



Organisations have an intrinsic need for comparative information.*

Performance Benchmarking: Value Beyond Competitive Analysis

By Greg Shea

PricewaterhouseCoopers (PwC) has provided benchmarking services to the forest and paper industry for almost twenty years. During this time we have observed the significant impact that benchmarking has on organisations engaged in maintaining and improving performance.

The goal of this article is to explore how organisations employ benchmarking and to discuss ways that performance benchmarking can create value beyond competitive analysis. Before examining benchmarking use and potential, we need to revisit the benchmarking concept.

Performance Benchmarking Overview

Benchmarking has been defined in several ways.

"Benchmarking is the continuous process of measuring products, services and practices against the toughest competitors or those companies recognized as industry leaders (best in class)."

Source: The Xerox Corporation

"Benchmarking is simply about making comparisons with other organizations and then learning the lessons that those comparisons throw up."

Source: The European Benchmarking Code of Conduct

Benchmarking is the ongoing, collaborative exchange of confidential information that enables organisations to evaluate relative strengths and opportunities. Benchmarking provides timely feedback on operating performance in the context of the organisation, industry and market.

The benchmarking concept is scalable. Organisations can benchmark their entire operation or an individual office or division. Alternatively, benchmarking can be problem based, focusing on a specific issue, or process based, focusing on a specific business process activity.

Benchmarking can be internally or externally oriented; both compare business units that perform like functions, thereby identifying and exemplifying best practices. When done regularly, internal and external benchmarking provide feedback showing the effects of current and past practices. The benefits of internal benchmarking include the relative ease of conducting such analysis, and the ability to interpret and reapply best practice.

In contrast, external benchmarking provides the independent perspective needed to confirm an organisation's potential performance. Generally, it is more difficult to obtain this type of benchmarking information.

Benchmarking Appeal

Benchmarking emerged as a common business practice in the 1980s and has endured to be one of the most relevant performance improvement techniques. The reasons for its popularity are inherent in the logic behind the following questions:

- How have others dealt with this situation?
- What should this cost?
- What is a reasonable return on investment?

When faced with uncertainty, organisations crave information. To avoid repeating steps already taken by others, organisations have an intrinsic need for comparative information. Benchmarking meets this need by offering unique insights into relative performance.

Benchmarking also enables organisations to link managerial compensation to performance. We have seen that striving for the top 50th percentile performance is a ubiquitous organisational goal, and benchmarking is the principal means to determine how to achieve this goal.

Key Success Factors

The key to successful benchmarking is to compare like information—a basic tenet that provides certainty to the benchmarking results, making it feasible to apply the results.

Successful benchmarking enables users to develop an understanding of what is behind the numbers that are pertinent to the situation. Careful consideration needs to be applied to the group of organisations included in the comparison. While industry-wide benchmarks make interesting conversation, they tend not to drive operational change. When embarking on performance improvement, it is also important to consider non-financial information with the benchmarking results to ensure that change is made in the context of the organisation's environment and culture.

Formal agreements identifying the roles and responsibilities of all benchmarking study participants are needed for successful benchmarking. Without such agreements, benchmarking studies are at risk of inaccurate or misrepresented data, compromising participant value.

Maximising Value from Performance Benchmarking

There are five general uses of benchmarking results:

1. Competitive Analysis
2. Allocation of Capital Funds
3. Managerial Incentives and Compensation
4. Performance Improvement
5. Performance Validation of Forecasts and Budgets

Companies need to understand their competitive environment. Benchmarking provides them with insight into industry cost curves, net revenues, and market shares. It also helps them to identify the strongest competitors and the best-in-class performance targets. Over time, companies are able to discern trends in regional and product-specific opportunities, promoting the effective allocation of capital funds. Annual benchmarking also provides an effective means to establish incentive compensation targets and to objectively measure performance.

The importance of competitive analysis depends upon the characteristics of the industry. Fragmented industries that produce similar products have a requisite need for competitive information. While consolidation decreases this need, the importance of performance improvement and validation remains.

The emphasis and rigour of performance improvement initiatives increase with industry consolidation. Companies engaged in consolidation follow a path of change management and the realization of “quick win” opportunities. Once synergistic opportunities are achieved, benchmarking provides an important source of incremental improvement opportunities. Methodologies such as Six Sigma can be used in conjunction with benchmarking to help organisations capture their most challenging incremental improvement objectives.

Benchmarking is also used to validate the accuracy and relevance of financial forecasts and budgets. This external feedback provides the context needed to evaluate relative performance in the current marketplace. In the financial industry, there are examples where the corporate budgeting process has been replaced with benchmarking and other market-oriented feedback mechanisms. The rationale is that budgets are costly and often ineffective due to the time investment and organisational tendency to rationalise deviations from plans.

Regardless of an organisation's budgeting practices, relative performance in the current marketplace is paramount, as is resource flow to those business units that demonstrate the greatest potential returns.

Summary

Benchmarking realises the business need for comparative information. Confidentiality and comparability are critical to successful benchmarking. Companies that benefit the most from benchmarking employ the results in multiple ways. Industry consolidation causes a shift in the primary use of benchmarking from competitive analysis and strategic planning to performance improvement and validation.

Benchmarking is a powerful tool to identify incremental performance improvement opportunities. Methodologies such as Six Sigma complement benchmarking by helping organisations achieve their performance goals. Benchmarking can be used to validate budgets and performance goals against market realities.

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