An introduction to Beyond Budgeting

- business agility in practice

Bjarte Bogsnes
Equinor
Chairman-Beyond Budgeting Roundtable

Outline

- The case for change – what is the problem?
- Beyond Budgeting
    - The model
    - Cases
- The Equinor model – Ambition to Action

The illusion of control

The definition

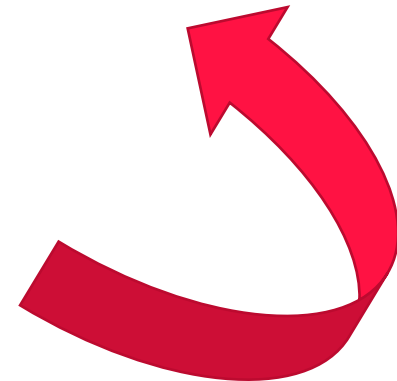"The power to influence or direct people's behaviour or the course of events"

The grand illusion

- People can and must be managed
- The future is predictable and manageable

In business terms

- Controlling people
- Controlling the future

«Most of what we call management is about making it difficult for people to do their job»

Peter Drucker

"Most corporate planning is like a ritual rain dance. It has no effect on the weather, but those who engage in it think it does. Much of the advice and instruction is directed at improving the dancing, not the weather" - Russel L. Ackoff

Budget problems

Very time consuming

Assumptions quickly outdated

Stimulates unethical behaviours

Creates illusions of control

Decisions made too early and often too high up

Can prevent value adding activities

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**?

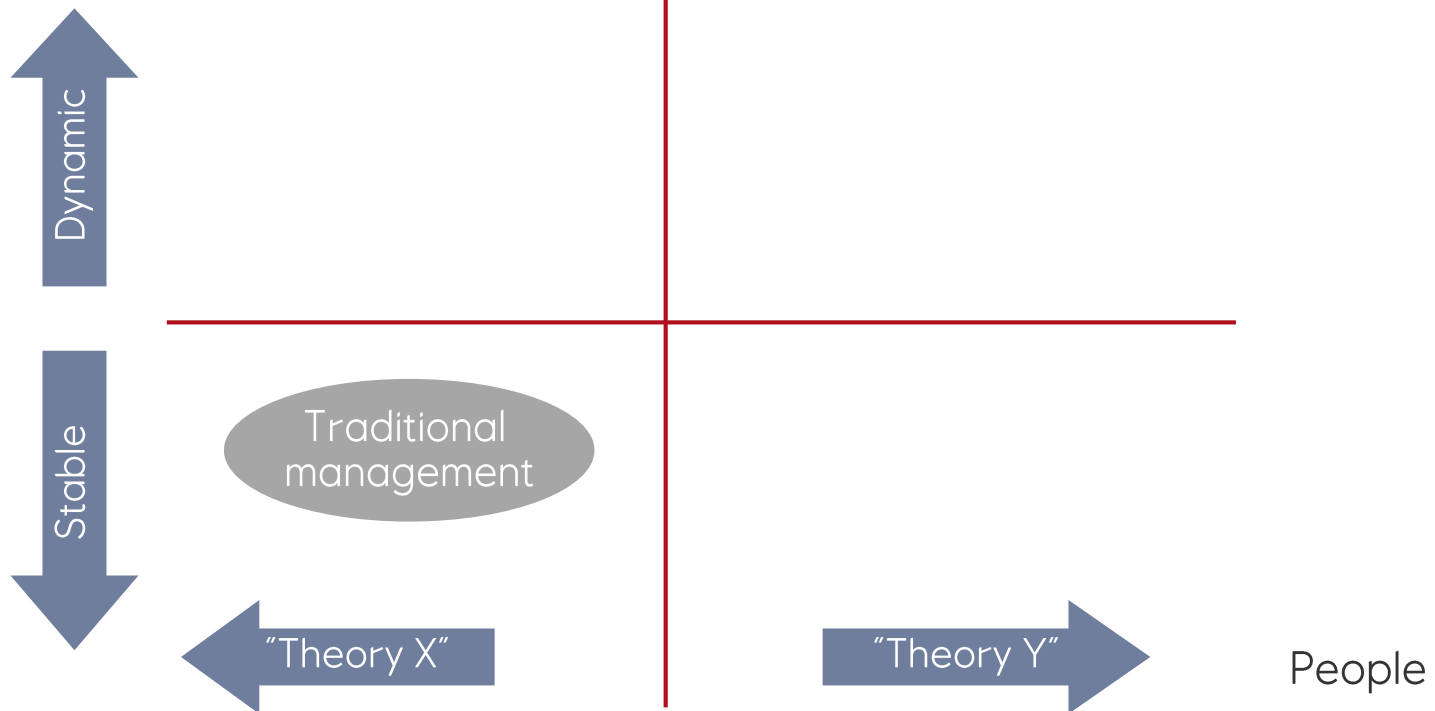# In which are **values** most important?

