Beyond Budgeting - Management innovation for new people and business realities

Ambition to Action - the Statoil journey

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Vice President - Performance Management Development
Chairman - Beyond Budgeting Roundtable
Outline

• The case for change
• The Beyond Budgeting principles
• The Statoil model - Ambition to Action
Statoil in brief

- Turnover approx. 90 bn. USD
- 23000 employees in 33 countries
- World’s largest operator in waters deeper than 100 metres
- Second largest gas exporter to Europe
- World leader of crude oil sales
- Listed in New York and Oslo

*Current production of oil and gas*
Simple, clear purpose and principles give rise to complex, intelligent behavior.

Complex rules and regulations give rise to simple, stupid behavior.

(Dee Hock - founder and former CEO of Visa)
What is Management Innovation?

“Exploring new ways of leading and managing in knowledge organisations operating in dynamic and competitive business environments”

(Not management of innovation....)
The innovation paradox

Technology innovation
- a very crowded place

Leading edge!
Uniqueness!
Forefront!

Management innovation
- not yet a crowded place

Great!
Scary!

Same purpose: Better performance!
Some of the budget problems

- Very time consuming
- Assumptions quickly outdated
- Stimulates unethical behaviours
- Often weak link to strategy
- Decisions made too early and often too high up
- Can prevent value adding activities
- “Accordion” forecasting horizon
- Often a bad yardstick for evaluating performance

Irritating itches - or symptoms of a bigger problem?
Managing traffic performance - one alternative

Who is in control?

Based on which information?
Managing traffic performance - another alternative

Who is in control?

Based on which information?
Which is most **efficient**?

Which is most **difficult**?

In which are **values** most important?
The world has changed - what about the way we lead and manage?

Business environment

Dynamic

Stable

Traditional management

"Theory X"

"Theory Y"

People
We must change both processes and leadership.

Processes

- Dynamic:
  - No traditional detailed budgets
  - Relative and directional goals
  - Dynamic planning, forecasting and resource allocation
  - Holistic performance evaluation

- Stable:
  - Rigid, detailed and annual
  - Rules-based micromanagement
  - Centralised command and control
  - Secrecy, sticks and carrots

Leadership

- Beyond Budgeting:
  - Values based
  - Autonomy
  - Transparency
  - Internal motivation

- "Theory X"
  - More agile
  - More human

- "Theory Y"
Companies on a similar journey
# The 12 Beyond Budgeting principles

<table>
<thead>
<tr>
<th>Change in leadership</th>
<th>Change in processes</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Governance &amp; transparency</strong></td>
<td><strong>Goals &amp; rewards</strong></td>
</tr>
<tr>
<td>1. Values – Bind people to a common cause; <strong>not to a central plan</strong></td>
<td>7. Goals – Set ambitious medium-term goals; <strong>not short-term fixed targets</strong></td>
</tr>
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<td>2. Governance – Govern through shared values and sound judgement; <strong>not detailed rules and regulations</strong></td>
<td>8. Rewards – Base rewards on relative performance; <strong>not on meeting fixed targets</strong></td>
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<td>3. Transparency - Make information open and transparent; <strong>don’t restrict and control it</strong></td>
<td><strong>Planning &amp; Controls</strong></td>
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<tr>
<td><strong>Accountable teams</strong></td>
<td></td>
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<tr>
<td>4. Teams - Organize around a seamless network of accountable teams; <strong>not around centralized functions</strong></td>
<td>9. Planning - Make planning a continuous and inclusive process; <strong>not a top-down annual event</strong></td>
</tr>
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<td>5. Trust – Trust teams to regulate and improve their performance; <strong>don’t micro-manage them</strong></td>
<td>10. Coordination - Coordinate interactions dynamically; <strong>not through annual budgets and planning cycles</strong></td>
</tr>
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<td>6. Accountability – Base accountability on holistic criteria and peer reviews; <strong>not on hierarchical relationships</strong></td>
<td>11. Resources - Make resources available as needed; <strong>not through annual budget allocations</strong></td>
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<td></td>
<td>12. Controls - Base controls on fast, frequent feedback; <strong>not on budget variances</strong></td>
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Start of the Statoil journey - solving a serious budget conflict

