

Does Your Organization Have the Capabilities to Execute Strategy?

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No organization can successfully execute strategy without the right people, processes, and technology (and information) capabilities. Yet, surprisingly, many organizations lack a clear idea of what capabilities are required and where the deficiencies are. The approach described in this article, which builds on Kaplan and Norton's concept of human capital and IT readiness reporting, provides a road map for organizations to follow to identify and assess capability gaps and puts in place a management process to close these gaps.

As recent Conference Board studies¹ have shown, the leading issue on the minds of CEOs and other senior executives is the inability of organizations to effectively execute strategy. A reasonable explanation for this deficit is that many organizations lack a coherent framework and methodology to ensure that strategy can be executed.

In our work with hundreds of organizations that have sought help implementing strategy—many of which have turned to the Balanced Scorecard because it is the only management approach that is linked to increases in shareholder value²—we've seen numerous barriers that stand in the way of successful execution. But after the issues of leadership support and alignment have been addressed, the next most persistent issue facing organizations is the lack of a clear understanding of which capabilities are required for their strategies to succeed. Organizations must be systematic about assessing the people, process, and technology resources that their strategies require. They must establish ways of measuring and closing capability gaps, and recognize that to close these gaps, planning for human capital (people), IT (technology and information), and operations

(processes) must be aligned to deliver the resources required by the strategy. This proper alignment of resources and strategy—so necessary for success—can be difficult for organizations that typically develop function-specific plans in a bottom-up fashion or in isolation from each other.

If your organization doesn't know or has struggled to identify the unique capabilities it needs to execute its strategy, it is not alone. Many companies lack this basic understanding. It doesn't help when many strategies are articulated as nothing more than a set of bold bullet-point statements such as “innovate to win” or “leverage best-in-class talent.” And when strategy is stated as a list of projects, loosely linked to a broad and vaguely defined long-term vision or mission statement, the outcomes achieved will often produce suboptimal results. But based on earlier work by Kaplan and Norton that identified the role of intangible assets as critical enablers

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of strategy, we can offer a practical approach for effectively aligning resources with strategy and achieving the execution premium.

In this article, we propose a new four-step approach that builds on Kaplan and Norton's concept of “strategic readiness” planning and measurement, as outlined in their 2004 article “Measuring the Strategic Readiness of Intangible Assets.”³

Step 1. Define Strategic Capabilities

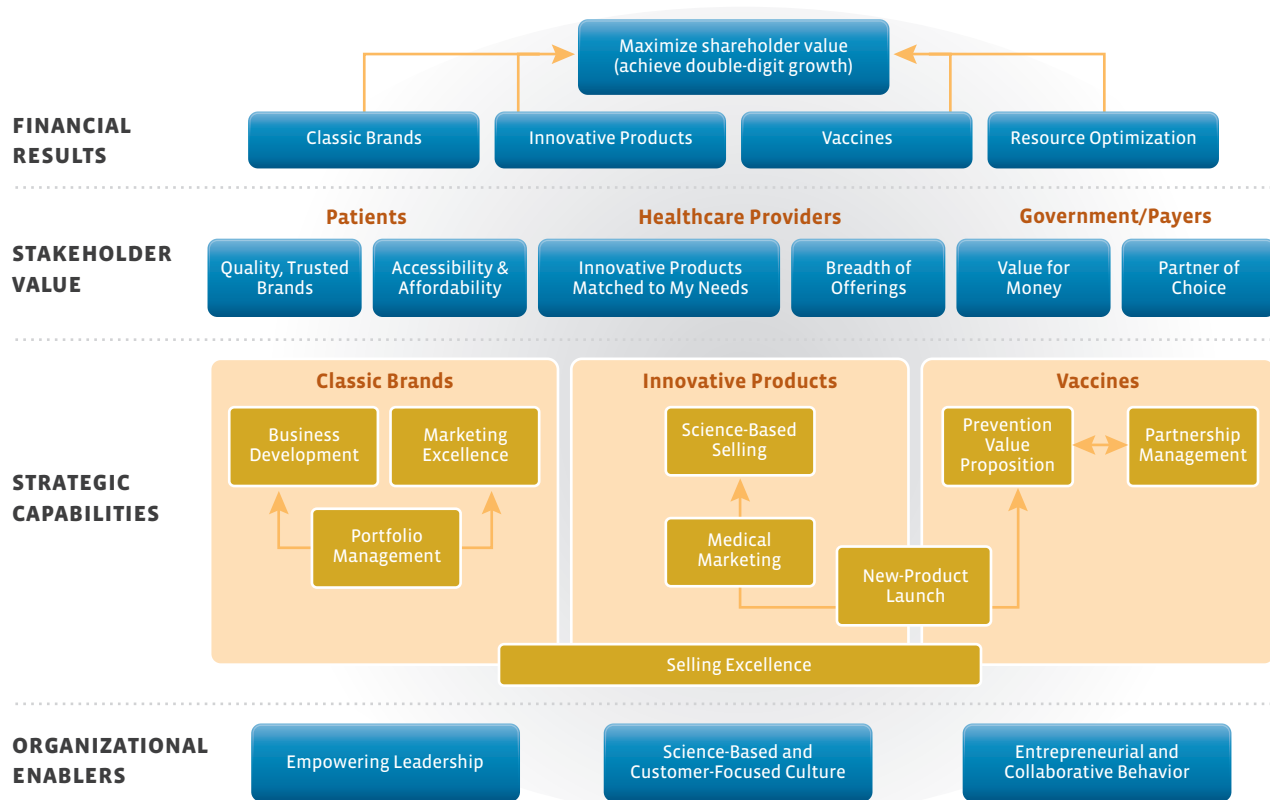
Strategic capabilities are the unique bundles of processes, people, and technology that enable an organization to create a competitive advantage. Often, a company's strategic capabilities are more valuable than its financial or physical assets because they are much harder for competitors to imitate. They represent a potentially powerful source of sustainable competitive advantage. For example, consider the retailer Zappos.com. For Zappos, superior customer service is a strategic differentiator that is delivered to the customer through a combination of an effective process for handling customer issues, enabled by a technology system, and delivered by employees who are talented at responding to customer requirements. Although it's not impossible for another online retailer to reproduce this combination of resources, doing so represents a formidable hurdle that limits imitation.

