PRACTICE FORUM

Top executive audits: strategic reviews of operational activities

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Abstract

Purpose – The paper explores the involvement of top management in strategic reviews of the organization's operational activities (known as top executive audits or TEAs). These are discussed in relation to strategy process and business excellence.

Design/methodology/approach – The case of Nissan South Africa (NSA) is used to illustrate their importance and their relation to *hoshin kanri* (policy deployment) practice.

Findings – The paper argues that TEAs are a very important and integrative aspect of the holistic management of the organization. TEAs are also crucial to *hoshin kanri* and facilitate operational effectiveness.

Originality/value – The paper suggests that strategic reviews, such as TEAs, are best operated when integrated together as an organization-wide managed system of review.

Keywords Auditing, Chief executives, Performance management, Strategic management

Paper type Research paper

Introduction

A key characteristic of strategic management is that external environments are ever changing, such as the make-up of governance and institutional structures, and the need to understand how these affect the making of optimal internal resource allocations. Strategic management research concerns the development of concepts and models that help to get a better grip of such problems (Chau and Witcher, 2005a), such as how senior personnel can facilitate activities at the operational level. Top management includes senior executives, people who attend board of directors meetings, and also those who have an active senior and general management role. The involvement of senior managers directly with lower-level activity and subordinate management is under-researched. This paper explores explicitly the link between top executive level reviews of the strategy process in relation with business excellence, and this is illustrated through a real case example.

The literature is typically focused on how subordinate management can be involved with strategic decisions, rather than the other way round (Westley, 1990; Floyd and Wooldridge, 1992; Dutton and Ashford, 1993). The involvement of senior managers in periodic strategic reviews at an operational level is usually discussed for its importance as a check on the assumptions of longer-term vision and strategy (Kaplan and Norton, 1996, 2001) or as a means to determine a strategic context for the rest of the organization (Ghoshal and Bartlett, 1994). This literature is therefore premised on beliefs that accept decision-making should be devolved, use flat hierarchies, and

accommodate emergent strategy; in general this suggests that senior level involvement in daily management should be low. Accepting that decision-making should be participative, it is often difficult for senior management to make strategically-related decisions that are informed by experience. Typically a programme started and championed by a CEO is difficult to evaluate objectively, especially if subordinates believe they are in danger of questioning authority when they hold back from giving adverse and critical feedback (Hofstede, 1976). So feedback on strategic decisions is likely to be delayed, and in the end the reasons why a project has failed may not be clear.

Mintzberg (2004, pp. 206-208), reviewing the behaviour of senior managers 30 years on from *The Nature of Managerial Work* (Mintzberg, 1973), observes that:

> Many senior managers are removed from the ongoing daily activities of their organization. This creates all kinds of problems, not the least of which is that we get grand and gloriously simple-minded strategies . . . strategies so removed from day-to-day life of their organizations . . . We have more and more disconnect between senior management and the rest of the organization.

Involving senior managers proactively in review at an operational level is a way of countering these possibilities. This is especially so if it brings senior managers closer to experience at daily management. In 1999, a Japanese CEO was appointed at Nissan South Africa (NSA) and this came with a revised approach to top management's understanding and commitment towards both shop floor and middle management's implementation and execution of strategic and other cross-functional improvement activities. This improved understanding came about by using the auditing method referred to at Nissan as the "Top Shindan Audit". The literal translation of this term from Japanese is "Top Executive Audit" (we refer to the acronym "TEA" in this paper). This new approach was part of a Japanese methodology known as *hoshin kanri*, the literal translation of which is "policy management" or deployment. In this paper, we give a brief introduction to *hoshin kanri* to consider the place TEAs have as a phase in the four phases of *hoshin kanri*. We explain what happened at NSA when TEAs were introduced. Our paper closes with a discussion of the role for top management more generally in relation to a managed system of multi-level review.

Hoshin kanri
The first detailed account of *hoshin kanri* is that of Akao (1991) which comprises a collection of articles written by Japanese academics and practitioners. One of these, Tokisuke Nomi distinguishes *hoshin kanri* from daily management and cross-functional management as:

> . . . all organizational activities for systematically accomplishing the long and mid term goals as well as yearly business targets which are established as the means to achieve business goals. In many cases it is used for yearly targets (Akao, 1991, p. 47).

