SCALING UP
How a few Companies Make it…and Why the Rest Don't
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Authors Bio: Verne is founder of the world-renowned Entrepreneurs' Organization (EO) and chaired for 15 years EO's premier CEO program, the "Birthing of Giants," held at MIT. Founder and CEO of Gazelles, a global executive education and coaching company with hundreds of partners on six continents, Verne has spent more than 30 years educating entrepreneurial teams.

Author's Big Thought: Scaling Up focuses on the four major decisions areas that every company must get right: People, Strategy, execution and Cash management. Running a business is ultimately about freedom. Scaling Up shows business leaders how to get their organizations moving in sync to create something significant and enjoy the ride. This book clearly lays out precisely what the management team must do to lead their entire company through multiple growth phases.

THE INTRODUCTION: Tools for Scaling Up

- CEOs and executives of growth firms want ideas and tools they can implement immediately to improve some aspect of their business — and want to enjoy the ride along the way!
- The following sequence describes the life cycle of most businesses as they move up the S-shaped curve of growth. The key to scaling this curve:
  1. Attracting and keeping the right People;
  2. Creating a truly differentiated Strategy;
  3. Driving flawless Execution; and
  4. Having plenty of Cash to weather the storms. This book gives you the tools to scale up 10x.

- Senior leaders know they have succeeded in building an organization that can scale — and is fun to run — when they are the dumbest people in the room! In turn, if they have all the answers (or act like they do), it guarantees organizational silence, exacerbates blindness (the CEO is always the last to know anyway), and means the senior team ends up carrying the entire load of the company on their backs.
- The best leaders have the right questions, but turn to their employees, customers, advisors, and the crowd to mine the answers.
- Every business is more valuable to the degree that it does not depend on its top leader.

- To scale up a business from a handful of employees to something significant, our tools and techniques focus on three deliverables:
  1. Reduce by 80% the time it takes the top team to manage the business (operational activities)
  2. Refocus the senior team on market-facing activities
  3. Realign everyone else (onto the same page) to drive execution and results

- And when these tools are successfully implemented, organizations attain these four outcomes:
  1. At least double the rate of cash flow
  2. Triple the industry average profitability
  3. Increase the valuation of the firm relative to competitors
  4. Help the stakeholders — employees, customers, and shareholders — enjoy the climb

- Yet there are three barriers to scaling up, which we'll discuss in the next chapter:
  1. Leadership: the inability to staff/ grow enough leaders throughout the organization who have the capabilities to delegate and predict
  2. Scalable infrastructure: the lack of systems and structures (physical and organizational) to handle the complexities in communication and decisions that come with growth
  3. Market dynamics: the failure to address the increased competitive pressures that build (and erode margins) as you scale the business

- Therefore, your team must use our tools to master four fundamentals:
  1. **In leading People**, take a page from parenting: Establish a handful of rules, repeat yourself a lot, and act consistently with those rules. This is the role and power of Core Values. If discovered and used effectively, these values guide all the relationship decisions and systems in the company.
  2. **In setting Strategy**, follow the definition from the great business strategist Gary Hamel. You don't have a real strategy if it doesn't pass two tests: First, what you're planning to do really matters to enough customers; and second, it differentiates you from your competition.
  3. **In driving Execution**, implement three key habits: Set a handful of Priorities (the fewer the better); gather quantitative and qualitative Data daily and review weekly to guide decisions; and establish an effective daily, weekly, monthly, quarterly, and annual meeting Rhythm to keep everyone in the loop. Those who pulse faster, grow faster.
  4. **In managing Cash**, don't run out of it! This means paying as much attention to how every decision affects cash flow as you would to revenue and profitability. With these fundamentals in mind, you're ready to start climbing.

- There is a set of habits — routines — that will make the climb easier. "Routine sets you free" is a key driving principle behind our methodologies and tools. You may set a goal to lose weight, but unless you change some daily and weekly routines, it will never be accomplished. Goals without routines are wishes; routines without goals are aimless. The most successful business leaders have a clear vision and the disciplines (routines) to make it a reality.

4D Framework
The framework includes these elements:

    1. **Driver:** Leaders drive implementation of the Rockefeller Habits with their teams. Execution is much easier if they and their teams engage in coaching, embrace learning, and encourage the use of new technologies to accelerate implementation of our tools.

2. **Demands:** Leaders have to balance two often competing demands on the business — People and Process. This requires simultaneously maintaining a great reputation with the employees, customers, and shareholders; and improving the productivity of how the firm makes/ buys, sells, and tracks these transactions.

3. **Disciplines:** To effectively execute, there are three fundamental disciplines (routines): Set Priorities; gather quantitative and qualitative Data; and establish an effective meeting Rhythm. It's in these meetings, debating the data (the brutal facts!), where the priorities emerge.

4. **Decisions:** Ultimately, all of the above require some decisions. To scale the business requires getting four key decision sets — People, Strategy, Execution, and Cash.

Right Questions

- Much of our work is helping leadership teams formulate the right questions. Once they get the questions right, the answers tend to appear.
- To start implementing the 4D Framework, the first question is, "Which of the 4 Decisions — People, Strategy, Execution, and Cash — needs the most attention next?" Start there!
- The following overview of each decision will further help you choose where to start in scaling up the business.

People

KEY QUESTION: Are the stakeholders (employees, customers, shareholders) happy and engaged in the business; and would you "rehire" all of them? Do you have the "right people doing the right things right" inside the organization?

- Then you need to evaluate all the key relationships surrounding the business. Would you keep all your existing customers? Are you happy with your investors/ bank? Are your vendors supporting you properly? Are your advisors — accountants, lawyers, consultants, and coaches — the best for the size of the organization and future plans?
- One-Page Personal Plan (OPPP). Having a strong and fulfilled personal life provides an important foundation for sustaining your efforts in the business.
- Function Accountability Chart (FACe): The FACe tool provides a list of seats (functions) that all organizations must fill. You want to delegate these functions to people who fit your culture and pass two tests: 1. They don't need to be managed. 2. They regularly wow the team with their insights and output.
- Next designate one or two key performance indicators (KPIs) for each function, defining objectively what activities each senior leader needs to be focused on day-to-day.
- Last, decide on a handful of results/ outcomes accountable to each function (i.e., who is accountable for revenue, gross margin, profit, cash, etc.). These outcomes normally represent line items on the financial statements. When completed, this one-page accountability tool helps you diagnose where you have people and performance gaps on the leadership team.
- Process Accountability Chart (PACe): Most work flows horizontally across the various functions. Functions are not isolated cells. When these functions aren't working well together, the firm can stall. This chart provides a place to delineate the four to nine processes that drive the business
- Next, designate who is accountable for each process.
- Last, decide on two or three KPIs that track the health of the process — the most important being the length of time, from start to finish, for a specific process.

Strategy

KEY QUESTION: Can you state your firm's strategy simply — and is it driving sustainable growth in revenue and gross margins?

- Think about it in terms of two distinct activities: strategic thinking and execution planning. Each requires two very different teams and processes. Strategic thinking requires a handful of senior leaders meeting weekly.
- The strategic thinking team is focused on discussing a few big strategic issues including those outlined in the SWT and 7 Strata tools summarized.
- Execution planning, in turn, requires a much larger team engaged in implementing the broader strategy. Setting specific annual and quarterly priorities, outcomes, and KPIs is best if middle management and frontline employees are involved.
- Add in both disciplined action and active learning activities and you have a simple Think, Plan, Act, Learn cycle of strategic planning.

- **Vision Summary:** The Vision Summary provides a one-page format to communicate key aspects of the company's vision to employees, customers, investors, and the broader community.

- **SWT:** (strengths, weaknesses, and trends). The SWT focuses on exploring broader external trends beyond their own industry or geography. It's a powerful tool to spot opportunities.

- **The 7 Strata of Strategy:**
  1. This tool represents the seven components (stratum) of a robust, yet simply stated, strategy.
  2. What word(s) do you own in the minds of your targeted customers (e.g., Google owns "search")?
  3. Who are your core customers, what three Brand Promises are you making them?
  4. What is your Brand Promise?
  5. What is your One-PHRASE Strategy that likely upsets customers but is key to making a ton of money and blocking your competition?
  6. What are the three to five Activities that fit Harvard strategist Michael Porter's definition of the essence of differentiation?
  7. What are your Profit per X (economic driver) and BHAG ® for the company?

- **One-Page Strategic Plan (OPSP)** It's designed to drive alignment, accountability, and focus. The first three columns of the OPSP represent the strategic thinking part of the plan supported by the work done on the 7 Strata; the last four columns represent the execution planning part of the plan.

Execution

KEY QUESTION: Are all processes running without drama and driving industry-leading profitability?
- You know you have execution issues if three things exist:
  1. There is needless drama in the organization (e.g., something shipped out late; the invoice was wrong; someone missed a meeting; etc.).
  2. Everyone seems to be working more hours, spinning his wheels, or spending too much time fixing things that should have been done right the first time.
  3. Most important, the company is generating less than three times industry average profitability.

- **Who, What, When (WWW):** Improve the impact of your weekly meetings by taking a few minutes at the end and summarizing Who said they are going to do What, When.

- The key is setting a "when" that is no longer than the time between weekly (or monthly) meetings. And if you have a more substantial initiative, the key is breaking it into pieces (eat the elephant one bite at a time) that can be accomplished within a few weeks.

- **Rockefeller Habits Checklist ™:** There are 10 fundamental habits that support the successful execution of your strategy.
- The key is focusing on one or two each quarter, giving everyone roughly 24 to 36 months to install these simple, yet powerful, routines. Then it's a process of continually refreshing them as the company scales up. The habits ("Routines that set you free!"):

1. ***The executive team is healthy and aligned.*** Your executive team needs to have a level of trust that permits true debate and constructive conflict to occur. Members of the team must embrace its diversity (the more the better) and be willing to challenge each other in making decisions and exposing the brutal facts.

2. ***Everyone is aligned with the #1 thing that needs to be accomplished this quarter to move the company forward.***

3. ***Communication rhythm is established and information moves through the organization accurately and quickly.*** The key is an effective daily, weekly, monthly, quarterly, and annual Meeting Rhythm, which, when executed properly, actually saves everyone a tremendous amount of time.

4. ***Every facet of the organization has a person assigned with accountability for ensuring goals are met.***

5. ***Ongoing employee input is collected to identify obstacles and opportunities***. Talk to one employee each week and ask, "What should the company Start/ Stop/ Keep doing?" Pay particular attention to the "stops." These are the roadblocks you need to eliminate from the company to keep people motivated.

6. ***Reporting and analysis of customer feedback data is as frequent and accurate as financial data.*** It is suggested that each senior leader formally ask customers questions that are more about gathering market intel, especially about competitors, than discerning whether they like your particular product or service.