So how do you identify what your organization's strategic capabilities should be? In our view, the capabilities required are a function of the strategy an organization is trying to pursue;

1 Conference Board, *CEO Challenge, 2007—Top Ten Challenges*.

2 “The Effects of Adopting the Balanced Scorecard on Shareholder Returns,” *Advances in Accounting, Volume 24, Issue 1, June 2008*.

3 R. Kaplan and D. Norton, “Measuring the Strategic Readiness of Intangible Assets,” *HBR, February 2004*.



■ **FIGURE 1: STRATEGY MAP (WITH STRATEGIC CAPABILITIES CLEARLY IDENTIFIED)**

In this strategy map for a life sciences firm, the necessary strategic capabilities are identified for each of the three strategic themes: Classic Brands, Innovative Products, and Vaccines. Each strategic capability should be further defined to indicate: reason for importance; the unique combination of people, processes, and technology required to satisfy the strategy; and how these capabilities will be delivered.

thus, the first step is to clarify strategy. For this step we recommend developing a one-page strategic capability map that corresponds to the four perspectives of the Balanced Scorecard. However, after defining the financial and customer perspectives, we suggest relabeling the internal process perspective “strategic capabilities” and the learning and growth perspective “organizational enablers.” This will encourage the thoughtful integration of people, processes, and technology in a way that can be more effective for identifying the resources required to deliver the customer objectives.

A strategic capability map builds on the idea of a conventional strategy map. The process of constructing such a map is similar. It is important to identify and interview a wide range of executives with expertise across all business units and functional areas, as well as any key internal or external stakeholders who