From *managing* performance......

....to *enabling* performance

The world has changed
– what about the way we lead and manage?

We must change both processes and leadership

Processes

Dynamic ↑
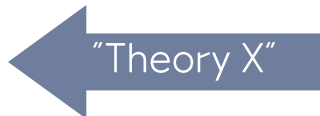
No traditional detailed budgets

Relative and directional goals

Dynamic planning, forecasting and resource allocation

Holistic performance evaluation

Stable ↓

Rigid, detailed and annual

Rules-based micro management

Centralised command and control

Secrecy, sticks and carrots

← "Theory X"

Values based

Autonomy

Transparency

Internal motivation

"Theory Y" →

Beyond Budgeting
- more adaptive
- more human
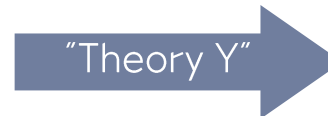
Leadership

Companies on the journey

Beyond Budgeting
- the adaptive management model

Leadership principles
1. Purpose - Engage and inspire people around bold and noble causes; **not** *around short-term financial targets*
2. Values - Govern through shared values and sound judgement; **not** *through detailed rules and regulations*
3. Transparency - Make information open for self-regulation, innovation, learning and control; **don't** *restrict it*
4. Organisation – Cultivate a strong sense of belonging and organise around accountable teams; **avoid** *hierarchical control and bureaucracy*
5. Autonomy - Trust people with freedom to act; **don't** *punish everyone if someone should abuse it*
6. Customers - Connect everyone's work with customer needs; **avoid** *conflicts of interest*

Management processes
7. Rhythm - Organise management processes dynamically around business rhythms and events; **not** *around the calendar year only*
8. Targets - Set directional, ambitious and relative goals; **avoid** *fixed and cascaded targets*
9. Plans and forecasts - Make planning and forecasting lean and unbiased processes; **not** *rigid and political exercises*
10. Resource allocation - Foster a cost conscious mind-set and make resources available as needed; **not** *through detailed annual budget allocations*
11. Performance evaluation - Evaluate performance holistically and with peer feedback for learning and development; **not** *based on measurement only and* **not** *for rewards only*
12. Rewards - Reward shared success against competition; **not** *against fixed performance contracts*