7. ***Core Values and Purpose are "alive" in the organization.*** The Purpose (a better word than "mission") provides the critical "why" behind everything you do (i.e., what difference is your company making in the world?).

8. ***Employees can articulate the following key components of the company's strategy accurately.*** All employees need to know and understand the company's 10- to 25-year goal (BHAG ®); who the core customers are; the three Brand Promises everyone needs to keep; and what the company does — and be able to explain it when asked (the elevator pitch).

9. ***All employees can answer quantitatively whether they had a good day or week***.

10. ***The company's plans and performance are visible to everyone.***

Cash

KEY QUESTION: Do you have consistent sources of cash, ideally generated internally, to fuel the growth of your business?

- Many growth company leaders pay more attention to revenue and profit than they do to cash when it comes to structuring deals with suppliers, customers, employees (think bonus plans), or investors/ banks. And when they receive their monthly financial statements, the cash flow statement is either nonexistent or ignored. The quickest action you can take is to have your CFO give you a modified cash flow statement every day detailing the cash that came in during the last 24 hours, the cash that flowed out, and some idea of how cash is looking over the next

30 to 90 days. This will keep cash top-of-mind and give you a great feel for how cash is flowing through the business.

- **The Power of One:** The 7 main financial levers available to managers to improve cash and returns in the business are:
  1. **Price:** You can increase the price of your goods and services.
  2. **Volume:** You can sell more units at the same price.
  3. **Cost of goods sold/direct costs:** You can reduce the price you pay for your raw materials and direct labor.
  4. **Operating expenses:** You can reduce your operating costs.
  5. **Accounts receivable:** You can collect from your debtors faster.
  6. **Inventory/ WIP (work in progress):** You can reduce the amount of stock you have on hand.
  7. **Accounts payable:** You can slow down the payment of creditors. The tool calculates the benefit to cash if a 1% or one-day change is made to each of these levers.

- **Cash Acceleration Strategies (CASh)** — Break down the CCC (Cash Conversion Cycle) into four components, and brainstorm one of three ways to increase the cash flow in the business. We've had many clients double their operating cash flow immediately after working through this tool.

2. THE BARRIERS: Leadership, Infrastructure, and Market Dynamics

EXECUTIVE SUMMARY: There are predictable evolutions and revolutions as an organization grows. These are dictated by the increasing complexity that comes with adding employees, customers, product lines, locations, etc. Handling a company's growth successfully requires three things: an increasing number of capable leaders; a scalable infrastructure; and the ability to navigate certain market dynamics. If these factors are missing, you will face barriers to growth. Scaling up successfully requires leaders who possess aptitudes for prediction, delegation, and repetition.

The growth paradox: the belief that as you scale the company — and increase your dream team, prospects, and resources — things should get easier, but they don't. Things actually get harder and more complicated.

Complexity:
- Expanding from three to four people grows the team only 33%, yet complexity may increase 400%. And the complexity just keeps growing exponentially. It's why many business owners often long for the day when the company was just them and an assistant selling a single service. This complexity generates three fundamental barriers to scaling up a venture:
  1. Leadership: the inability to staff/ grow enough leaders throughout the organization who have the capabilities to delegate and predict
  2. Scalable infrastructure: the lack of systems and structures (physical and organizational) to handle the complexities in communication and decisions that come with growth
  3. Market dynamics: the failure to address the increased competitive pressures that build (and erode margins) as you scale the business
- When you remove these barriers, then that you can better navigate through those points in the company's growth where you're bigger, but not quite big enough to have the next level of talent and systems needed to scale the venture.

Leadership: Prediction, Delegation, and Repetition

- As goes the leadership team, so goes the rest of the company. Whatever challenges exist within the organization can be traced to the cohesion of the executive team and its capabilities in prediction, delegation, and repetition.

Prediction:

- Leaders don't have to be years ahead, just minutes ahead of the market, the competition, and those they lead. The key is frequent interaction with customers, competitors, and employees. This is much easier when the company is small and becomes increasingly more difficult as the business scales up.
- Senior leaders become further isolated from customers and frontline employees, losing their gut feel for the business and the marketplace. Ultimately, our tools and techniques will free the senior team so they can spend 80% of the week engaged in market-facing activities.

Delegation:

- Letting go and trusting others to do things well is one of the more challenging aspects of being a leader of a growing organization.
- To get to 10 employees, founders must delegate activities in which they are weak. To get to 50 employees, they have to delegate functions in which they are strong! In many cases, the strength of the top leader becomes the weakness of the organization.
- From 50 employees on up, the senior leaders must develop additional leaders throughout the organization who share the same values, passion, and knowledge of the business. This way they have enough talent to whom they can delegate the myriad number of activities and transactions necessary to grow the business.
- Successful delegation requires four components, assuming you have delegated a job to the right person or team:
  1. Pinpoint what the person or team needs to accomplish (Priorities — One-Page Strategic Plan).
  2. Create a measurement system for monitoring progress (Data — qualitative and quantitative key performance indicators).
  3. Provide feedback to the team or person (Meeting Rhythm).
  4. Give appropriately timed recognition and reward (because we're dealing with people).

Repetition

- The leader's final job is "to keep the main thing the main thing" — to keep the organization on message and everyone heading in the same direction.
- Repetition encompasses consistency. Finish what you start. Mean what you say. And don't say one thing and do something else. Consistency is an important aspect of repetition.
- A key function of leadership is delivering frequent messaging and metrics to reinforce these key attributes of the company and culture.

Scalable Infrastructure

To keep things flowing, an organization needs a scalable infrastructure.

Market Dynamics

- When the market is going your way, it covers up a lot of mistakes. When fortunes reverse, all your weaknesses seem to be exposed.
- As the firm scales from $ 1 million to $ 10 million in revenue, the senior team tends to be focused externally on amassing new business. Yet this is precisely the time when a little more

internal focus, to establish healthy organizational habits and a scalable infrastructure, would pay off in the long term.

- As the business scales past $ 10 million, organizational complexities tend to draw the attention of the senior team inward (leading to firefighting). This is precisely when the team needs to be focused more externally on the marketplace (by talking to customers), given the increased competitive pressures that come with size.
- There is also an important sequence of focus when it comes to your financial metrics. Between startup and the first million or two in revenue, the key driver is revenue (sell like hell). The focus is on proving that a market exists for your services. As for cash, which many business owners might think is the first focus, the entrepreneur has to rely mainly on family and friends (or fools!).
- It's between $ 1 million and $ 10 million that the team needs to focus on cash. Growth sucks cash, and since this is the first time the company will make a tenfold jump in size, the demands for cash will soar.
- This is when the cash model of the business needs to be worked out (e.g., "How is the business model going to generate sufficient cash for the company to keep growing?"). As the organization passes $ 10 million in revenue, new internal and external pressures come to the forefront. Externally, your organization is on more radar screens, alerting competitors to your threats. Customers are beginning to demand lower prices as they do more business with your company. At the same time, internal complexities increase, which cause costs to rise faster than revenue. All of this begins to squeeze an organization's gross margin. As gross margin slips a few points, the organization is starved of the extra money it needs in order to invest in infrastructure, like accounting systems and training. This creates a snowball effect of further expensive mistakes as the company passes the $ 25 million mark.
- To prevent the erosion in your margins, it's critical that you maintain a clear value proposition in the market. At the same time, the company must continually streamline and automate internal processes to reduce costs. Organizations successful at doing both will see their gross margins increase during this stage of growth, giving them the extra cash they need to fund infrastructure, training, marketing, R& D, etc. By the time it reaches $ 50 million in revenue, an organization should have enough experience and a strong-enough position in the market to predict profitability accurately.
- Which brings us full circle to the main function of a business leader: to build a predictable revenue and profit engine in an unpredictable marketplace and world.
- It's this predictability, driven by effective processes, that is ultimately the key to crafting an organization that attracts and keeps top talent; creates products and services that satisfy customer needs; and generates significant wealth.
- In summary, growing a business is a dynamic process as the leadership team navigates the evolutions and revolutions of growth. To deal with these challenges, the company must grow the capabilities of the leadership team throughout the organization; install scalable infrastructure to manage the increasing complexities that come with growth; and stay on top of the market dynamics that affect the business. To do this, there are 4 Decisions that leaders must address: People, Strategy, Execution, and Cash.

SCALING UP PEOPLE

KEY QUESTION: Are all stakeholders (employees, customers, shareholders) happy and engaged in the business; and would you "rehire" all of them?

If you fail to address these relationship issues head on, they will continue to drain your emotional energy, leaving little left to expend on the Strategy, Execution, and Cash aspects of the business. That's why we address People first in our 4 Decisions model.

3: THE LEADERS The FACe and PACe of the Company

EXECUTIVE SUMMARY: "The bottleneck is always at the top of the bottle," notes management guru Peter Drucker. Challenges within the company normally point to issues with, or among, the leaders. To address them, this chapter will focus on the leadership team. We will share three tools that help leaders get clear on their personal goals; define senior leadership accountabilities, key performance indicators (KPIs), and outcomes; and delineate the four to nine processes that drive the company.

- As a company scales up, the toughest decisions involve people and their changing roles in the organization, especially within the leadership team. Loyalties, egos, and personal friendships make these decisions even more difficult when the company faces a situation in which it has outgrown some of its early leaders.

- The main principle underpinning effective organizational design is to divide big teams into smaller ones aligned around projects, product lines, customer segments, geographical locations, etc., based on the idea of getting everyone in the organization into small teams and as close to his or her respective customers as possible. This is a way to increase the surface area of the company, giving the maximum number of employees a chance to interact with the marketplace.
- It's important to delineate the differences between accountability, responsibility, and authority.

Accountability, Responsibility, and Authority

- These business terms are often haphazardly interchanged. Here are our definitions:
- *Accountability:* This belongs to the ONE person who has the "ability to count" — who is tracking the progress and giving voice (screaming loudly) when issues arise within a defined task, team, function, or division. The rule: If more than one person is accountable, then no one is accountable, and that's when things fall through the cracks.
- *Responsibility:* This falls to anyone with the "ability to respond" proactively to support the team. It includes all the people who touch a particular process or issue.
- *Authority:* This belongs to the person or team with the final decision-making power.
- Those who have advanced up the ranks find that they've taken on increasingly more accountability for things they have less and less real control over — until they reach the top. Leaders get paid the big bucks — to bridge this ever-increasing gap between accountability and authority, using their skills of communication, persuasion, education, visioning, etc.

One-Page Personal Plan (OPPP)

- Just as there are 4 Decisions you make to build a thriving company — People, Strategy, Execution, and Cash — there are parallel areas in your personal life — Relationships, Achievements, Rituals, and Wealth.

Column 1 — Relationships

- List the key groups of people with whom you want a lasting relationship (10 to 25 years). In your personal life, important relationships include family and friends. Also list the various communities in which you're involved.