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<th>The budget purposes</th>
<th>Step 1</th>
<th>Step 2</th>
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<td><strong>Budget =</strong></td>
<td>Separate</td>
<td>Improve</td>
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<tr>
<td>• Target</td>
<td>Target</td>
<td>• Inspiring &amp; stretching</td>
</tr>
<tr>
<td>• Forecast</td>
<td>Forecast</td>
<td>• VUCA robust</td>
</tr>
<tr>
<td>• Resource allocation</td>
<td>Resource allocation</td>
<td>• Unbiased - expected outcome</td>
</tr>
<tr>
<td>Same number for conflicting purposes</td>
<td>Different numbers</td>
<td>• Limited detail</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• No detailed annual pre-allocation</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• KPI targets, decision authorities, gates and criteria</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Trend monitoring</td>
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**Start of the Statoil journey - solving a serious budget conflict**

**The budget purposes**

- **Budget =**
  - Target
  - Forecast
  - Resource allocation

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<td><strong>Same number for conflicting purposes</strong></td>
<td>Different numbers</td>
<td>Event driven, not calendar driven</td>
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Financial performance - as we define it

Shareholder Return

Return on Capital

- Total
- Repsol
- Royal Dutch Shell
- Statoil
- ConocoPhillips
- BP
- Eni
- ExxonMobil
- BG
- Chevron
- Anadarko
- Petrobras

Target: Above Peer Average

- Total
- Statoil
- ConocoPhillips
- Royal Dutch Shell
- BP
- BG
- Repsol
- ExxonMobil
- Anadarko
- Eni
- Chevron
- Petrobras

Target Top 1/3
Ambition to Action - purpose and process

- Translating strategy - from ambitions to actions
- Securing flexibility - room to act and perform
- Activating values and leadership principles

Strategic objectives

KPIs

Actions & forecasts

Individual or team goals

Where are we going – what does success look like?
- Most important strategic change areas
- Medium term horizon

How do we measure progress?
- Indicative measure of strategic delivery
- 5-10 KPIs, shorter/longer term targets

How do we get there?
- Concrete actions and expected outcome (forecast)
- Clear deadlines and accountabilities

What is my or our contribution?
- My Performance Goals
  - Delivery
  - Behaviour
Ambition to Action example

<table>
<thead>
<tr>
<th>People &amp; Organisation</th>
<th>Where are we going?</th>
<th>How do we get there?</th>
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<td>People &amp; Organisation</td>
<td>&quot;Strategic objectives&quot;</td>
<td>&quot;Actions&quot;</td>
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<th>HSE</th>
<th>How do we measure progress?</th>
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<td>HSE</td>
<td>&quot;Key Performance Indicators&quot;</td>
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**Strategic objectives**

<table>
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<th>People &amp; organisation</th>
<th>Key performance indicators</th>
<th>Actions (top 5 in period)</th>
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<tbody>
<tr>
<td>A values-based and performance driven organisation</td>
<td>Living the values</td>
<td>Accelerate performance, people development and mobility (31.12.11)</td>
</tr>
<tr>
<td>Secure compliance and learning</td>
<td>PPS process</td>
<td>Secure strong ownership to compliance and ethics on all levels (30.12.11)</td>
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</table>