Equinor in brief

- Turnover approx. 60 bn. USD
- 20.000 employees in 40 countries
- World's largest operator in waters deeper than 100 metres
- Second largest gas exporter to Europe
- Large offshore wind player
- Listed in New York and Oslo
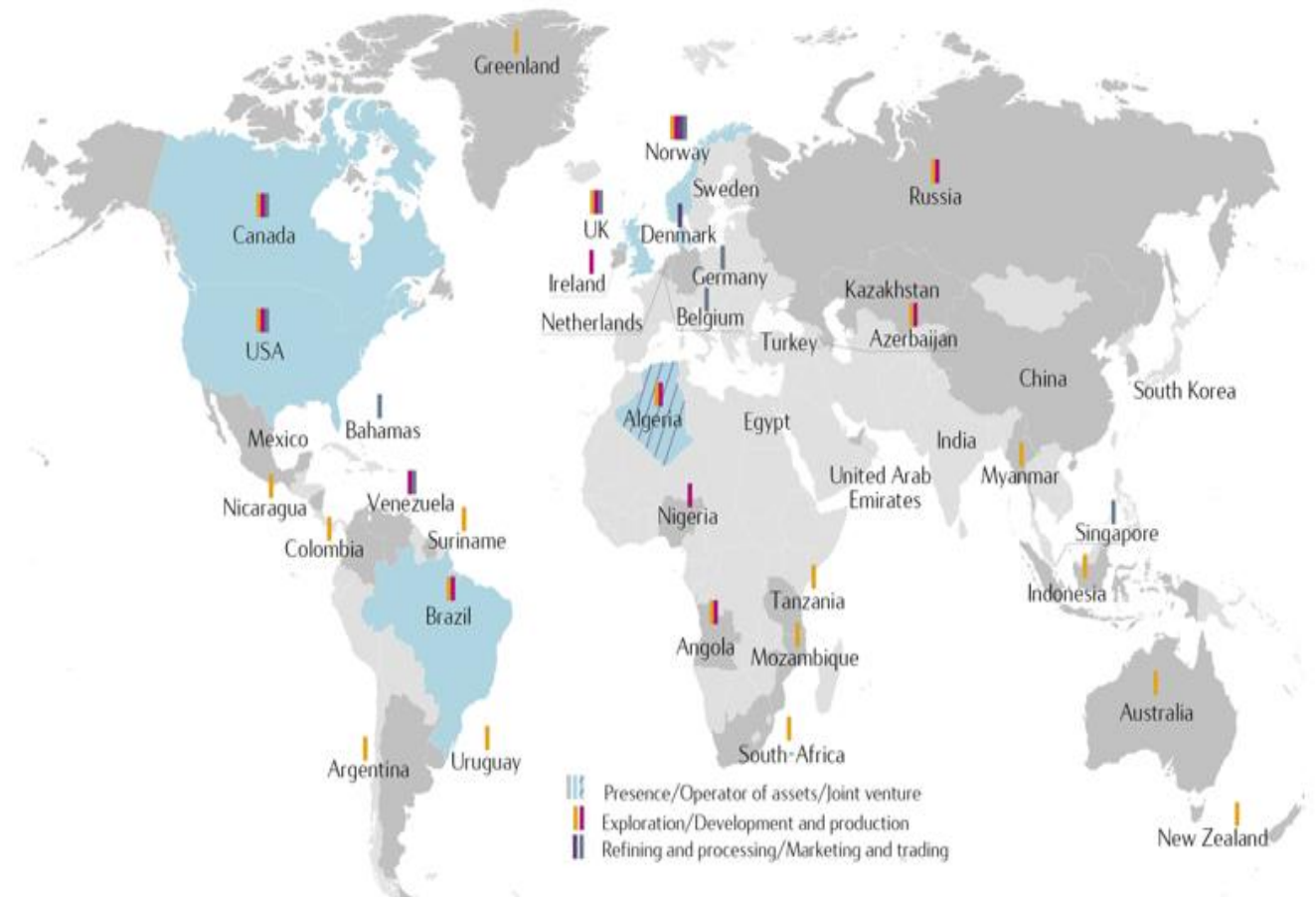
Getting started - solving the budget conflict

The budget purposes

- Target
- Forecast
- Resource allocation

Same number - conflicting purposes

1. Separate

Target
What we want to happen

Forecast
What we think will happen

Resource allocation
What it takes to make it happen

Different numbers

2. Improve

- Inspiring & stretching
- VUCA robust

- Unbiased – expected outcome
- Limited detail

- Dynamic – no detailed allocation
- KPI targets, mandates, decision gates and decision criteria
- Trend monitoring

Event driven - not calendar driven

Ambition to Action - purpose and process

- Translating strategy and managing risk

- Securing agility - room to act and perform

- Activating values and leadership principles

| Strategic objectives | → | Risks | → | Actions & forecasts | → | Indicators | → | Individual or team goals |

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

What are the risks?
- Identify
- Analyse
- Evaluate

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

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

What is my or our contribution?

My or our Performance Goals
- Delivery
- Behaviour

Shaping the future of energy

STRATEGIC OBJECTIVES

Safety, security and sustainability
An industry leader in safety, security and carbon efficiency

Where are we going?