- The next step is to look at the groups listed and pick a few key relationships on which to focus your attention for the next 12 months and the next 90 days.
- There's a space on the form where you can note relationships you want to end gracefully.

Column 2 — Achievements
- Think about the major ways you'd like to make an impact through your work beyond reaching monetary goals. In your personal life, you'll want to think about how you can make a real difference to the key people in your life. The key is focusing on short-, medium-, and long-term achievements relative to the people listed in the relationship column.

Column 3 — Rituals
- Establishing regular routines in your life will help you achieve your larger goals. There might be some bad habits or behaviors you wish to stop.

Column 4 — Wealth
- Rather than viewing financial wealth as an end in itself, see it as a resource for supporting the rest of your personal plan. Overall, focus on how your wealth will flow through you in the service of others, rather than hoarding it. This seems to attract more wealth — the natural law of reciprocity.

Function Accountability Chart (FACe)
- The second one-page People tool — the Function Accountability Chart (FACe) — focuses on making sure you have the right butts in the right seats at the top of the organization.
- You want to delegate the functions listed on the FACe tool to leaders who pass two tests (including culture fit):
  1. They don't need to be managed.
  2. They regularly wow the team with their insights and output.
- The chart asks you to list one or two key performance indicators (KPIs) for each function. These KPIs represent the measurable activities each functional leader needs to perform on a day-to-day basis.
- The last column on the chart captures the outcomes expected for each function (i.e., who is accountable for revenue, gross margin, profit, cash, etc.). These outcomes normally represent line items on the financial statements.
- If you need to bring someone in from the outside to fill a senior leadership position, you should do this only once every six to nine months. The rule is to take it slow when bringing outsiders into senior leadership roles. The exception is when the company is venture-backed and/ or growing 100% a year and needs to bring on three or four key executives within a short period of time.

Completing Your Function Accountability
STEP 1
- The first column lists the functions every business must support and provides a few blanks so you can add those unique to your business. There is also space to note discrete business units. Focus on the jobs that need to get done.

STEP 2
- Once the team has agreed on the people accountable for each function, consider the four questions summarized at the bottom of the form:
  1. Do you have more than one person accountable for a function? The rule is that only one person should be accountable; otherwise, there will be confusion. Having more than one name in a box is a red flag.

2. Does someone's name show up in more boxes than everyone else's?

3. Do you have any boxes with no names in them? This often happens when someone says, "Hey, who's accountable for marketing?" and the response is, "All of us!" "All of us" really means "none of us," and the box should be left blank.

4. Are you enthusiastic about the person you have in each box?

ACTION: Discuss these four questions and decide where there are glaring gaps in the leadership team.

STEP 3

- The second blank column is for listing one to three KPIs for each of the listed functions. These are intended to be leading indicators, measuring the daily and weekly activities of a particular leader and meant to drive superior results.

ACTION: In the third column of the FACe, note one or two KPIs — leading indicators — for each function and business unit.

STEP 4

- For the fourth column of the FACe — "Results/ Outcomes" — pull out a recent detailed Profit and Loss (P& L) and Balance Sheet (B/ S) statement and assign a person accountable for each line item. Then discuss the same four questions we asked earlier about the people listed for the functions (summarized at the bottom of the FACe tool).
- As with the functions, spread the workload evenly among the leadership team, with just one person ultimately accountable for each line item.

ACTION: Go through your financial statements and decide who is accountable for each line item. Then pick the most important line items for each of the functions listed on your FACe tool and transfer the answers to the "Results/ Outcomes" column.

Process Accountability Chart (PACe)

- The third one-page People tool — the Process Accountability Chart (PACe) — lists who is accountable for each of the four to nine processes that drive the business and how each process will be measured to guarantee it's running smoothly.
- We strongly recommend that companies implement the principles of Lean. Lean is an approach to process design focused on eliminating time wasted on activities that don't add value for customers. Lean, though it requires a real change in mindset, uses a few very simple tools to drive dramatic improvements.

Completing Your Process Accountability Chart (PACe)

STEP 1

- Gather your executive team together (it's smart to include some middle managers) and name the four to nine key processes driving the business. This chart takes a couple of 90-minute sessions to complete.

ACTION: Discuss and agree on the four to nine key processes in your organization.

STEP 2

- Next, assign accountability for each process to a specific person. Remind everyone that assigning someone accountability for a process doesn't mean that he is the new boss of everyone who touches the process, nor does he necessarily have increased decision-making authority.

- His job is to monitor the process (time, cost, quality), let the team know if there are any issues, and lead a regular meeting to fix or improve that particular process. Ideally, this person will have some cross-functional experience.

ACTION: For each key process you've identified, decide who within the organization will be accountable. These people are then accountable to the head of operations.

STEP 3

- Identify a few KPIs to track each process. One of the most important KPIs for processes is time — in either number of days (to deliver) or number of hours (to produce). Although time is not the only KPI, it does drive efficiency in your business and customer satisfaction and is the key measurement in the Lean process of designing and streamlining processes.

ACTION: List one to three KPIs for each process to measure its speed, quality, and cost.

Mapping the Process

- It's important to revisit and examine one process every 90 days as part of your quarterly planning process. With four to nine processes, each will get examined roughly every 12 to 24 months, which is sufficient to keep your company running drama-free.

ACTION: Assemble the appropriate people for each key process, and list, debate, and decide the steps and decision points for that process.

Checklists

- Once you've identified and mapped your processes, you can then bring them to life every day through checklists.
- To conclude, the strength of your People comes from the right leadership doing the right things right (FACe); and the right systems and processes supporting these people to keep the business flowing (PACe). With the combination of the right FACe and the right PACe, you have the key people and process ingredients for a great company.

4: THE TEAM Attracting and Hiring

EXECUTIVE SUMMARY: Attracting and hiring A Players, at all levels of the organization, is as critical as landing the right customers. This requires the active participation of the marketing function in the recruiting process and the use of Topgrading methodology in the interviewing and selection process. With both, detailed in this chapter, your company will have a huge pool of candidates from which to choose enough "strange" people (who fit your differentiated strategy and culture) to scale up the business.

NOTE: The cost of a bad hire is 15x his or her annual salary, according to Topgrading, so it's important to get the recruiting and selection process right.

Get the Best Talent

- Before starting your search for a key executive or frontline associate, create a Job Scorecard (vs. the standard job description). A Job Scorecard details a person's purpose for the job, the desired outcomes of this individual's work, and the competencies — technical and cultural — required to execute it.
- You need to attract the largest and most capable talent pool excited about the job and willing to accept your compensation package (e.g., McDonald's has the same chances of hiring A Players as Goldman Sachs), and have the tools to select the best people from this group of prospects. The Job Scorecard is the starting point.

- A central element of a Job Scorecard is the handful of specific and measurable outcomes that a potential hire needs to accomplish over the coming one to three years. While a job description tends to list what people will be doing, a Job Score-card describes the outcomes you want from such activities.
- Being specific about outcomes allows you to directly evaluate each candidate's capacity to actually deliver these results. Another central element is the list of candidate competencies that align with your culture and strategy. It's more important to hire for this kind of fit than for specific skills, so long as a person has the capacity to learn and grow.
- In addition to seeking culture fit, it is critical to hire people who can deliver on the Brand Promises and activities underpinning your strategy.
- These central elements of the Job Scorecard — the outcomes and competencies — drive the recruiting, interviewing, and selection process.
- If you want to have a differentiated strategy, you can't hire, compensate, and have the same HR systems supporting the same people as your competition. You need a "strange" culture and a "strange" strategy to differentiate your firm in the marketplace. This is why it's so critical to discern the real Core Values underpinning your culture; and create the elements of an industry-dominating strategy.

Recruiting Is a (Guerilla) Marketing Function
- The best people to consider first are those with whom you have already worked.
- Research strongly suggests that you need a minimum of 20 applicants per position (frontline to senior) if you want to dramatically increase your odds of hiring A Players.
- The marketing team must be as actively involved in recruiting a steady stream of potential employees as it is in attracting potential customers, yet most organizations fail miserably in this area. The key to finding the right people is by creating a recruitment strategy that reflects your Core Values and Purpose and then using your marketing skills to reach the right potential pool of talent.
- It is easy to stand out if you use whatever approach fits your culture and you show some originality.

The Topgrading Interview
- Once you have attracted a large number of qualified candidates, which significantly increases your chances of finding A Players, a rock-solid evaluation process (is needed to bring the numbers down from 20 to 10, then to three, and finally to the one top candidate who will deliver 150% of your Job Scorecard.
- The Topgrading methodology includes a screening interview used to further narrow your list from 10 to the top three candidates. This interview consists of five powerful screening interview questions. They work for any position for which you're hiring and can be addressed in 30 to 45 minutes over the phone or in a short meeting.
- Once you're down to the top three candidates, it's time for the Chronological In-Depth Structured (CIDS) interview — a thorough three- to four-hour interview covering a candidate's entire career history, with the objective of discovering behavioral and performance patterns that are likely to repeat themselves at your workplace. When hiring, bear in mind that past performance is the best indicator of future performance.
- A three- to four-hour interview is appropriate for a middle or senior leader; one to two hours might be more suitable for entry-level or less experienced candidates with limited work history.
- Checking for culture fit in the interview process can be handled in a variety of ways.

Test-Drive Potential Employees
- Though it's not always possible, the best way to select the right people is to have candidates work with you for several weeks.

5: THE MANAGERS Keeping and Growing (Educating) the Team

EXECUTIVE SUMMARY: Once you've hired your team members, it takes great managers to keep them happy and engaged. Failing to develop these managers throughout the organization can become a major growth barrier. Five critical activities distinguish great managers and the routines they use to educate their people. The word "coach," more accurately describes the role. Investments in training and coaching (vs. R& D and capital expenditures) provide you with the best returns available to your business.

- People join companies. They leave managers. Therefore, to keep your team happy and engaged, you need one thing above all else: great managers. And great managers are not just born; they are continually advancing their skills and those of their employees.
- Failure to develop sufficient leadership is one of the three biggest barriers to growth.

Keep Your Talent Engaged

- Google applied its data analytics capability, to bring the same level of rigor to People-decisions that it does to engineering challenges. What the data showed is that periodic one-on-one coaching (rather than superior technical knowledge) ranked as the #1 key to being a successful leader. From our experience, great managers must focus those coaching sessions with their "direct supports" (a better term than "direct reports") on five topics representing the five main activities of successful managers.
- Here are the five in reverse order:

  5. Hire fewer people, but pay them more. People will sacrifice certain perks to work with a firm with a worthy Purpose that's making a difference. Look to your Core Values, your business model, and your Brand Promise, and let them instruct you in the design of your compensation plan. Don't copy somebody else's system. Last, when it comes to the key people who absolutely drive performance, great managers simply do whatever it takes to keep them on board, including offering a customized compensation package.