**Health, safety, environment**

<table>
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<th>Industry</th>
<th>Key performance indicators</th>
<th>Actions (top 5 in period)</th>
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<tr>
<td>Serious incident frequency</td>
<td>Implement learning (31.12.11)</td>
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<td>Climate</td>
<td>Improve the quality of PSE risk management at all levels (61.12.11)</td>
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</tr>
<tr>
<td>TTS Observations and actions</td>
<td>Ensure technical integrity for transport and wells (15.12.11)</td>
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**Operation**

| Operational and functional efficiency | PE NCS (Repsol) | Deliver ramp-up of Lelis demo, Peregrino, Marcellus and Eagle Ford according to milestones (del) (31.12.11) |
| Business asset, EOR and new development | Production of Statoil share | Ensure sufficient in-house capacity for Beltskamp |
| Competitive cost and quality project design and execution | Cost efficiency (PA) | Final investment decision |

**Market**

| A trusted company | Reserve replacement ratio (RRR) | Deliver technology programme to enhance value in the oil sands and Palagonite (01.03.12) |
| Ensure quality and efficiency from our suppliers | Downstream NOI (NOG) | Sustain NCS production though improved regularity, optimised rig capacity, well deliveries, IHR and the fast-track initiative (30.11.13) |
| A recognized and value creating exploration company | Finding cost | Deliver onshore manufacturing improvement programme (01.08.13) |
| Maximise value creation through our value chains | New Resources from Exploration | Secure petroleum activities in Northern NCS areas and high impact exploration opportunities globally (30.09.12) |

**Finance**

| Finance | Relative ROACE | Implement and deliver on the seven corporate initiatives listed under "Improvement Initiative Safety and Operations" (25.08.13) |
| Retain financial robustness | Relative Shareholder Return | Building a commercial and cost conscious mindset (31.01.12) |
| Competitive shareholder return and value | | Improve exploration cost efficiency (31.05.12) |

18
More than 1400 "Ambition to Actions" across the company

......and more
Performance evaluation - from narrow measurement to a holistic assessment

Pressure testing KPI results:

- Deliver towards the strategic objectives?
- How ambitious KPI targets?
- Changed assumptions, with positive or negative effect?
- Agreed actions implemented, or corrective actions initiated as needed?
- Delivered results sustainable?

Living the values

- Day-to-day observations
- 360° / 180° / 90° surveys
- People survey

Ambition to Action

Delivered

Behaviours

Development plan
Rewards
Towards a simpler, more dynamic and self-regulating Ambition to Action process

More cost conscious
- less «cost cutting»

More event driven
- less calendar driven

More translation
- less cascading

More relative
- less absolute KPIs

More transparency
- less secrecy

Simple is not the same as easy!
Questions or comments - now or later?

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Beyond Budgeting Round Table
www.bbrrt.org
Want to learn more?

1. The problems with traditional management
2. The Beyond Budgeting model
3. The Borealis case
4. The Statoil case
5. Implementation advice

Wiley (US)
Available from e.g. Amazon.co.uk

(Available also in Russian and Japanese)
Other recommended books

Beyond Budgeting
Beyond Performance Management
Future Ready
The Leader’s Dilemma
Back up
Implementation advice

- Create problem understanding before talking solutions
- What’s the real risk - upside vs downside
- Design to 80% and jump
- You can’t get rid of «command and control» through command and control
- Careful if starting with rolling forecasting
- Keep the cost focus
- Involve HR and Agile IT
- Don’t become a fundamentalist
Too holistic, too subjective? Can never be 100% objective!

**KPI DEFINITION UNCERTAINTY**

Right KPI? Indicator only!

**KPI TARGET UNCERTAINTY**

What is the right number?

Target - what does good performance look like in 12 months?

Forced to be subjective (must make assumptions)

Why not subjective also here? (assumption uncertainty is gone)

Evaluation

Measurement

Jan

Dec
The mindset required…..
– cost conscious from the first penny

Do I have a budget for this?

Is this really necessary?
What is good enough?
How much value is this creating?
Is this within my execution framework?

Budget

Not OK

OK

OK?
…..and the tools available

Select based on what works best in your business

Monitoring of actual development, intervention if needed only