People and organisation
A values-based and high-performing organisation

Operations
A driver of energy industry transformation

Market
A flexible and resilient energy portfolio

Finance
A cash generating, profitable and competitive company

RISKS

Major accident

Injury to personnel

Cyber-attack

Regulatory framework related to climate

What are the risks?

Workforce capabilities

Core values and...

Business integrity

Production

Project execution

Digitalization and efficiency

Resource replenishment

Energy transition

Oil price

Natural gas price

Robustness and Financial Flexibility

Unstable regulatory and fiscal framework

Competitive cost level

ACTIONS

Enhance safety initiatives to accommodate a step change in safety

Continue to implement 2020 security roadmap with focus on compliance and competence development

Strenghten information security measures to safeguard Statoil's information systems and assets

Strengthen people development through learning and deployment

Strengthen our values-based delivery culture through value creation leadership and culture

How do we get there - managing the risks?

Optimise production to maximise value creation

Develop and capture value from the portfolio and drive production attainment

Drive efficiency and cost discipline across the business, implement new work processes by Lean implementation

Access, mature and drill high quality prospects

Highgrade the portfolio, and strenghten core areas through attractive BD opportunities

Ensure sufficient financial capacity

Secure trust, support and a strong reputation among key stakeholders (continued)

DPUSA 90-50

INDICATORS

Serious incidents frequency (SIF) Serious HSE incidents

Total recordable injury frequency (TRIF)

CO2 intensity for the upstream portfolio

Oil-/gas leakage

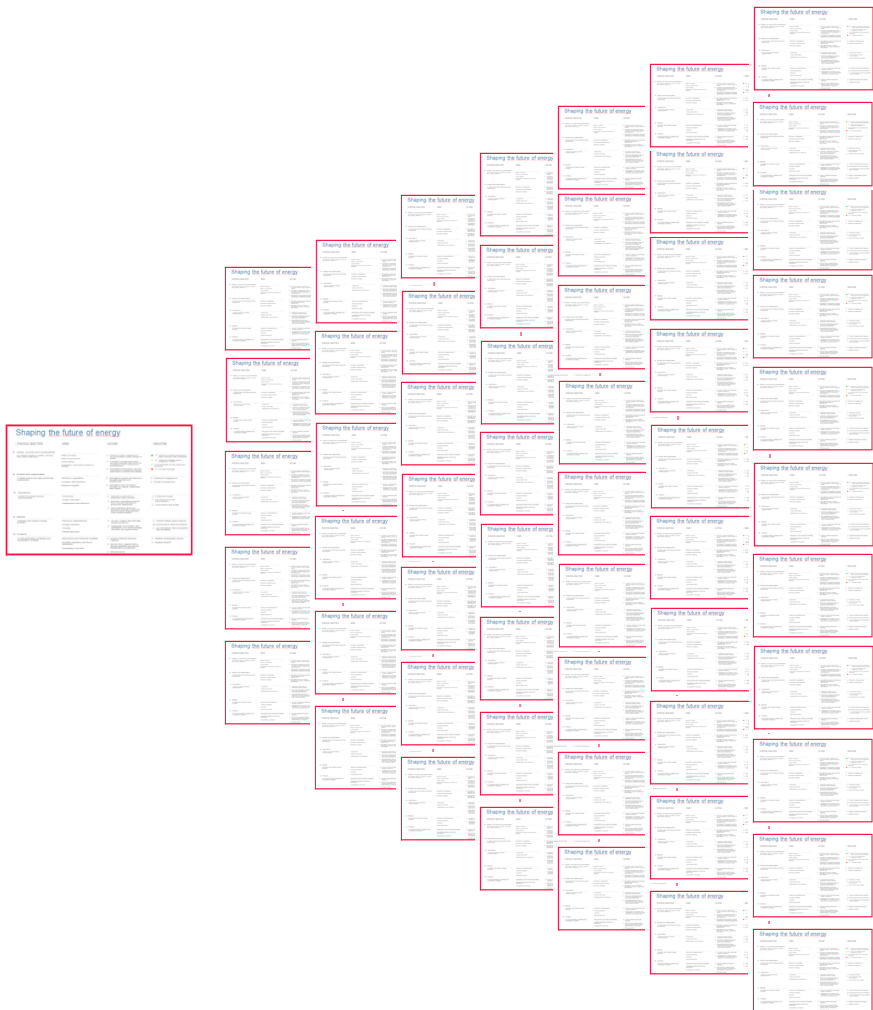Employee Engagement

People Development

Production Equity

cec PRODUCTION EFFICIENCY

Fixed OPEX and SG&A...