  4. Give recognition, and show appreciation. Studies have shown that for people to be happy and productive at work, they need to experience positive interactions (appreciation, praise) vs. negative (reprimands, criticism) with their manager in a ratio of at least 3: 1. The way people want to receive recognition varies greatly. Great managers test different approaches and observe reactions until they find the triggers that work best with each of their people.

  3. Set clear expectations, and give employees a clear line of sight. Great managers explain how their people's work contributes to the greater objectives of the company and then help them align their individual priorities with those of the firm. Once people understand their role and contribution, great managers set clear and consistent expectations about the outcomes of their team's work. By defining the What and not the How, great managers give employees the autonomy to find their own way of achieving these goals. Feeling the liberty to figure things out for themselves and apply their own style is very important for people, since autonomy is one of three main drivers of human motivation.
  - Column 7 of the OPSP provides space to define for each quarter: 1. KPIs — Two to three key performance indicators that objectively signal people on whether they had a productive day or week. 2. Priorities — A handful for the next quarter needed to achieve

the Critical Number and improve on a KPI. 3. Critical Number — The main bottleneck that each employee or team must fix during the quarter.

2. **Don't demotivate; "dehassle."** The best managers are less concerned about motivating their people and more concerned about NOT demotivating them.

They consider it their job to prevent the hassles that block their team's performance. The #1 demotivator for talented people is having to work with B and C Players who slow them down and suck their energy. Fixing people issues for your team can also mean "firing" a client.

   o On the process side, focus on ways to make your team's job(s) easier — a great definition of an effective manager.

1. **Help people play to their strengths**.   A strength isn't just something you're good at; it's only a strength if it literally gives you strength, gives you energy. In turn, a weakness is something that, though you may be good at it, drains the life out of you.

   o A key function of great managers is helping individual employees refocus and prune their jobs over time so they focus more on activities that give them strength and less on activities that make them weak.

   o Embracing strengths-based management practices will bring you more fulfilled, happier, and engaged employees who will lift themselves and your organization to new levels of energy and performance.

Grow Your Talent

- In order to keep your company competitive and your people loyal, you must grow them through education and coaching. And this investment in people is the biggest single predictor of a company's ability to beat its direct competitors and the overall market.

Onboarding — Getting the First Impression Right

- One of the biggest opportunities to grow and align your people is when they first start working for you. Their initial weeks on the job represent a unique chance to create connection and deeply ingrain a company's DNA into new people. Yet few companies make proper use of this opportunity.
- Onboarding needs to be a celebration, not paperwork. It should create emotional connections between the new recruit and a maximum number of team members.

Formal Orientation

- To inculcate a new employee (bring her into the culture) properly, structure a formal orientation process. It's most effective when organized around doing real work while emphasizing the company's Values and Purpose.
- People are exceptionally positive, receptive, and willing to learn in this phase, and they experience deep attachment to whatever you expose them to.

All Growth Companies Are Training Companies

- The only way to grow a company is to grow the people first.
- Research shows that training and development increases loyalty.
- Focus first on your middle management. In most growth companies, they have the hardest jobs and are critical to employee engagement and retention, yet get the least preparation for it.

Online Learning

- Longstanding Gazelle clients take advantage of online learning as well.

Growing People through Coaching

- As Google's people analytics team discovered, one-on-one coaching is the #1 factor linked to great management.
- Coaching requires a rhythm of use to make it effective. Regularly scheduled one on one coaching conversations are helpful and can help replace the dreaded quarterly or annual performance review.
- Use these conversations to review individual KPIs, Priorities a, and Critical Numbers from column 7 of the OPSP at each meeting. Recognize good performance, analyze underperformance, and discuss activities needed to get back on track. Ask questions to put the focus on the process, rather than lamenting results. Also give feedback on adherence to Core values, and if necessary develop strategies to correct behavior. Timely feedback is the most effective. It is easier to digest and prevents the formation of bad habits.
- Last, in order to grow people, you must expose them to different experiences. Search for opportunities to refocus activities on areas that the person is naturally drawn to but at the same time represent a challenge.
- Make your coaching situational throughout the process.
- People are not resources that you consume. So rethink the name of the department that takes care of them. Call it Talent development, Human relations, People Support – anything but Human Resources.

SCALING UP STRATEGY

KEY QUESTION: Can you state your firm's strategy simply – and is it driving sustainable growth in revenue and gross margins?

- Articulating a clear and differentiated strategy, supported by a strong core culture that can deliver on the brand's promises, is the key for any company wanting to scale up.
- Sustainable top-line revenue growth and increasing gross margin dollars are the two key financial indicators.
- Customers beating a path to your door, dragging along everyone they know is another.
- In turn, if you don't have a killer strategy your company will face continuous price pressures as the market commoditizes your products and services.
- It's critical that the senior leadership team works on strategy every week, free from day-to-day firefighting.

6. THE CORE: Values, Purpose and Competencies

- EXECUTIVE SUMMARY: The Core bridges the People and Strategy discussions and examines the Core of the organization: its Values, Purpose and Competencies. A strong Core is the foundation for an effective strategy.
- Without a strong core, the organization risks instability from cultural challenges, loss of focus, disengagement, and lack of heart as it scales up. At the center of the organization the core consists of values, Purpose, and Competencies.
- This Core provides the link between People and Strategy in the 4 Decisions model. It is most critical once a company gets larger than 50 to 70 employees.
- These three foundational attributes of the company anchor the left side of the One Page Strategic Plan (OPSP). They represent the heart and soul of the organization.

The Core Values
- Core values are the rules and boundaries that define the company's culture and personality, and provide a "Should/Shouldn't" test for all the behaviors and decisions by everyone in the firm. It's especially important that top managers lead by example, making sure their behaviors and decisions align with the Values.

The Organization's personality
- Your company is a living, breathing organism with a distinct personality. It expresses its personality through its Values.

Discovering the Right Words
- Discerning the Core Values is a DISCOVERY process, not the creation of a wish list of nice-to-haves. Let the Values bake for a year testing their validity at the next several quarterly planning sessions. Are there examples of how you lived these values?
- Values listed should be phrases, not single words.
- Values aren't good or bad, they just are. The key is to articulate them accurately.
- Describe each Core Value with a phrase, defined in a sentence or tow, and then anchor it with a story detailing how an employee or a team lived that value.

The Core Purpose
- If the Core Values are the soul of the company, the core Purpose (some call it a mission) gives it heart. The purpose answers the ageless question "Why?" What does what we do matter, and what difference are we making in the world? Why would our customers or the world miss us if we weren't around?
- Research finds that if you ignite and capture their hearts, not just their heads, employees will give you 40% more discretionary effort.
- A powerful purpose tends to revolve around a single word or idea.
- This central word or idea is then expanded into a phrase or two, but is most easily remembered and acted upon when it has a single word or idea at its core.
- To discern this Purpose, gather a team together and begin by asking "What do we do?" Then ask "Why" several times (5 Whys) until you get to your version of "Save the world" and then back up a step.
- Most teams, when asked to determine a Purpose, often describe Brand Promises instead.
- Out of this single idea should emerge a "stump speech" that the CEO shares repeatedly, reminding everyone of the big picture and "why we do what we do."

The Core Competencies
- Understanding a company's inherent strengths is essential. A Core Competency has three attributes:
1. It's not easy for competitors to imitate
2. It can be reused widely for many products and markets.
3. It must contribute to the benefits the end customer experiences and the value of the product or service to customers.
- It's equally important for a company to understand what it is inherently incapable of doing, or its core weaknesses.
- Core Competencies provide boundaries for determining what product and service offerings you should pursue. They are also foundational in helping you determine how to differentiate the company in the marketplace,

- Once you articulate your Values, Purpose, and Competencies, put them to work in creating an engaged and focused team. This will direct massive action around the right activities.

Bringing Your Core Alive

Eight ways to reinforce your culture are:

1. **Storytelling** – stories provide the explanation for Core Values that might seem unusual or cryptic on their own.
2**. Recruitment and Selection**
   - Design your interview questions and assessments to test how candidates align with your Core values. Then rate candidates in terms of their personal alignment with each Core Value.
   - Shape your hiring processes around your Core values.
   - Hire for culture fit – this will improve retention and lower turnover.
3. **Onboarding Process** - A proper onboarding process makes new hires feel welcome and integrates them more quickly into the culture. The key is designing the process around the teaching of your Core Values and Purpose.
4. **Performance Appraisals and Handbooks**
   - Core Values should provide the framework on which you hang your performance appraisal system.
   - Organize your employee handbook into sections around each Core Value.
5. **Recognition and Rewards** – Organize your recognition and reward categories around your Core Values.
6. **Newsletters** – use a word or phrase from your Core Values to come up with a catchy title.
7. **Themes** – establish a rhythm that keeps the Core Values top-of-mind by repeating them.
8. **Everyday Reinforcement** (The most important Step) – Hiring managers who are engaged, every day, in reinforcing the company's value and Purpose through their decision-making is the most important routine of the eight.

7. The 7 Strata of Strategy

EXECUTIVE SUMMARY: This chapter guides you through a framework for constructing an industry-dominating plan. It integrates several of the best –known components of strategy into a single framework and provides an agenda for the strategic thinking team to create and maintain a competition-crushing, differentiated approach to a specific market.

- Without an effective strategy, you're going to spend the next several years executing a plan that is less than optimal and leaving a pile of money on the table. Worse, you'll keep the doors open for savvier competitors to swoop in and take over your industry.
- The idea is to use the 7 Strata worksheet to answer a series of strategic questions and plug some of the answers into the appropriate spaces on the OPSP. The questions will help you make key strategic decisions.
- Strategy is what a senior team should be spending the bulk of its time on – not fighting fires on a day-to-day basis which is best left to the middle managers.

Strategic Thinking Team – The Council

- It's helpful to think about *strategic thinking* and *execution planning*. The 7 Strata framework is one of the key tools guiding the strategic thinking agenda of the company.
- The first step in completing the 7 Strata and working through the 4Ps (Product, Place, Price and Promotion) or 4 Es (Experience, Everyplace, Exchange, and Evangelism) is designating a strategic thinking team. Select no more than three to five people to meet for an hour or so each week to discuss each of the Strata and other issues of strategic importance.

- It's all about iterations: making a few decisions, testing them, and coming back to the table the following week for discussion.
- Besides a few key members of the senior team, you might include someone with specific industry or domain knowledge underpinning your strategy.
- The council doesn't accomplish its work in isolation. The council members are expected to spend some time each week talking with customers and employees and checking out competitors, extracting insights and ideas to fuel their strategic thinking.
- In the end strategic decisions need to be made, and it's the job of the CEO to make them. Yet it's advisable to recruit several pairs of eyes (and to have frequent contact with the market to help you navigate.

