SURVIVAL LESSONS

WHAT UTILITIES CAN LEARN FROM THE AUTOMOTIVE INDUSTRY

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As utilities in more countries face threats to their business models, one industry offers survival lessons: automobiles.

The core of the traditional utility business model is under siege and pressure on performance is increasing – especially as renewables gain ground and regulatory pressure rises. Unfortunately, the top-down performance improvement measures that utilities have followed in the past are not working.

We've seen this story before. When automotive companies faced similar threats to their business, they changed – dramatically. As a result, the companies not only stayed in business, but also discovered new opportunities and revolutionized manufacturing. The best-in-class have repeatedly and sustainably improved their performance by establishing new business designs, making efficient investments, reducing total costs and increasing flexibility. Their cultures were also realigned so that they could sustain these advances.

The automotive industry's continuous performance improvement is characterized by three key characteristics: a more holistic perspective, portfolios of smaller initiatives and continuous performance dialogue aimed at permanently integrating improvements into the company's operations. Below we explore how each of these tenets could help utilities to thrive in spite of a business landscape that is undergoing dramatic change.

CHANGING PERSPECTIVE

Most utilities' performance improvement projects focus on costs and growth. But ultimately they result in little more than an incremental improvement.

Instead, utilities should adopt what we call "a business model perspective." Utilities must change their viewpoint significantly so that they can abandon their familiar environment. Like automotive companies, utilities should take into account both new and existing business areas as well as both external and internal customers. (See "A Business Model Checklist" for 10 questions that we suggest managers ask themselves to determine where their perspective could be strengthened.)

By adopting a more holistic view of how to improve operations, utilities can unlock new and far-reaching profit potential. For example, after conducting an extensive examination of current and future business models, a utility was able to both reduce costs in its customer service department by 25 percent and formulate a new value proposition based on the actual needs of internal customers. Before switching to such a business model outlook, the customer service department had identified potential savings of only 10 percent based on a traditional cost reduction approach.

At the same time, companies should link financial and operational outlooks. Before embarking on new improvement initiatives, managers need to determine if operational changes are meant to improve their costs, profit, cash or debt. Next, they should draw up plans for how to measure their operational improvements and benchmark themselves against competitors. Automotive companies, for example, often use benchmark analyses, such as the Harbour Report, to help them define appropriate targets for improvement.

There should also be a strategy for how the company's business model will continue

to develop and a broad understanding of what that will mean for both operational management and its financial performance. For example, automotive companies have improved their key performance indicators and operating results substantially, in large part because they consider almost every aspect of their business before making critical decisions – their value chain, marketing, quality, productivity in production, supply chain, as well as technical assistance and administration. More recently, some even involve their suppliers and service providers both in production and in supporting functions such as contract manufacturing and pre-assembly, or as system suppliers.

A PORTFOLIO OF INITIATIVES

It is counterproductive to carry out "big bang" initiatives in environments with constantly increasing market pressure. Traditional stand-alone isolated, cost reduction projects have a defined end, and thus cannot create sustainable profitability.

A better approach, and one pioneered by automotive companies, would be for utilities to implement permanent programs with multiple initiatives. In the automotive industry, individual improvement steps may assist with a new production plant or the launch of a new product. But permanent improvement measures that range from material cost reductions to better utilization of materials and capacities to the construction of new production plants, deliver the most significant progress. Indeed, projects like these can lead to not just one-time cost savings in the range of 10 to 15 percent, but also annual improvements in the range of 3 to 5 percent.

One reason a portfolio of smaller initiatives is preferable for a utility is that it lets the company avoid disaster should one big initiative not work out. To make a major contribution to sustainable performance, each smaller initiative must be integrated into a program portfolio and fulfill a specific requirement. Multiple initiatives, such as purchasing process improvement or group-wide liquidity management, often impact the program's goals in new ways. Every initiative must also have a clear focus and a clearly defined objective.

A succession of different initiatives also enables companies to achieve improvements driven from top-down as well as up from a grassroots level. The focus, for instance, can begin with costs, and then move on to cash. At times, groupwide global issues, such as a utility's information technology infrastructure, could take priority. At other times, targeted initiatives at the individual stages of the value chain can be the focal point.

PERMANENT INTEGRATION

Automotive companies have shown that performance improvement programs can only reach their full potential with consistent management. Ideally, a continuous performance dialogue will be established that extends from the board of directors and management team (with quarterly performance reviews for each business area) down to an operational team level (with team performance reviews at much shorter intervals).

Individual employees also must be motivated to participate in the improvement of the company's performance. This means involving people starting from when problems are first identified, through the generation of ideas, to the detailed development of a solution. In addition, it is important to adapt both employee incentive systems and career paths, so that each employee finds it personally worthwhile to contribute.

A utility can start a program at any level. These programs, however, are usually most effective when someone is given the authority to manage the initiatives and to define clear targets for them. With the help of management tools, it is possible to monitor the results of performance improvement initiatives and to spread those successes throughout the organization. Operating divisions can also be helped in optimizing the results of performance improvement initiatives by providing them with a few flexible tools.

BREAKOUT PERFORMANCE

Automotive companies have proven that it is possible for manufacturing industries to achieve breakout performance. While it may not at first seem intuitive, we believe utilities have a real chance to benefit from the auto industry's experiences. By combining a "business model" performance orientation with a diversified, long-term improvement program, utilities can also systematically prepare themselves for future challenges. Like automotive companies, they will gain financial leeway for strategic realignment and, consequently, foundations for successful and continued development in a rapidly changing market environment.

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