How do we measure progress?

...PEX per annual...

cec RESOURCE REPLACEMENT

cec RESERVE REPLACEMENT RATIO (RRR)

Relative Shareholder Return

Relative RoACE

More than 600 Ambitions to Actions across the company

- **Alignment:** Through translation, not cascading

- **Rhythm**: - More business and event-driven than calendar-driven

Why a holistic performance evaluation?

| Fixed targets struggle in a dynamic world | Create comfort around ambitious targets | KPIs are *indicators,* does not always tell the full story | Always wiser in hindsight, always more information |

" Not everything that counts can be counted,
and not everything that can be counted counts

(Albert Einstein)

A broader performance evaluation
## - from narrow measurement to a <u>holistic</u> assessment

Ambition to Action

"Pressure testing" measured results:

- Deliver towards the strategic objectives?

- How ambitious targets?

- Changed assumptions, with positive or negative effect?

- Which risks were taken?

- Delivered results sustainable?

Delivery

50/50

Behaviour

Development Rewards

Living the values
- Day-to day-observations
- Global People Survey
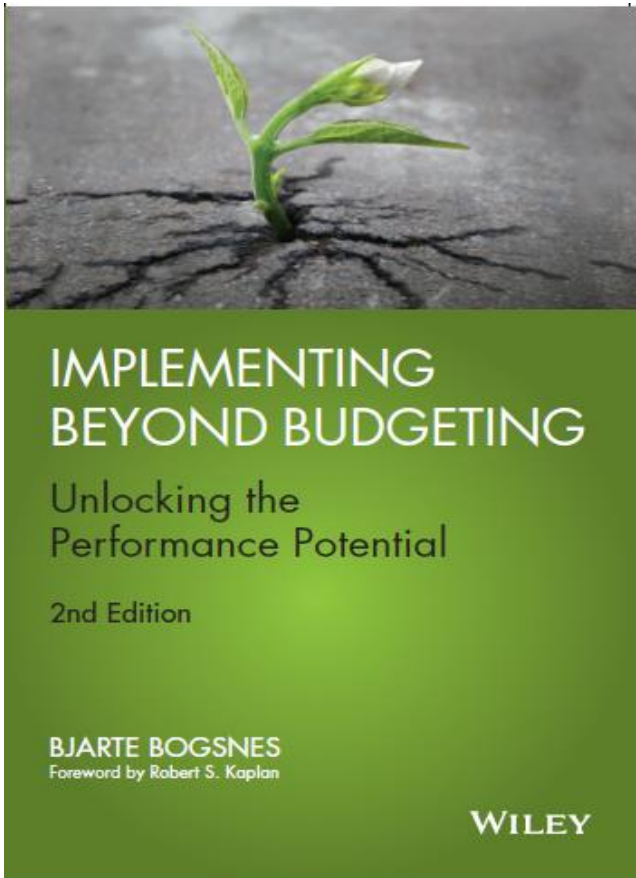
Want to hear more?

1. The problems with traditional management
2. The Beyond Budgeting model

   Cases: Handelsbanken, Miles, Reitangruppen
3. The Borealis case
4. The Statoil case
5. Beyond Budgeting and Agile
6. Implementation advice

Wiley (US). Translated to Chinese, Japanese and Russian

"At last, Bjarte Bogsnes has made his experience and enthusiasm for Beyond Budgeting available for a wider audience with this remarkable book. I have appreciated his engagement in these important management issues for many years, and his knowledge and leadership has been critical in the transformation of our organization."

-Eldar Sætre, CEO Equinor