The 7 Strata are:

Words You Own (mindshare)

- The key is owning words that matter – the ones people think about and use to search for your product and services.
- Take a moment to search the words or phrases you think you should own in the minds of your customers, and see how high your company ranks – or whether your lesser competitors are outranking you. Then go to the Google AdWords Keyword Planner to see how many times someone has searched for your target word or phrase. This tool will show you what related words are searched and with what frequency, both locally and globally. This will help you refine the words you choose to dominate.
- Hire writers and videographers to create case studies, white papers, and videos that naturally catch the attention of the search engines and media and educate the customers about the words you want to own. Videos and images have dominated over text ever since Google purchased You Tube.
- People don't want to be sold, they want to be educated.
- If you focus on only one of the 7 Strata, this first one is the most important in driving revenue. The rest help you defend your niche, simplify execution, and turn your revenue into huge profit.
- The key is picking a niche and owning (or creating) the words in the minds of the people you want as your core customers.

Sandbox and Brand Promises

- There are four key decisions to make on stratum 2:
1. Who /What/Where are your (juicy red) core customers? These are the customers from whom the business can mine the most profit over time. Once you know more specifically Who they are, it's much easier to know Where to find them.
2. What are you really selling them? The primary mistake companies make in describing What they sell is to focus on the benefits and features. All sales are emotional, initiated through the heart and then justified logically through the head.
3. What are your three Brand Promises? Most companies have three Brand Promises, with one promise that leads the list. The key is to define the company's Brand Promise quantitatively so they can be measured and monitored. Refrain from using the words "quality", "value", or "service" as brand Promises. E.g. McDonald's has defined its three measurable brand promises as speed, consistency, and fun for kids.
4. What methods do you use to measure whether you're keeping those promises? (Kept Promise Indicators, a play on KPIs.) A promise has no weight if you don't keep it, resulting in lost customers and negative word of mouth publicity. Thus it's critical that you know how to measure daily whether you're keeping your promises.

Brand promise Guarantee (Catalytic Mechanism)

- Called this because it needs to hurt when a brand promise is broken. The Brand Promise Guarantee also reduces customers' fear of buying from you.
- Professional service firms might offer "short pay" guarantees giving the client an option to pay whatever he thinks is reasonable if there are any issues.

One-PHRASE Strategy (Key to making Money)

- The first three strata are expensive to accomplish. This is why it's critical to identify your one-PHRASE Strategy. This phrase represents the key lever in your business model that drives profitability and helps you to choose which customer desires to meet and which to ignore.
- Great brands don't try to please everyone. They focus on being the absolute best at meeting the needs/wants of a small but fanatical group of customers, and then dare to be the absolute worst at everything else. In turn, competitors, in striving to be the best in everything for everyone, actually achieve greatness in nothing – and end up as just average players in the industry.

Differentiating Activities (3 to 5 Hows)

- Underpinning the One-Phrase Strategy is a set of specific actions that represent HOW you can execute your business differently from the competition. Competitors can pursue owning the same words, make the same Brand promises, and offer the same guarantees. However, it's HOW you deliver on your promises where differentiation occurs.
- A true differentiator can only be defined as something your competitor won't do or can't do without great effort or expense.
- The key is to choose HOW you go about delivering your products and services in your industry in ways that are nearly impossible for your competition to copy.

X-Factor (10X- 100X Underlying Advantage)

- A 10X -100X underlying competitive advantage, which is normally invisible to customers, is the edge that underpins strategic activities and blocks competition from even trying to copy. It typically addresses a huge, established choke point in an industry.
- To figure out an X Factor, start by asking: What is the one thing I hate most about my industry? What is driving me nuts? What is the choke point constraining the company? It could be a massive cost factor. It could be a massive time factor. The challenge is that you are often too close to the situation and as blind as everyone else to the real problems that have been accepted as industry norms.
- By focusing on the roadblocks challenging your industry and figuring out a 10X – 100X advantage, you'll have a huge leg up on the competition.

Profit per X (Economic Engine) and BHAG (10-25vYear Goals)

- These are the final two decisions to cap the strategy with a single overarching KPI.
- The Profit per X metric represents the underlying economic engine of the business and provides the leaders with a single KPI they can track maniacally to monitor the progress of the business.
- Though the numerator can be any metric you like – profit, revenue, or gross margin - the denominator is fixed and represents your company's unique approach to scaling the business. And it generally ties back to the One-PHRASE Strategy.

Big Hairy Audacious Goal (BHAG)
- This phrase was coined by Jim Collins and he placed the BHAG at the center of the Hedgehog Concept, noting that it must fully align with all the components of your strategy. This is why Gazelles made it the seventh and final stratum.
- Your BHAG should be measured in the same units as the X. The profit per X and the BHAG need to align very tightly. The BHAG must also align with the Purpose of the company.

7 Strata Summary
- The payoff is huge if you figure out all of the attributes of the 7 Strata. Nail down what you can and keep moving, Set up your strategic thinking team, have each member read (and master) one of the resources mentioned, and start testing your theories and honing your strategy to perfection. You'll know you're on the right track when sustained revenue growth and great margins start coming more easily.
- This is difficult work, so it is important to trust the process. Keep meeting every week and talking about the ideas and the answers will come to you.

8. THE ONE-PAGE STRATEGIC PLAN – The Tool for Strategic Planning

EXECUTIVE SUMMARY: The bigger your company, and the faster it's growing, the harder it is to keep everyone on the same page. The OPSP, used by more than 40,000 companies worldwide, is a simple yet powerful tool that helps you edit down your vision to a single, action-oriented page. The OPSP offers a way to track and drive business performance and brings better alignment, accountability, and execution.

Vision Summary
- The Vision Summary provides a simplified OPSP framework for companies just getting started with implementing the Rockefeller habits and for firms with 50 employees or fewer.
- For larger firms, the Vision Summary provides a one-page format to communicate key aspects of the company's vision to employees, customers, investors, and the broader community.
- Core Values, Purpose, Brand Promises and the BHAG are the strategic components of the Vision Summary. They represent the key components of the company's vision that every employee should know and understand thoroughly, making the summary useful as a key onboarding tool for new employees.
- The strategic components and the listed priorities provide a quick snapshot of the company's vision.

One-Page Strategic Plan (OPSP)
- A vision is a dream with a plan: a One-Page Strategic Plan. To flesh out the vision, you need to answer seven basic questions: who, what, when, where, how and why, and the often challenging question, But should we or shouldn't we?" These questions anchor the seven columns of the OPSP.

- The OPSP process provides the organization with:
  1. A **framework** that details your corporate vision.
  2. A common **language** with which to express that vision.
  3. A well developed **routine** for keeping the vision current.
- The OPSP is for internal consumption. It's designed to help a team get the technical aspect of the strategic plan correct vs. crafting marketing messages.

- To see how to fill in the OPSP refer to the summary of tools that accompanies this book summary.
- One of the keys to keeping people engaged is making a connection between their day to day efforts and the goals and vision of the company.
- The three main groups of People involved in any business are the employees, customers and shareholders. The goal is to continuously improve the company's Reputation with all three as you balance competing demands between each group.
- The three main processes that drive any business are Make/Buy, Sell, and Recordkeeping. The goal is to continually improve the company's Productivity in all three as you balance the potentially opposing demands between each process.
- The big challenge is balancing the competing demands among all six. You want to continually improve your processes to drive better results, but you don't want to greatly upset any of the groups of People as you do so.
- Maintaining this balance between the demands of the People and Process sides of the business, as you scale up your reputation and productivity requires frequent feedback and metrics.

Preparing for a Strategic Planning Session

- There are four main activities in preparing for a strategic planning session (quarterly or annual):
1. Managers at all levels gather feedback fro employees and customers. Send out a short Start/Stop/ Keep survey to all the employees and then ask the same three questions of your customers. Be sure to incorporate customer feedback into the process.
2. Middle management completes a SWOT analysis and submits a Top 3 Priority list. It's an excellent tool for gathering ideas and input from middle managers, who are more internally focused and closer to the day-to-day operations of an organization.
3. Senior leadership completes a SWT analysis and submits a Top 3 Priority list. The SWT is an updated approach that identifies inherent *Strengths and Weaknesses* within their firms while exploring broader external *Trends* beyond their own industry and geography. To anchor strategic thinking, senior leaders need to complete the SWT. It will help them face the brutal facts about the company's inherent strengths and weaknesses, and the global trends threatening their industry.
4. Everyone aims to keep learning and growing as a team.

Scaling Up Execution

KEY QUESTION: Are all processes running without drama and driving industry-leading profitability? This section is structured around the Rockefeller habits, divided into three disciplines (routines) fundamental to execution;
1. **Priorities:** less is more in driving focus and alignment.
2. **Data:** Qualitative and quantitative feedback provides clarity and foresight.
3. **Meeting Rhythm:** Give yourself the time to make better/faster decisions.

9. The Priority: Finish Lines, and Fun

EXECUTIVE SUMMARY: Individuals or organizations with too many priorities have n priorities and risk spinning their wheels and accomplishing nothing of significance. In turn, laser-focusing everyone

on a single priority- today, this week, this quarter, this year, and the next decade – creates clarity and power throughout the organization.

- The key to prioritizing is sequencing a series of #1 priorities that keep everyone focused and heading in the same general direction together.
- By sequencing these initiatives so they align and build on each other, you can tackle the hundreds of decisions and activities that need to be addressed without overwhelming and defocusing the team.

The Rockefeller Habits Checklist

- The checklist consists of 10 routines and is an execution checklist. By accomplishing the items on the list you will save time and make more money. You can't implement any of what is taught in this book unless Rockefeller Habit #1 – "The executive team is healthy and aligned" – exists. The order in which you implement the other habits doesn't matter. Choose just one or two each quarter, based on what will give you the most immediate benefit.

Rockefeller Habit #1 – Healthy Team

- Take your team through Patrick l
- Lencioni's Five Dysfunctions of a Team Assessment and training process to strengthen the levels of trust, debate, commitment, accountability and results. It's a great tune up for even healthy teams.
- Many of the Rockefeller Habits reinforce routines that keep the team healthy, like taking a few minutes to share personal and professional good news at the start of a weekly or monthly meeting.
- Once the team is healthy, then it is ready to tackle the tough work of setting priorities successfully.

Rockefeller Habit #2 – The #1 Priority

- The BHAG, derived from your strategy, is the main long-term priority anchoring the *strategic thinking* in the vision. The quarterly or annual Critical Number is the main short-term priority anchoring the *execution planning* side*.*
- Rockefeller Habit #2 starts with identifying this Critical Number. Find the one initiative that, when pursued, makes it easier to accomplish anything else. Or identify the bottleneck or choke point and address it first.
- Quarterly Themes – This I a fun motif you can use in your internal marketing to rally everyone around achieving your Critical Numbers.
- If, in the middle of a Quarterly Theme or an annual one, you feel the team is going to miss the Critical Number, you have three options:
1. Repeat the Critical Number in the next quarter if it's still crucial that the organization achieve the target.
2. Move on to another Critical Number if you sense that enough momentum was created with the previous target to keep the organization trending in the right direction.
3. Do a root cause analysis to uncover the reasons your organization didn't achieve your Critical Number. Choose one of those reasons to fix in the next quarter.
- It isn't uncommon for teams to fall short f their goals in the beginning. Don't change the goals.
- Having three potential targets – Super Green, Green and Red – ups the odds that the team will earn a medal. Even if you don't hit the minimum goal, convene the team for an event to announce the results.
- As the company matures in the use of quarterly and annual themes, you can dial up the rewards.