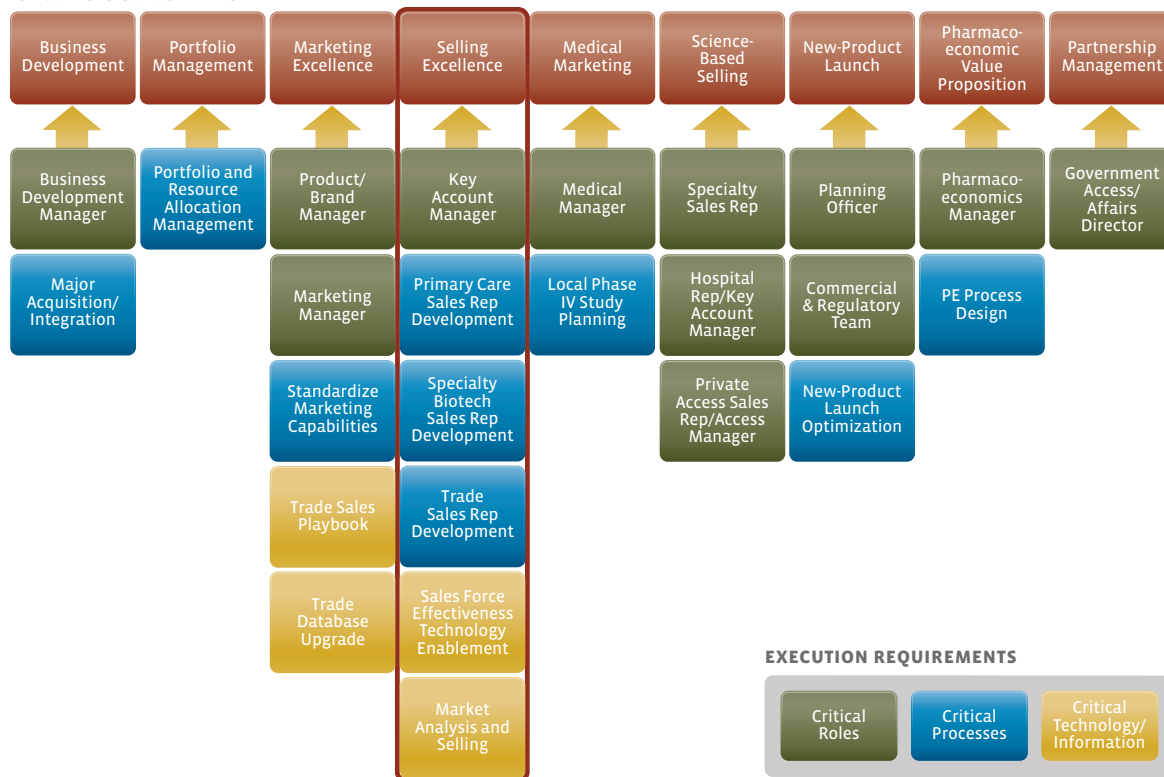
can offer a valuable perspective on the organization’s people, processes, and technology capabilities. These interviews typically involve asking pointed questions that explore the importance of and the links between the people, processes, and technology required to deliver value to customers and financial results:

1. What are the key processes at which you must excel to deliver the customer value proposition?
2. For these processes, what critical roles are required for their successful execution?
3. For these processes and roles, what information and/or technology is critical to success?
4. What does the organization need to focus on from a culture and leadership perspective to further enable the strategy?

Once the interviews are complete, you can condense your findings into the structure of the strategic capability map. The logic of the strategic capability map is similar to that of a traditional strategy map. A real-life example based on our work with the emerging markets group of a large pharmaceutical company (disguised as “Pharmaco”) is shown in *Figure 1*. Under pressure to deliver double-digit growth, this group turned to the Kaplan-Norton methodology as a means of identifying investment requirements and increasing its chances of successfully executing its strategy.

Once all the strategic capabilities have been identified, it is important to define each one in a way that articulates (a) why each capability is important; (b) what specific combination of people, processes, and technology is needed to provide this capability; and (c) how the organization is going to deliver each capability. For example, for the Selling

STRATEGIC CAPABILITIES



■ **FIGURE 2: STRATEGIC CAPABILITY REQUIREMENTS MAP (WITH CRITICAL ROLES, PROCESSES, AND TECHNOLOGY/INFORMATION IDENTIFIED)**

Building on the high-level representation provided in Figure 1, this drawing provides additional detail for each of the components of the capabilities required in terms of roles, processes, and enabling technology.

Excellence capability, Pharmaco’s emerging markets team developed the following definition:

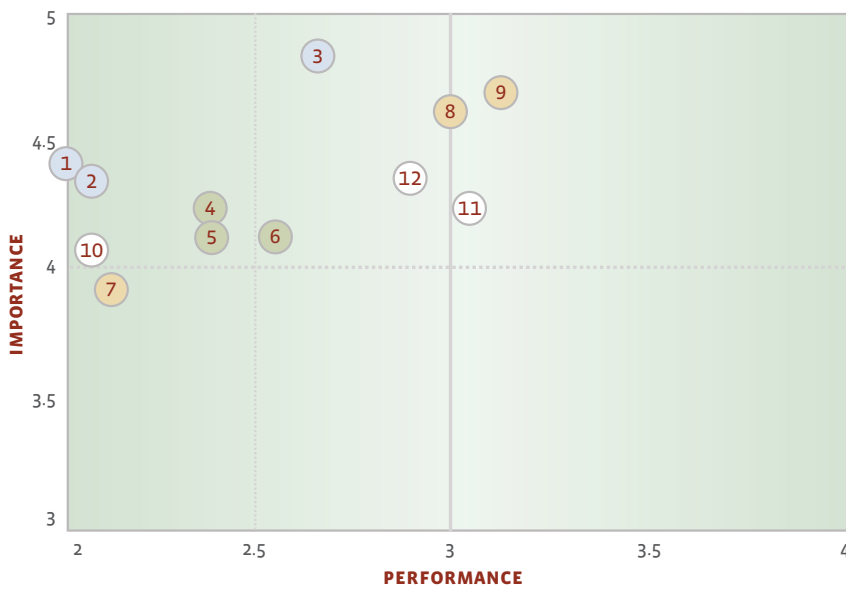
Our success depends on our ability to match the products in our portfolio to the specific needs of healthcare providers and patients and build trusting relationships with all customers. Therefore, we need to develop the capability (including the supporting IT) to segment and target customers that represent the most profitable opportunity for Pharmaco in each customer segment and leverage customer/consumer data and insights to understand what the customer needs, wants, and values. We must also ensure, through effective on-boarding and talent development, that our customer-facing teams use this information to make the right decisions for our customers and Pharmaco.