We define "*hoshin*" as a strategic objective, which is expressed as a short statement of a senior management level policy or goal; this outlines in broad terms the expected associated strategies and means. The term "*kanri*" refers to the management of the hoshin. The basic principle is that everyone in the firm should contribute to the achievement of hoshins, so that at the end of an annual cycle, the organization as a whole will have moved beyond what it might have only achieved through normal

working (Witcher, 2002). Hoshin related activity has priority and is used to align other systems, plans, and other activities. The linking of strategic goals to objectives in daily management is central to effective Japanese total quality management (TQM) (Witcher and Butterworth, 2001).

Research indicates that *hoshin kanri* consists of four main strategic implementation and execution tasks – focus, alignment, integration, and review (Witcher, 2003; Chau and Witcher, 2005b). Hence:

- Senior management must focus organization-wide attention on strategic objectives, but to balance these with other incremental diagnostic objectives to set the short-term vital-few (specific breakthrough objectives) strategic priorities.
- The organization as a whole should use these priorities to align plans and other local priorities and management systems.
- Everybody should integrate the priorities in daily management by applying TQM (TQM – the principle of continuous quality improvements at lowering costs) and PDCA (stages of plan, do, check and act, which is what characterises good management practice) principles to the management of work.
- Senior management must then review the operational effectiveness of the core organization-wide management processes, including the effectiveness of strategic management itself.

This "FAIR" view is represented figuratively as a strategy management annual cycle (Figure 1); strictly, the FAIR cycle involves the implementation and execution of longer-term strategy into shorter plans and actions. TEAs apply to the "review" part of this cycle. It represents an annual in-depth check on how strategy and other cross-functional performance management activities have been managed during the year. Kondo (1988) gives probably the most comprehensive description of TEAs when discussing Japanese *hoshin kanri*. He notes its purpose is to see if action is required by top level management on its strategy. The idea is not for the organization to pass an examination, but to stimulate mutual discussion between senior management and people who implement top management goals to find ways and means to improve the existing situation. It is not therefore merely corrective action or diagnosis: Kondo also stresses the importance of discussions based on facts. Typically a senior management
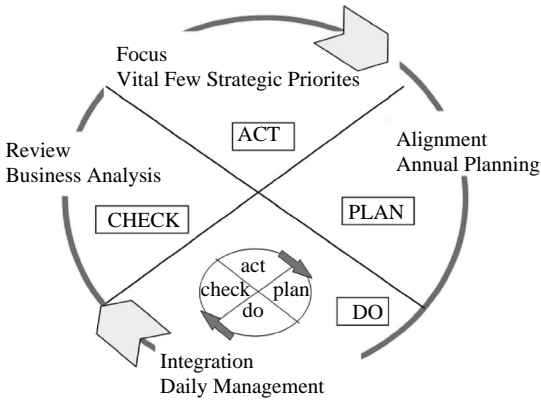

Figure 1.
Hoshin kanri FAIR and
Deming's PDCA

team will provide an initial short report, and top level management will draw up a checklist of subjects to consider. Surveys of the present situation may be conducted. Because annual audits can lapse into repetitiveness, some organizations will use a theme (say, how to double productivity in five years, or beat a competitor). The audit team will take part in plant tours, walkabouts, where employees will be involved with discussion with senior management. There will also be roundtable discussions. At the end of the audit, recommendations will be suggested from top management, and these are likely to be considered at the next audit. Hence, it is argued:

> The educational character of the audit is considerable. The business audit offers the best chance for top management to grasp systematically those facts that may reflect on themselves. The employees audited are also given opportunities to examine and to rearrange their daily work. Moreover, the internal audit contributes to the improvement of mutual understanding and human relations among the employees. Such an opportunity can hardly be obtained through the daily meetings and reports (Kondo, 1988, pp. 35F15-16).

A visible involvement of senior management sends messages to other employees about top level commitment to strategy and strategic objectives. The involvement of people at other levels also acts to reinforce motivation with regard to company-wide issues. It can also play an important role for the dissemination of knowledge generally across the organization, particularly when results are relayed at large through an organization's communication media and specialist networks. Top management audits take a variety of forms in companies. The most simple is to roll up data from periodic strategic and operational reviews, and to use checklists and questionnaires such as employee and customer satisfaction surveys. Some organizations use performance excellence models (good/best practice assessments) and benchmarking (comparative techniques to identify best-in-class achievements). One of the most well known is Xerox's use of a management model based on the Baldrige criteria (see for the latest version, NIST, 2006) and other performance excellence criteria (Witcher and Butterworth, 1999).