- The Critical Number, like the rest of the organization's strategy, cannot be set in isolation from the realities of the company and the marketplace.
- Theme Creation and Celebration
- Delegate the actual creation of the theme to a nonexecutive team. Almost every company has a team member who is skilled in using a computer to create videos, posters, and other themed collateral. The senior team doesn't need another job, and it's best if an employee –run team drives the theme activities.
- At the celebration, ask the most powerful question a leader can pose when a team has successfully completed anything: "How did you do it?"
- Nothing builds momentum and energy like having specific targets.

Rockefeller Habit # 3 – meeting Rhythm (discussed later)

Rockefeller Habit #4 – Every facet of the organization has a person (one) assigned with accountability for ensuring goals are met. (Already covered)

Rockefeller Habit #7 – Core Values and Purpose are "alive" in the organization. (Already covered)

Rockefeller Habit #8 – Employees can articulate the key components of the company's strategy accurately. (Already covered)

10. THE DATA -Powering Prediction

EXECUTIVE SUMMARY – The fundamental job of a leader is prediction. And at the heart of a leader's ability to predict is data. Big data analysis has become mainstream and within reach of companies of all sizes. Yet leaders also need plain old human-gathered intelligenc3 to get a gut feel for the market and what is happening in the company, so that they can make the right decisions. Talking weekly with customers and employees and then discussing what's been learned at the executive huddle is critical. And engaging all of your employees in data collection, with is middle-management team leading them, spreads out the work so the senior team doesn't get buried.

Big Data
The way in which businesses use data to make decisions, to predict, is undergoing a radical change since the beginning of commerce.

Intelligence Gathering
- Data analysis must be augmented with plain old human intelligence-gathering.
- Two lessons:
- Senior leaders need to be in the market 80% of the week, either figuratively or literally.
- This routine must start on day one and continue through half a trillion in revenue (Wal-Mart).

Metrics Everywhere
- Gazelle's growth Tools are replete with requests to pick KPIs etc. The challenge is choosing metrics that matter, meaning those that measure what's important to customers, and provide sufficient insight to help both the leadership team and all employees see problems and opportunities in time to react.
- Quantitative metrics alone provide an incomplete view. Qualitative insights from conversations wit the market and observations of customers and competitors fill out the data set needed to guide decisions. Input from advisors, experts, and "the crowd" also contribute. Piling all this

data into computers and our brains engaging in healthy, frequent debate helps leaders make decisions regarding hiring, product, marketing, etc., with a high degree of confidence.

Rockefeller Habit #5: Gather Employee Input
- Bring every brain into the game. Without a formal routine to prompt members of your team to share their experiences, you risk those ideas walk out the door at the end of the day. Worse yet, your workers miss an opportunity to contribute and feel good about it.
- At a minimum, all executives (and middle managers) should have a Start/Stop/ Keep conversation with at least one employee weekly. (What should we start doing, stop doing, keep dong). Choose employees who work directly with customers and those newest to the company. Recent hires will have fresh eyes that lead them to notice things longer-term employees have come to accept.
- Pay particular attention to the "stop-doing" responses.
- If you plan to act on any concrete "start" or "stop" ideas, feed them into a more formal employee suggestion process.
- Collect weekly input from employees about obstacles and opportunities. Ask employees to submit suggestions to increase revenue reduce costs, make something easier/better for the customers or employees.
- Gathering employees' feedback and ideas will backfire on the company if management doesn't close the loop and act on their suggestions. At a minimum, let an employee know why an idea can't be implemented.
- Hold a middle management team accountable for responding to employees' feedback on all obstacles and opportunities.
- Track the number of days it takes to implement the ideas gathered from your employees.
- Last, be transparent with employees. Publish updates in internal newsletters.

Rockefeller Habit #6: Gather Customer Input

Conversations with Customers
- Gazelles implore all executives and middle managers to have 4 Questions (4Q) conversation with at least one end user weekly. These questions are asked in person – not by survey:
- How are you doing – offers insight into pain points and priorities as well as what their bonus may be tied to. Show how your products and services can help them reach their target.
- What's going on in your industry/neighborhood? This question offers insight into trends.
- What do you hear about our competitors? This is the most important question because it can help you cut through your own biases.
- How are we doing? This is asked only after the other questions as the conversation is about them.
- Look at these efforts as an investment in customer retention. If companies were able to hold on to the customers they now lose from neglect, it would fuel half of their growth.

Discuss at the Weekly Meeting
- Share insights from conversations with customers at the executive team's weekly huddle. As much as 20% of the weekly meeting should focus on customer feedback.

Involve All Employees (Especially Salespeople)
- Whichever competitor has the most market intelligence, and uses it, wins.
- It's particularly important to encourage all your salespeople, distributors, and independent reps (in all of your sales channels) to gather and report market intelligence.

- Require all of them to call in daily to a voice mailbox and leave a three-minute update on any positive sales result. Ask them to provide feedback from customers and about competitors and report on barriers they are facing in making sales. Written reports won't happen.

Net Promoter Scores
- The NPS measures the net percentage of your customers who are actively spreading the good word about your company. The NPS question: "Would you recommend us to a friend?"

Rockefeller Habit #9: KPIs for Everyone
- Each team and person needs individual quarterly goals that align with the plan. This creates "line of sight", so every employee feels connected to the vision and direction of the company.
- Every member of the team needs to be able to answer objectively the question, "Did I have a great day or week?" the key: Each person must report on *one or two KPIs weekly.*
- You will succeed only if every team member in your company looks at posted information and makes adjustments or decisions based on their KPIs weekly.

One Critical Number and 3 to 5 Rocks
- The magic of the Scaling Up process is getting everyone in the company to accomplish one additional thing that is aligned with the company's focus every 90 days. (i.e. each employee has one Critical Number that aligns with the company's Critical Number for the quarter, illustrating that there is a clear line of sight.
- Like the company, all employees or teams need to set a handful of priorities (known as rocks) that will help them achieve their Critical Number (i.e. each individual/team should have three to five rocks that align with those of the company.)

Peer Coach
- All executives and middle managers should have a coach (or peer coach) holding them accountable for behavioral changes. An external coach is best – to lead quarterly and annual planning sessions, and check in monthly to monitor progress.
- Everyone should find a peer coach internally too. Choose five behaviors or actions you need to start or stop, and then report your progress to your peer coach.

Rockefeller Habit #10: Scoreboards Everywhere
- We can all take a page from sports facilities where no matter where you sit you can see the score. The real-time digital scoreboards should be the standards by which we monitor our own company performance.
- At a minimum, have your metrics, goals, and plans up big and visible in a place where you host the various weekly meetings (i.e. establish a "situation room" for weekly meetings, whether they're physical or virtual. In the case of a virtual meeting, the "room" might be a particular conference line).
- Make sure the *Core Values, Purpose, and Priorities are posted throughout the company.*

Accountability Management Systems
- At some point, when the company is bigger than 50 employees and expanding into multiple locations, it's important to have a system in place for tracking and managing the cascading Priorities and KPIs. (Gazelles offers Align).
- The end goal is to keep the output from the Growth Tools top-of-mind.
- Meeting rhythms give everyone a routine through which all the input data, and metrics can be discussed and debated, and decisions can be made.

11. THE MEETING RHYTHM: The Heartbeat of the Organization

EXECUTIVE SUMMARY: To move faster, pulse faster. At the heart of a team's performance is a rhythm of well-run daily, weekly, quarterly, and annual meetings. These meetings bring focus and alignment, provide an opportunity to solve problems more quickly, and ultimately save time. They also address the #1 challenge people face when they work together: communications.

- It is a rhythm of communication that drives alignment throughout the organization. Regular meetings act as placeholders in everyone's calendar.
- This rhythm of meetings shouldn't require more than 10% of a standard workweek for senior leadership, 5% to 7% for middle managers, and 3% for frontline staff. This rhythm is sufficient to manage the business.

More Frequent Meetings

- Many companies have quarterly and annual meetings. IN Gazelles' methodology, the key agenda for these meetings is updating the Growth Tools, including the OPSP.
- Having more frequent routines makes it easier to attain goals. This is why the daily, weekly, and monthly meetings are critical. They drive the deliverables outlined in the less frequent meetings, with each meeting building on the next.
- Plus, teams need regular, face-to-face huddles to discuss new opportunities, strategic concerns, and bottle necks as they arise.
- The faster you're growing the faster your meetings should pulse.

Three Powerful Advantages to Meeting Regularly

- The two main arguments for not meeting regularly, especially for the daily huddle:
  1. We don't have the time
  2. We see each other all day anyway
- To address the times issue: If your meetings follow our agenda, they save time. Because everyone is together in a daily meeting, things get communicated quickly and accurately.
- As for the second point: Bumping into each other all day doesn't substitute for tightly focused team discussions. Casual encounters fail to take advantage of the three most powerful tools a leaders has in getting team performance.
- Peer pressure
- Collective intelligence
- Clear communication
- By holding one –on-one conversations with their team members in lieu of a weekly meeting, leaders lose these advantages.
- Meeting in a group, takes the heat off the leader and creates peer pressure that increases the rate of deliverables.
- Last, holding a team meeting means that everyone is hearing the same information. You don't have to repeat the same message three or four times in one-on-ones or casual conversations.

Rockefeller Habit #3: Meeting Rhythm

- This rhythm of meetings is designed to support cascading communication around the priorities and metrics-driving strategy. Specifically:
- **The daily huddle**. A 5-15 minute meeting to discuss tactical issues and provide updates. This will help you avoid minor train wrecks and to take quick advantage of unforeseen opportunities. Normally, a daily huddle saves everyone an hour or so of needless email updates and ad hoc interruptions. Issues that emerge drive the main topics for the weekly meeting.
- **The weekly meeting**. A 60 to 90 minute discussion to review progress on the quarterly priorities and tap the collective brainpower of the team in addressing one or two main topics.

This meeting also provides a time to discuss the market intelligence gathered that week from customers, employees, and competitors. Repeated patterns of discussion determine the one or two main issues for the monthly meeting.

- **The monthly management meeting**. A half to full day meeting, in which all senior, middle-management. And frontline managers come together to learn and collaboratively address one or two big issues requiring several hours of effort. It's also designed to transfer (DNA (knowledge, values, approach) from upper to middle management.
- **The quarterly and annual meetings**. At this one to three day offsite meeting, leaders update the Growth Tools and establish the next quarterly and/or/annual theme. Once each quarter, the leadership team shares an update of the new plans with all employees in a 45-minute meeting.