Upon completing these strategic capability definitions, a clearer understanding of the details of each strategic capability should start to emerge. At this point in the process, the organization is ready to pinpoint specific critical roles, processes, and technology/information requirements that are essential to successful execution. We recommend depicting these on what we call a “strategic capability requirements map” as shown in Figure 2. This example, developed by a country within Pharmaco’s emerging markets group, illustrates the major requirements for each strategic capability. For the Selling Excellence capability, country-level leaders identified critical roles required from people such as key account managers, critical processes such as sales rep development, and technology requirements such as the addition of a mobile CRM system or a software application that supports on-the-go data entry.

Step 2. Analyze Strategic Capability Gaps

Now that the organization’s strategic capabilities have been defined, it is important to understand the “gaps” that must be filled in order to successfully execute the strategy. In this step, we find it useful to deploy an online survey that asks management a few critical questions regarding each capability:

1. What is the importance of this strategic capability to achieving the organization’s high-level financial goals? (1-to-5 scale)
2. What is the organization’s current performance of this capability? (1-to-5 scale)
3. What actions or initiatives should be taken to improve performance and deliver on the people, processes, or technology/information requirements for this capability?



Strategic Capabilities:

1. Pharmaco-economic Value Proposition
2. Marketing Excellence
2. New-Product Launch
4. Business Development
5. Portfolio Management
6. Science-Based Selling
7. Selling Excellence
8. Medical Marketing
9. Partnership Management

Enablers:

10. Entrepreneurial and Collaborative Behavior
11. Empowered Leadership
12. Science-Based and Customer-Focused Culture

- # Tier 1
- # Tier 2
- # Tier 3

FIGURE 3: STRATEGIC CAPABILITIES PRIORITIZATION MATRIX

The four-box matrix, shown in this figure, can be used to evaluate strategic capabilities along two axes: current level of performance and level of importance to the strategy. Both axes are rated on five-point scales. Strategic capabilities that are in the upper left-hand quadrant are considered high priorities in need of additional investment.

These survey questions yield three important observations. First, the difference between the ratings of importance versus performance provides an understanding of which strategic capabilities have the largest gaps and therefore are most deserving of investment. Second, you will be able to understand where the greatest disparity in opinion lies within your leadership regarding which capabilities are currently sub-optimized. Third, you will derive a set of ideas for actions and initiatives that can potentially close the gaps in each strategic capability.

Recommended actions to close gaps come in many forms. For people gaps, actions may be expressed in terms of hiring new employees to staff existing positions, developing training for existing employees, clarifying roles and responsibilities, or adding new positions to the organization. For process gaps, actions or initiatives may be expressed in terms of new processes that must be implemented, process improvement efforts, or elimination of processes that do not serve the company's strategic capabilities (or do not serve them well). For technology or information gaps, actions may be providing additional in-

formation required to support a specific people or process capability or systems to tie disparate data and information together.

Step 3. Prioritize and Identify Actions to Close Gaps

Now that your strategic capabilities have been appropriately prioritized and actions to close strategic capability gaps have been identified, convene a meeting with the leadership team to discuss this analysis and understand which strategic capability gaps need to be closed and which specific actions and initiatives are critical to closing identified gaps.

One way to analyze and display the relative ranking of strategic capabilities is to use a four-box prioritization matrix depicting the importance and current performance of each (as described in Figure 3 using the Pharmaco example).

Presented in this format, one can clearly see that those capabilities that fall closest to the upper left-hand corner of the box have the greatest level of importance but the lowest level of current performance, and therefore deserve to be prioritized for investment.

