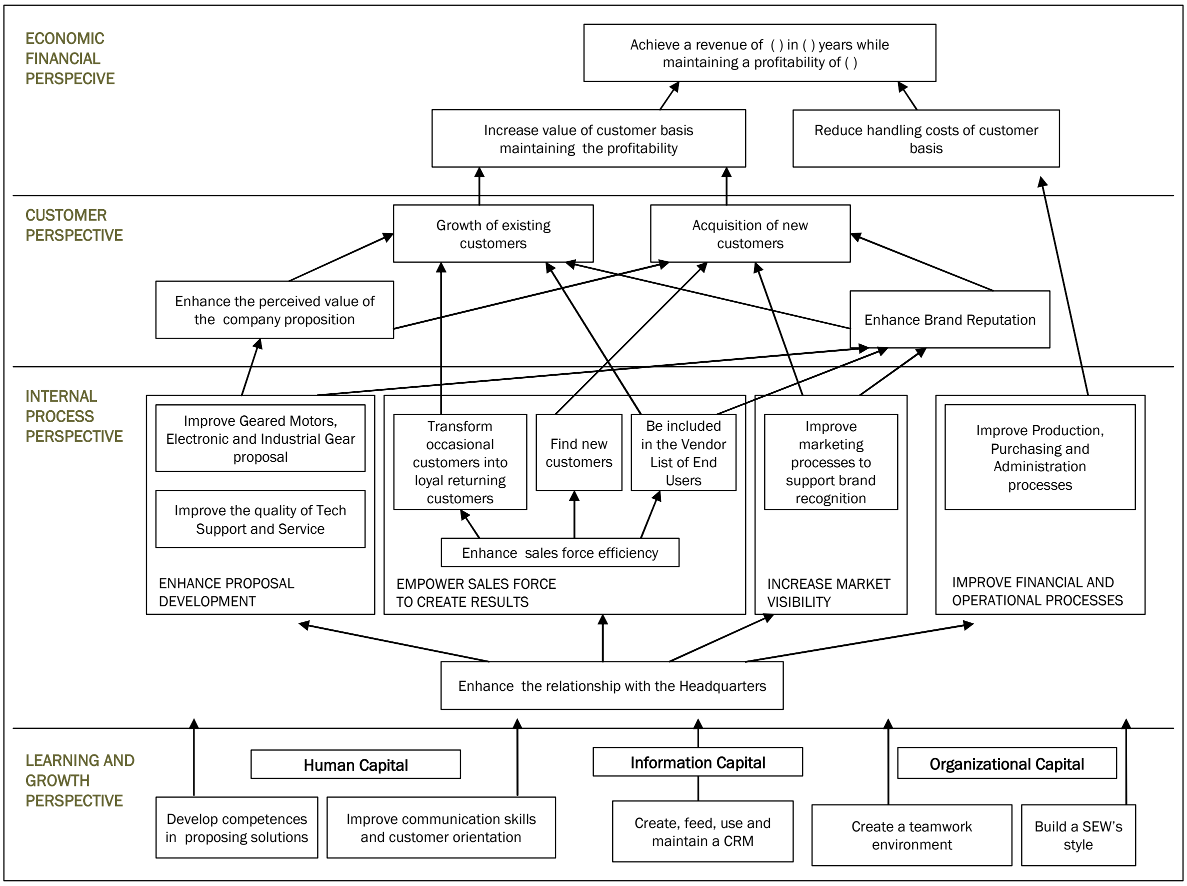

Figure 2 – 2006 strategy map

Results, findings and conclusions

Both objectives and indicators in the first release of the BSC were too many. They have been reduced in the second release focusing more on strategic priorities rather than operational issues, but they are still too many. People from the front line desire operational measures that drive they daily work. Executives desire to focus on few measures that matter. Using a unique scorecard for the whole subsidiary makes difficult to find an optimized solution to this issue. Having a couple of scorecards linked together could be a good compromise.
What is the executive view on the results of this experience?
The scorecard allowed to learn and teach.

The main result achieved was to have built up a team. Project and review sessions allowed people to work in a cross-functional environment, reflecting together on business strategy and chains of cause and effect relationships, finding shared solutions to shared strategic issues. All managers worked together understanding everybody's else needs and problems and having the common interest driving their thoughts. They now feel a sense of belonging, the consciousness to be integrated parts of the same organization.
The second result achieved was to have all internal processes under control. People are aware about their performance progress and how their individual performance affects the subsidiary performance. On the other hand, executive have the right feedbacks about what is driving the future performance of the subsidiary. This can avoid internal discussion about perception of inefficiency which are not really true and allow to focus on what really matter.
The third, most complex and long term one, was to change the mind set of the sales force. The challenge was to change their attitude to visit customers "on demand" in a new market-driven approach identifying the biggest potential and developing strategies and action in order to grow existing customers and enter in new market segments.
As it was developed, the Balanced Scorecard of the Italian subsidiary could easily be transferred to other subsidiaries of the multinational company maintaining a core of common objectives and indicators and developing just those ones that are driven by the local needs of each country .

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