- Note that the more frequent gatherings draw context and continuity from the longer and more strategic planning sessions.

What Kills the Daily – and Most – meetings?
- In a word, generalities! As teams tell stories and share information, it's critical that they include specifics. We need to hear names, numbers, dates, issues, and concerns if our brain is going to make the kind of connections that make this process powerful.

- *Timing* – Set the start of the daily huddle at an odd time (like 8:08). People are more likely to be on time. Start the meeting on time, whether everyone is present or not. End on time. Plan 1 minute per person. Choose whatever time best fits the rhythm of the business.
- *Setting* – Stand up – it'll help to keep the meeting short.
- *Who Attends* – the general rule is to have more people in fewer meetings, rather than fewer people in more meetings. In general, frontline employees will be in only one daily huddle, and anyone in management will be in two: one with their direct reports and one with their peers and leader.
- *Who Runs the Meeting* – Pick someone who is naturally structured and disciplined to keep meetings running on time. Suggest "take it offline: whenever people get off on a tangent that doesn't require everybody's attention.
- *The Agenda* – The agenda should be the same every days and it's just three items long, with five minutes maximum per item:
  1. *What's up (in the next 24hous)?* Be very specific. The idea is to let people detect conflicts, crossed agendas, and missed opportunities immediately. These updates should relate to key activities, meetings, decisions etc. NOT a recitation of someone's daily schedule.
  2. *What are the daily metrics?* You are looking for patterns and trends. Since it generally takes six data points to constitute a trend, it's going to take months to see patterns if you look at metrics only every 30 days.
  3. *Where are you stuck?* This is the most important agenda item. You want members to bring up constraints and concerns that would prevent them from having a great next 24 hours. The brutal facts need to be shares, and the leader needs to see a pattern of "stucks" to understand what underlying issues must be addressed. Verbalizing is the first step in solving problems, because until the mouth starts moving, the brain won't engage. Second, you want to focus your team's energy on breaking through constraints. The only people who don't get stuck are those who aren't doing anything or are so stuck that they don't know it.
- Avoid checking on whether someone did something the previous day as team members will feel micro-managed.

The Weekly Meeting

- If the daily huddles are functioning well, they will lead to immediate action on scores of issues that would otherwise clog up the weekly meeting.
- The idea of the weekly meeting is to keep everyone focused on the #1 priority – the big rocks supporting that mission.
- You want to tap the collective intelligence of the team for 30 to 60 minutes on one or tow important topics. This affords the group an opportunity to resolve 50 to 100 important things in a year.
- Pick one morning or afternoon and host ALL of your functional and project meetings back to back. This allows everyone to get in a meeting mindset and flow, and frees senior management to spend the rest of the week out in the marketplace.

- *The Schedule* – Schedule the meeting for the same time, same place each week. Set aside 30 minutes for frontline employees, 60 to 90minutes for middle and executive teams.

Suggested Agenda

- **5 to 7 minutes** • Good News - Have everyone share a SPECIFIC personal and business good news story, from the past week. This is a way to counter the negativity of these meetings, since they are mainly focused on addressing challenges, and helps people begin to see the good, not just the bad. It's also a great way to get to know each other better and to give each other a pat on the back. This may feel awkward at first, but it's important that everyone participates.
- **2 to 5 minutes** • Who/What/When Review - The leader should go over the list and confirm the completion of the accountability items. If something is not completed a new date is selected or, if no longer relevant, the item is removed. The Who/What/When is always done as a team to show the team who is living up to their commitments.
- **5 to 10 minutes** • The Numbers - Go over individual or team weekly measures of productivity. Don't get hung-up in conversation. Just report the numbers. You will see trends in the data better if every team graphs their weekly measurements and shares them in the meeting. The numbers come from your individual goal metrics, the quarterly goals, the Profit X numbers and any other critical business number the management team is monitoring.
- **10 minutes** • Customer & Employee Feedback - Go over the Hassle Logs. Again, don't get hung up in conversation, instead, look for recurring issues or concerns that the team or its customers are facing day in and day out. Choose one issue, get to the root cause, and assign a person or small group to explore it.
- **10 to 30 minutes** • A Rock, or Single Issue – A big mistake made at weekly meetings is covering everything every week. As a result, the team deals with issues on a shallow level and never focuses its collective intelligence for a period of time on one issue. The key is focusing on a large priority for the quarter, the ROCKS for the quarter. Make sure to assign the accountabilities on the Who/What/When.
- **2 to 5 minutes** • Who/What/When Review - The leader confirms and summarizes the Who/What/When commitments made by each participants in the meeting and all the commitments due in the next week.
- **One Phrase Closes** Take turns having everyone say a word or phrase that represents how they feel at that moment about the meeting.

Weekly CEO One-Pager

- Many CEOs also send out a weekly one-pager to all employees updating them on the status of the #1 Priority and other significant developments inside the company and the industry.

Employees want to hear from their top leader and appreciate the sense of being on the inside provided by this kind of report.

The Monthly Management Meeting

- Unless the senior team instills its DNA (knowledge and values to make a good decision) in everyone from the middle managers on down, the top leaders will find themselves increasingly overwhelmed by the demands of a growing business.
- Doing this requires one simple routine: a well-structured, one day monthly management meeting that includes everyone who supervises or manages anyone in the business. It should be a day focused on learning, sharing, and problem solving vs. a day of mind-numbing reports.
- The monthly meeting is a time to really dive into a specific strategic company problem or issue. Generally it is a rock that was identified on our one page strategic plan in the quarterly session. The start of the meeting is similar to a weekly meeting but is followed by a more in-depth conversation of where you are with each of your quarterly rocks and objectives. The people presenting their rocks should be well prepared for presenting a 60 to 90 minutes presentation in the meeting.
- Don't forget the **WHO/WHAT/WHEN** sheet for the meeting, you are not there to chit chat but to effectively run the meeting and assign accountability to resolve rocks and get results.

Suggested Agenda

- **5 to 10 minutes** • Good News - Have everyone share a SPECIFIC personal and business good news story, from the past week.

- **5 to 10 minutes** • The Numbers - Go over individual or team weekly measures of productivity. Don't get hung-up in conversation. Just report the numbers. Graphing the weekly measurements will assist the Team to see trends in the data.

- **5 minutes** • Quickly go over the WHO/WHAT/WHEN from the previous meeting and check items off the list.

- **10 minutes** • Customer & Employee Data - Go over the Hassle Logs. Don't get hung up in conversation. Just look for any recurring issues or concerns that the team or its customers are facing day in and day out. Choose **one** issue, get to the root cause, and assign a person or small group to explore it. Don't forget the WHO/WHAT/WHEN.

- **30 minutes** • Review of One Page - Go over the quarterly section of the one page strategic plan and review the details of each of the key performance indicators. Each person will report on their rock and the CEO will give a report on where the organization is as a whole.

- **60 to 90 minutes** • Review a Rock. If someone is in the red or close to it they need to give a detailed analysis of what they have done to move the rock and why they are stuck. The person in charge of the rock should then brainstorm with the group to overcome the challenges they're facing. This is an open forum to discuss the fine details of everything done to date and what actions need to be taken to overcome the barrier.

- **60 to 90 minutes** • Review a Rock II. Same as last item.

- **5 minutes** • Quickly go over the WHO/WHAT/WHEN additions from this meeting and reconfirm the commitments in WHO/WHAT/WHEN format.

- **60 minutes** • Learning - Review a book by having, a leader present a new procedure or have a Team member share a class they've attended. This is an opportunity for learning.

- **One Phrase Closes** Go around the room and ask everyone to say a word or phrase that represents how they feel at that moment about the meeting.

- **This is a 3 to 4 hour meeting,** if effective.

Monthly Town Hall
- In addition to the weekly CREO one –pager, many top leaders host a monthly town hall meeting, at which they make a few key announcements and give employees an opportunity to ask questions and discuss issues important to them.
- One of the biggest mistakes a CEO can make, in the spirit of transparency and openness, is to share important changes and improvements with all the employees before briefing the middle managers.

Quarterly and Annual Planning Meetings
- The main agenda for these one to three day offsite planning sessions is to work through and update the Growth Tools. They provide the questions, focus, and agenda for these quarterly and annual planning sessions.

SCALING UP CASH
- KEY QUESTION: Do you have consistent sources of cash. Ideally generated internally, to fund the growth of your business?
- You can get by with decent People, Strategy, and Execution, but not a day without Cash. Cash becomes even more critical as the business scales up, since "growth sucks cash." The key is innovating ways to generate sufficient profits and cash flow internally, so you don't have to turn to banks (or sharks!) to fuel your growth.
- Great companies, by choice, keep three to ten times more cash reserves than their competitors. That allows growth firms to weather the storms.

12. THE CASH: Accelerating Cash Flow
EXECUTIVE SUMMARY: Cash is the oxygen that fuels growth. The cash conversion cycle (CCC) is a key performance indicator (KPI) that measures how long it takes for a dollar spent on anything (rent, utilities, marketing, payroll, etc.) to make its way through your business and back into your pocket. Brainstorm ways to improve cash flow at each 90 day planning session and pick related initiatives as one of your handful of priorities each quarter. Constantly improving the cash flow of the company, and better understanding how cash moves through business, is a powerful driver for improving the firm as a whole.

Cash Conversion Cycle (CCC)
- Improving the CCC is a matter of looking for ways to improve it. E.g. billing more often.

Cash Acceleration Strategies (CASh)
- Gazelles created a one page tool called Cash Acceleration Strategies (CASh) which breaks down the CCC into four main components: Sales Cycle, delivery Cycle, make/Production and inventory Cycle and Billing & Payment Cycle.

- Most businesses will have some aspect of each of these cash cycle components. What might differ is the sequence of these components, with some cycles overlapping others or occurring in a different order.
- Management teams should set aside an hour or more each month to brainstorm ways to improve each of these cash cycle components. This is a powerful exercise to do with the broader middle-management team at a half-to-full-day monthly management meeting. It will give everyone a better understanding of how cash flows through the business and how each function can contribute positively.
- Some areas of opportunity:
  - Have your available cash reported daily
  - Ask to be paid sooner
  - Give value back to customers who pay on time or in advance
  - Get your invoices out more quickly
  - Send friendly reminders 5 days before payments are due
  - If invoices are recurring get credit card authorizations
  - Understand why clients are paying late
  - Understand each customer's paying cycles
  - Pay many of your own expenses with a credit card
  - Help your customers improve their cash flow
  - Improve margins and profit

- Almost all of these ideas fall into three general categories where you can make improvements:
  1. Shorten sales cycles
  2. Eliminate mistakes
  3. Change the business model

13. THE ACCOUNTING: Driving Profitability
EXECUTIVE SUMMARY: Accounting can help leaders anticipate problems, grow a business profitably, and drive valuation.