Once the strategic capabilities are prioritized, the leadership team should closely examine each strategic capability to understand the deficient people, processes, and technology/information components and consider ideas for improvement, including those that were proposed during executive interviews and surveys. This exercise involves defining the desired future state, assessing gaps in comparison to the current state, and identifying specific actions or initiatives required to close gaps. For example, for the Selling Excellence capability, where enabling technology is identified as a critical requirement for performance, Pharmaco identified the following:

Enabling Technology for Sales Force Effectiveness

Desired Future State:

- Captures customer and market intelligence and provides an integrated view of the customer
- Supports customer segmentation and targeting
- Supports key account management (such as trade, hospitals, etc.)
- Enables sales tracking
- Provides competitive intelligence

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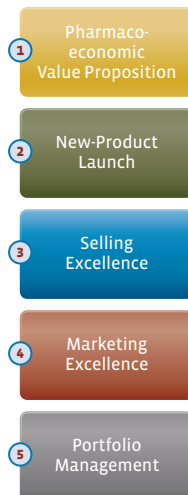
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CAPABILITIES



ACTIONS AND INITIATIVES



FIGURE 4: PHARMACO COUNTRY-LEVEL STRATEGIC CAPABILITY GAP-CLOSING INITIATIVES

To deliver the necessary strategic capabilities to the organization, it is likely that some new actions or initiatives will be required. This figure includes an example for the life sciences firm we have been following in this article. The color coding shows the specific capability sets that each initiative is related to.

Current-State Assessment of Gap:

- Lack of mobility and ease of use
- Poor reporting capability

Decision/Actions to Close Gap(s):

- Implement Mobility Project (Enabling technology for sales force effectiveness)
- Timeline: One year
- Develop the business case to support funding
- Executive sponsor: John Smith

Once the actions and initiatives to close strategic capability gaps are identified, it is important to facilitate a prioritization exercise with the leadership team so it can drive focus and allocate scarce resources to the initiatives that are expected to have the largest impact on performance in the shortest period of time. For Pharmaco, this analysis yielded the output shown in *Figure 4*.

It is also important to link these actions and initiatives to the organization's existing (or new) initiative management framework. Effective initiative management ensures that each initiative has a defined initiative charter that clearly specifies the sponsor, project manager,

a description of the initiative, the gap it addresses and the benefits expected, and key milestones from start to conclusion.

Step 4. Establish Governance and Renewal

Just as with the creation of a traditional Balanced Scorecard, it is important to manage the allocation of strategic resources to ensure that actions are being taken to close gaps and that the capabilities selected always reflect the unique mix of people, processes, and technology that provide competitive differentiation.

To monitor whether the actions being taken are effectively closing capability gaps, it is important to define the measures you will use to evaluate the performance of the capability. Taking the Zappos.com example, if the strategic capability you are monitoring is excellent customer service, you may elect to measure the following:

1. A people component such as the number and percentage of customer service reps fully performing with the required skills and competencies required

Once the capabilities are prioritized, the leadership team may choose to conduct a deeper examination of each strategic capability to discuss the people, processes, and technology/information components and the ideas for improvement that have been proposed during executive interviews and surveys.

2. A process component such as the time from sales order to delivery
3. A technology component such as the number of reported failures to process customer transactions

Organizations can also establish “readiness measures”—similar to what Kaplan and Norton propose for human capital and IT readiness—as a means of gauging progress over time. The key is to implement measures as part of the ongoing governance process, which is paramount to ensuring a consistent linkage between an organization’s evolving strategy and the capabilities required to support differentiation. For instance, if Zappos.com made a shift in strategic direction and began to focus more on price competitiveness, its strategic capabilities would naturally need to be revised to reflect new capabilities such as “gaining efficiencies in supply chain” and “operational excellence.” New measures of success would also be required. If the governance process is designed to be reviewed with sufficient frequency (we recommend reviewing progress and performance on either a quarterly or monthly basis to ensure that the process remains evergreen), it should be possible to react quickly enough to shifts in strategy.

Conclusion

Whether your organization develops its strategy based on an analysis of its strategic capabilities (What do we have to work with?) or chooses to identify required capabilities after developing its strategy (What do we need to have to get where we want to go?), the approach outlined here can clarify the linkages between a unique and differentiated strategy and the capabilities necessary to support its execution.

For those organizations that already use the Balanced Scorecard as a management tool, each of the internal process objectives on your existing strategy map can provide a starting point for defining the unique capabilities required to execute your strategy. We recommend that functional leaders from HR, IT, and operations play an active role in the process to ensure that there is a strong connection back to the work each function is doing to support the strategy. In our experience, these leaders will enthusiastically embrace the approach since it helps focus their work on what is truly critical for the organization to outperform the competition. ■



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