An important advantage of a performance excellence framework is that it gives an easily grasped total perspective (some call it strategic transparency) for everyone, which makes it easier for an organization to band together and focus its capabilities on those critical success factors that underpin competitive advantage. This helps to achieve an organization's overall strategic objectives, and enables top management to drive the management of key processes in a way that will improve or harness them for best results. Some organizations audit more frequently than yearly, but usually its timing is tied into an annual planning cycle. This approach to management has manifested itself in NSA in different ways. Previously the executive, up until the appointment of a new Japanese CEO in 1999, was not always able to evaluate whether data presented at various operations meetings reflected the true situation in the organization. Often the data presented were distorted or misreported. The new CEO paid much more attention to operating detail and wanted to see actual results and more significant data, even if they were not as predicted or desired.

Top executive audits at Nissan South Africa
One of the first major changes to management that came from the new CEO was to introduce *hoshin kanri* and the concept of TEAs into NSA. A clearer clarification of a TEA can be given as below:

- A TEA is defined as a detailed audit performed to obtain an overview of each activity that is supporting the company's stated strategic goals and objectives.
- The senior executive of the company always conducts the audit, which is focused on an individual's function and proposed improvement activity.
- The audit is based on the ongoing review of the level of actual achievement of targets by an improved activity against the company's agreed business plan.
- The audit can be conducted at any level in the organization where an activity supporting the business plan takes place.
- The TEA provides feedback to evaluate longer-term strategic management, including the assumptions that underlie longer-term purpose and objectives.
- The audit also provides feedback for the shorter-term tasks of strategic management, namely the implementation and execution of longer-term strategy as short-term plans and targets.

The CEO of NSA conducted audits at each department to understand personally what performance level was being achieved. These audits were not formally structured as might be the case for a formal quality audit for certified standards. There was no formal check list or report-back format. At first it appeared as though these audits were very informal and impromptu but it soon became apparent that they were part of a broader plan. Each division would be scheduled for an audit based on the current level of performance and the impact on the company's targeted goals. A total of 50 audits were scheduled and conducted. The aim of each was to monitor performance results following improvements to the system of production and service areas that were supporting production. Each level of management and supervision was then interviewed by the CEO and the activities that supported each business plan item were assessed for relevance and accomplishment. It was up to each individual being audited to state their improvement activity and to listen to advice given and then to act upon that advice in order to achieve improved results. There was no direct criticism, only comments on improvement opportunities. If an area had been seen to be successful the CEO would comment that the performance to date was "very good."

The effect of restructuring top management meetings
The new CEO also decided to restructure the operations meetings at NSA to focus more on actual improvement activities and this had an immediate effect on the feedback of the business performance. The focus of action was now turned to actual results emanating from improvement activities which each divisional head had to explain to the meeting attendees in detail. If the divisional head did not have a full understanding of the specific activity, the relevant manager or engineer would be called upon to explain the detail. In order for top management to be able to report on the real issue, presenting the real data at the operations meeting, they had to become far more involved with the actual day to day activity through observing and understanding the process. The CEO had a very good in-depth knowledge of each process through his many TEAs and was able to ask searching questions to establish the understanding of each senior executive of the actual performance criteria and result. This feedback and debate on the real issues created a more open discussion and over a period of time reduced the fear factor that had been previously present in these meetings. If a target

was not met according to the data being presented, the CEO would openly discuss the issue and either suggest an alternate action or ask for other opinions to address the concern and not the individual presenting it. In the early stages of this new format there was some resistance to the new approach but over time this method became the accepted normal activity. A paradigm had then been changed and a new paradigm was emerging.

The need to focus on consistency

One of the expected outcomes of the TEA is to ensure that there is an alignment of activities in the cascading of strategic objectives and operating methods. It is an important part of Japanese management to be consistent in the application of each task allocated; since it is difficult to improve a process that is out of control, so therefore, any variation in a process needs to be limited. The first aim in limiting variation is to focus on the consistency of the task being performed. The degree of documentation developed is dependent on the nature of the task and the skill and experience of the person performing the task. This is why the Japanese spend a lot of time and effort evaluating the magnitude of the task as well as the skill level of the operator performing that task (Drucker, 1971).

At the higher level in the organization, consistency comes through the development of the *hoshin kanri* activity. This methodology is aimed at being consistent in target setting and achievement, not just in the magnitude of the target set but in the overall relevance of the target to the organization's strategic goals. Nissan Motors Limited of Japan has created a management systems framework referred to as the Nissan Plant Management System. This framework prescribes an approach to achieve quality and productivity improvements by consistently utilizing various benchmark standard practices developed by Japanese engineers.