Accounting: Underappreciated
- If the #1 weakness of growth companies is marketing, the #2 problem is accounting. Accounting is often underappreciated. It is seen as a necessary evil to keep the tax collectors at bay; invoice, collect and pay bills; and provide monthly accounting statements – which often receive a cursory glance at the bottom line of the P & L.
- Accounting is often underfunded as a result. Hiring just one more person to either support the CFO or carry some of this executive's workload enables him or her to provide the following:
  1. Better cash and cash flow management
  2. Waterfall graphs, to share more granular accounting data for better decision-making
  3. Trend analysis and earl-warning systems to support better predictions

Waterfall Graphs
- A key accounting activity is to slice and dice a company's financial data as granularly as possible. This allows the team to view the gross margin, profit, and cash flow by categories, such as individual customers, location product lines etc.,
- This kind of data allows leadership to eliminate consistently unprofitable items.

Trend Analysis

- A fundamental responsibility of leasers is prediction, and they need both frequent quantitative data and qualitative feedback from the market to make the right calls. Any data older than a week is old.
- The accounting function is critical in this regard. It should provide the kinds of reports and graphs that help the leadership team see into the future.

Two Sets of Books

- One set of accounting books is needed to satisfy the rules of the Financial Accounting Standards Board (FASB) and the tax authorities. However, rarely should you make business decisions solely on these regulations.
- The key is to decide on the practices and rules by which you want the company to run, and have accounting align your internal books in support.

Simple Numbers

- Greg Crabtree's Simple Numbers process focuses on four key areas to running a wealth – building business

Clear the Distortions

- If a company generates less than $20 million a year in revenue, then compensation and distributions to the owners can distort the true picture of profitability.
- The next major accounting distortion is centered around revenue. Focus instead on a redefined version of gross margin. Calculate gross margin to be the revenue minus all NONLABOR direct costs. This definition of gross margin gives you the true economic top line of the business. The focus is more on gross margin dollars than gross margin as a percentage. Gross margin is THE most powerful indicator of an effective sales team, a differentiated strategy, and real growth. Since gross margin dollars more accurately measure sales performance, you should never base sales compensation on revenue unless your cost of goods sold does not vary from sale to sale. You will be paying commission on revenue while allowing your salespeople to set the price.

Set Appropriate profit targets

- The first decision is whether to define profit as a percentage of revenue or gross margin. As a general rule, once your gross margin percentage gets beyond 40% you should relate profit to gross margin. Lower margin businesses must sell a significant volume of other people's products and services to succeed.

Use Labor Efficiency to Drive Profitability

- The number 1 driver of profitability, labor efficiency, a measure of the productivity of each dollar spent on labor. View labor as something you can leverage. You just need to know the multiplier. The theory is that as long as you can keep applying productive labor at the right multiple, the only bottleneck is lacking enough of the right people to keep growing. The three segments of labor efficiency to focus on are:
  1. *Direct labor efficiency*: gross margin dollars divided by direct labor cost
  2. *Sales labor efficiency*: contribution margin dollars divided by sales labor cost
  3. *Management labor efficiency*: contribution margin divided by management labor cost

Understand the 4 Forces of Cash Flow

- Once a company is on the road to 15% profitability as defined by the Simple Numbers formula, it faces additional cash flow challenges.

- **Force #1: taxes**. Know how much you owe in taxes throughout the year t avoid the annual tax day surprise. True wealth is created only with after-tax dollars.
- **Force #2 Manage Debt**: debt is not your friend. If not managed properly, debt will enslave your business and keep it from reaching its full potential. Eliminate your debt or your line of credit and remain current on any term loans.
- **Force #3 Core Capital Target:** meeting your Core Capital Target means having two months of operating expenses in cash, after setting aside money to pay taxes and a
- **Force #4: Harvest Profits by Paying Dividends**. Once you have set aside taxes, paid off your line of credit, and met your core capital target, you can safely take your after-tax profits in the form of a distribution or bonuses to employees, assuming you have nothing drawn on your line of credit. If you run a business bat 10% profit that has hit its core capital target, you now have a business that is producing a MINIMUM return on equity of 50% PER YEAR!

14. THE POWER OF ONE: 7 Key Financial Levers

EXECUTIVE SUMMARY; the income statement often receives more attention than the cash flow statement. By giving the cash flow statement a little more consideration, and tweaking 7 key financial levers, a company can grow considerably faster using its own internally generated can, then by raising or borrowing external capital. The Power of One refers to the benefit in cash flow if a 1% or one day change is made to each of the 7 levers that affect it.

Profit vs. Cash
- What is more important, profit or cash? If you're a growing business, it's cash.
- A healthy profit and loss statement can mask pending cash-flow issues that will only get worse as the business continues to scale. It is therefore imperative that you understand your business from the perspective of bankers and investors.
- The only indisputable facts in any set of financials are the numbers that relate to cash. Your profit is an opinion, and data can be manipulated to provide a specific outcome. Your balance sheet is for the most part also an opinion. You can amend valuations to produce a desired result. Only your cash and debt balances are facts. Banks recognize this and use these umbers to determine your performance.
- Most business use the term to describe a general availability of cash. To a banker, cash flow has a specific value. It is a ration that describes management competence. And that competence begins with the business owner understanding the information to stay in control of their business.
- Cash flow is the change in cash and debt balances across a given period.
- There are only two uses for cash flow:
  1. Cash is used to invest in growth, or
  2. Cash is used to fund management influences waste.

Measuring Financial Success
- We are focusing here on two measures of financial success:
  1. Cash flow
  2. Returns
- The following is arguably the most useful ratio for measuring management effectiveness. The ratio brings into consideration both the P & L of the business (which provides the EBIT) and the balance sheet.

$$\text{EBIT/net operating assets} = \text{return on net assets}$$
$$(\text{EBIT} = \text{earnings before interest and taxes})$$

Operational Efficiency and Sales Effectiveness

- The beauty of the DuPont Formula is that it measures both the operational efficiency and the sales effectiveness of the company.

$$\frac{\text{EBIT}}{\text{Revenue}} \quad X \quad \frac{\text{Revenue}}{\text{Net Operating Assets}} = \text{return on net assets}$$

- The EBIT/revenue ration is a measure of P & L efficiency (i.e. how much profit is produced from every $1 of revenue). This translates into a measure of how effectively you're operating and tells you if you are squeezing the most profit from every dollar of revenue.
- In turn, the Revenue/ Net operating ratio is a measure of balance sheet effectiveness known as asset turnover. It is also a key indicator of sales effectiveness – telling you how much revenue the business can generate from the least amount of assets or investment.
- As these equations show, business leaders who ignore this information are missing a major determinant of how successful they are and where opportunities for improvement might be.

Minimum Return on Assets

- To keep it simple, midsize businesses should target at a minimum 30% return on net assets. If you are not achieving this, you should consider whether the EBIT you are producing from revenue generated is sufficient, or whether the business is producing enough revenue for the assets being deployed. If not, your investors might be better off investing their money elsewhere.

Return on Net Assets

- As a business owner you should also consider that equity is the most expensive source of funding and that it is usually cheaper to source debt financing.

Your Return is a Measure of Your Strategy

- If your return is not at the appropriate level, you need strategies that focus performance where you are increasing EBIT faster than you are growing net assets and consequently, are growing returns.

The 4 Drivers

- It is possible to measure success using ratios that measure returns, yet as a manager, you can't change returns directly. You need to modify aspects of the business – the drivers if you will, in order to change your returns.
- There are 4 financial drivers and they inform the bank and investors.

Driver #1: Profitability

- The first place to focus in improving cash is increasing profitability

Driver #2: Working Capital Management.

- Working capital is the amount of cash that your business requires to trade, and is generally consumed by two major current assets: your debtors (AR) and your inventory.
- Your trade creditors will fund some of this, so we always subtract AP from the other two figures when calculating working capital requirements.
- Working capital items are measured in days, to represent your current trading terms and requirements.

- Because your working capital requires cash, banks will often calculate one additional working capital required by the business and is calculated as (AR + Inventory – AP)/sales X 100.

Driver #3 Noncurrent Asset Management
- Together, the key drivers measure the rest of a balance sheet's performance. The results are propelled by success in actively managing and improving the measures identified in driver #1 1nd #2.

Driver #4 Cash Flow/Funding
- This driver helps predict the likelihood that you'll be able t o pay bankers and investors back.

Marginal Cash Flow
- This ratio calculates the amount of cash retained by the business's working capital machine and compares it to the amount of cash the business produces at the gross margin level.
- Our final cash flow measure highlights in simple terms the key difference between profit and cash flow. Operating cash flow reflects the impact of movements in your working capital on your earnings before interest, taxes, depreciation, and amortization (EBITDA) over a certain period. Bankers use this measure to calculate your debt service capacity. You should be using it as your means to increase cash for growth, distributions, and other advantages that a cashed-up business will provide

The Power of One and the 7 Levers
- Managers adjust the 4 drivers by tweaking the t main financial levers available to them to improve cash and returns in the business. There are benefits to cash if either a 1% or one-day change is made to each of these levers.
  1. **Price:** You can increase the price of your goods and services.
  2. **Volume:** You can sell more units at the same price.
  3. **Cost of Goods sold (COGS)/direct costs**: You can reduce the price you pay for your raw materials and direct labor.
  4. **Operating expenses:** You can reduce your operating costs.
  5. **Accounts receivable:** You can collect from your debtors faster.
  6. **Inventory/work in progress;** You can reduce the amount of stock you have on hand.
  7. **Accounts payable:** You can slow down the payment of creditors.

- In reality improving all the drivers isn't feasible. This is where management should start to set specific goals: combinations and increments of the 1% and one-day changes that are actually achievable.

- **Recommendation:** This is a rare book that not only addresses the core elements of running a successful business but also has the specific "how to" information necessary to put these critical ideas into action. Of course, to maximize your success, engage and be guided by a Gazelle coach!

For more summaries like this Contact Dr. Frumi at 949-394-9201
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About the reviewer: Frumi Rachel Barr, MBA, PhD
Dr. Frumi is known as "Dr Why" and "The CEO's Secret Weapon" and has long been an advisor to CEOs and their teams.

Do you ever wonder why some companies explode and grow while others just limp along?
The difference is in the disciplines and metrics they persistently focus on.

Scaling 4 Growth supports companies determined to accelerate their growth. We guide them through executing their strategies by infusing these disciplines into how they do things every day. And most importantly, we assist them to grow without "growing broke".

Dr Barr is the author of a ***CEO's Secret Weapon: How to Accelerate Success***. The book was ranked top business book of 2012 by ExecRank and has a forward by her colleague Simon Sinek, international author of best-selling ***Start with Why***.