Once daily management is under control the *hoshin kanri* methodology can be used to gain the improvements necessary to remain competitive. The TEA can then be used to monitor improvements and ensure business plan targets are met on time. At shop floor level, once the operating system is under control, improvements to the process can be made through *kaizen* activities or gradual small improvement steps as described by Imai (1986). The overall purpose of the TEA is then to confirm the current status of the *hoshin kanri* methodology and the strategic objectives and to check the appropriateness of individual objectives and methodologies to the overall strategic objectives, and to gain the required support from the lower levels of supervision. Specific managerial skills such as active listening, questioning, probing and coaching are crucial to the auditor in striving for common understanding and facilitating the achievement of the *hoshin kanri* objectives and methodologies. TEAs focus on constancy of purpose by comparing improved methods and results across functional barriers and determining whether they are focused on the broad company objectives.

TEA and a managed system for organization-wide review

Learning from experience and developing the competencies to problem solve issues are essential aspects of the learning organization (Senge, 1990; Nonaka and Takeuchi, 1995). This applies as much to top level management as it does to everyone else. Review does not just involve strictly monitoring, but it also involves a more considered evaluation of context, assumptions, as well as progress. The meaning of "review"

typically suggests periodic reviews when progress is assessed against pre-set milestones or to review critical issues. Reviews work most effectively if they are linked together as an organization-wide managed system of review, which delivers an audit trail of how the organization as a whole has been performing to achieve its purpose and longer-term strategic goals. In this way, learning is achieved in a way Mintzberg (1978, p. 935) describes as falling within "a pattern in a stream of decisions" because the executive can refer back to that audit trail to learn from that "pattern." This system provides an essential feedback loop for organization-wide learning and an opportunity for strategically aligned evaluation, problem-solving, and corrective action where there are obvious and critical deviations. In this way, review provides the thread that knits a methodology such as *hoshin kanri* together.

Examples of documented accounts of managed company-wide systems of review are rare; but for those of Hewlett-Packard, see Cole (1999) and Witcher and Butterworth (2000). Review is also a social activity that involves participants in a shared evaluation of objectives and facts, which reinforces consensus, especially for cross-functional management and where individuals from different functional areas may meet only infrequently.

How periodic review is conducted is important. The stress is on review as a method for investigating issues and not centred on who is to blame. At the same time, individuals who have ownership of objectives and plans must ensure that review is carried out. If top management takes responsibility for an overall managed system of review, then it is likely that meetings will be held when necessary, that they are prepared, chaired, and followed up effectively. A managed system requires its own administration and staff support, and involves administrative tasks such as managing meetings, agendas, logistics, the provision of advice, even training to assist the reporting process, and post-review activities to ensure that follow up action happens quickly.

The *hoshin kanri* FAIR approach uses "review" to mean only the TEA or a business (performance) excellence evaluation, and which will include an appraisal of the annual strategic management process (*hoshin kanri*) itself. It is probably the most important vehicle for driving and facilitating organization-wide learning, especially for strategy and improvement in core organizational cross-functional processes. The participation of top management means that a wide involvement of people is likely and the relevance of the state of health and the company's operational effectiveness in relation to best practice will become more understood in the wider organization. Figure 2 shows how an inter-linked system of review might look.

Information from review is used as part of the strategic management process shown in the figure as a sequence of boxes: first, as feedback on longer-term strategy and to inform the determination of annual priorities, which starts off the FAIR process. The circle to the left illustrates that data may be rolled upwards from a daily to an annual level of review. The TEA is shown here as an "annual business audit" under "review." The arrow from "review" points to a business excellence framework, an approach favoured by Western companies, which is likely to involve best practice benchmarking, as well as data rolled up from strategic reviews. Such TEAs typically concern an evaluation of an organization's effectiveness in managing its core cross-functional processes, in terms of both enablers and business results. One of these enabling processes will be strategic management. The importance of this form of
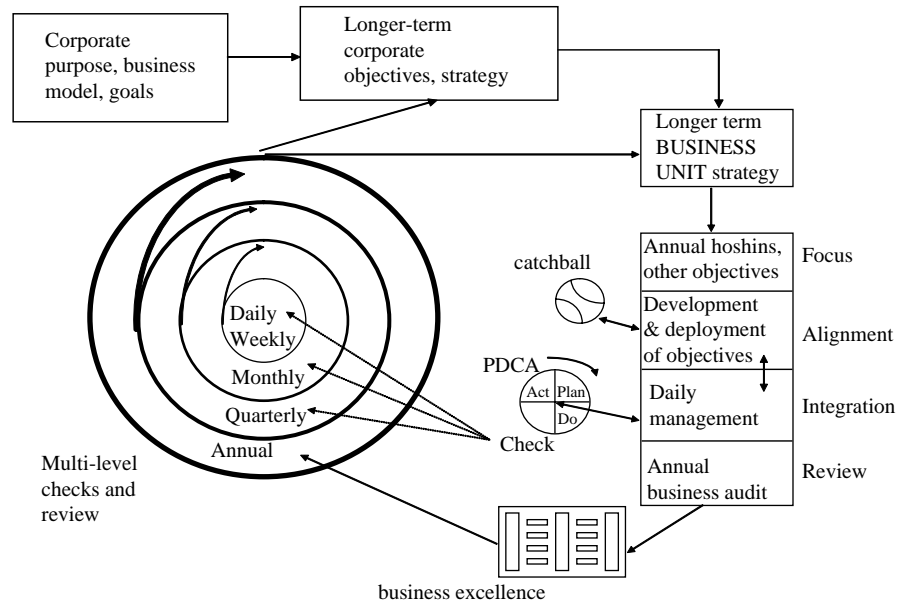
Figure 2.
Classification of reviews

annual review is that it should involve top level management in a way that enhances its understanding of daily management. This is shown in Figure 2 linked to Deming's "Plan-Do-Check-Act" cycle, a TQM-based business process approach for managing work (Deming, 1986). In fact, PDCA is an essential principle for effective *hoshin kanri*: top management should use a PDCA cycle approach to manage FAIR (see how each of the annual PDCA stages, shown in the earlier figure, corresponds to a counterpart in the FAIR phases).

The importance of feedback and review to strategic and general management, of course, goes back a long way (Ackoff, 1971; Argyris and Schon, 1981; Lorange *et al.*, 1986; Simons, 1995), and in the resourced-based view of the firm (Nelson and Winter, 1982), especially where strategic management is understood as a dynamic capability (Teece *et al.*, 1997; Eisenhardt and Martin, 2000). Japanese approaches, such as the Toyota Production System (Liker, 2004) which uses TEAs (Monden, 1998), are often used as examples of the learning organization. However, how a senior level of management can learn is unclear. Specifically, for the implementation and execution of strategic objectives, Kaplan and Norton (1996, p. 264) observe, in the case of the balanced scorecard, that "a process to learn whether organizational strategy was working and being implemented effectively" for senior managers is typically missing. The scorecard idea was originally developed out of hoshin kanri practice (Kaplan and Norton, 1993), but the business process basis for managing strategic decisions, which is the important feature of *hoshin kanri*, is not (usually) followed for the scorecard. The advantage of using TEAs, however, is that the highest level of management gains the understanding to which Kaplan and Norton refer; if TEAs were used for scorecard management then top management is likely to be more effective in its implementation and execution of strategic management because it will know more about experience at an operational level. This is because TEAs help to create transparency between the

levels of the organization in understanding these operational level constraints; this, in essence, is a purpose the balanced scorecard endeavours to achieve, and so arguably the balanced scorecard and *hoshin kanri* should be regarded as complementary, rather than alternative approaches, as some literature seem to suggest (Andersen *et al.*, 2004).

Conclusion

In conclusion, we see the role of review as extremely important to the long-term strategy and operational effectiveness of an organization. In particular, the role of strategic reviews, such as (TEAs, or top shindan audits) form not only an important component of the FAIR framework used for successful hoshin kanri practice, but also as an integrative managed system of strategic review, perhaps with the balanced scorecard to link knowledge of operational activities to CEO level plans. This is when their use is most optimal. The case study of NSA has shown how they operate in practice, the issues that arise during its implementation, and particularly how they can be beneficial. Hence, the use of strategic reviews provides a framework for assessing company performance and business excellence that links top executives more closely to operational activities. The competitive advantage of a firm depends inevitably on its control over it intangible resources (as well as the tangible). In this way, the use of strategic reviews, particularly as part of *hoshin kanri*, provides an improved form of monitoring and performance management framework that helps to focus organization-wide effort and improve operational effectiveness. The contribution of this paper is in how this has been so for the case of NSA.

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