ENDANGERED SPECIES: STAYING OFF THE LIST

Reorganization and headcount reductions alone won't keep companies from landing on the endangered species list. Changing the way they operate will.

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Approximately 65 million years ago, a large meteorite struck the Earth, setting off significant climate and atmospheric changes that gradually killed off most living things. Dinosaurs, the largest creatures of that era, disappeared, never to be seen again, and the few species that survived had to learn how to adapt in order to thrive in a new, harsher environment.

While no large meteorites struck the Earth in July 2014, that time will forever mark the beginning of the end of business as usual for traditional E&P companies, for that was the last time they saw oil prices above $100 per barrel.

Managing The Cycle

Some E&P organizations no doubt believe they are similarly endangered. In response to a 50% drop in oil prices, they have adapted by rapidly cutting capital spending and shedding costs and headcount. Some see the price drop as a "temporary adjustment" and are content to "cut and cope" until the market rights itself and capital starts to flow again. Others see this tectonic shift in market dynamics as the new reality and believe the old way of operating will neither be profitable nor competitive going forward.

In fact, in order to survive, E&P companies will need to fundamentally transform and take back the high ground in this new reality. That will take more than a strategic restructuring or negotiating with contractors to lower drilling dayrates. To sustain viability requires doing more with less and increasing one's capability and efficiency. This includes learning new ways to lead, communicate and execute—while bravely letting go of many of the traditional operating paradigms that have defined this industry over the past several years.

If companies don't think about how they can change their operating model while the oil price is low, they may end up damaging their business in the medium term if oil prices don't go back to $100 as soon as expected. And, if prices do rise sooner and companies haven't made any real operational changes, the opportunity to do so could be lost.

Lessons from other industries

E&P is not the only industry to experience a sea change recently. In fact, since the most recent boom/bust cycle in oil prices, there have been several examples of businesses that have, in the face of a changing environment, either perished or thrived.

Endangered/Extinct	vs.	Surviving/Thriving
Motorola		Apple
Blockbuster Video		Comcast/Netflix
Digital Equipment/Compaq		IBM
Kodak		Canon
Borders Books		Amazon

Whether today's E&Ps will end up on the right or the left side of this graphic depends on their willingness to make hard choices, embrace new ways of thinking and, most important, learn new skills and behaviors.

While it may not feel like it, the easy part is just ending—the significant cuts in rigs, headcount and costs. Next comes the harder part: how to unlock enterprise value in order to return to profitability, productivity and innovation. Reorganization and headcount reductions alone won't keep companies from landing on the endangered species list. Changing the way they operate will.

Which version of the truth do you want?

E&P organizations are no longer made up of a collection of silos—the stand-alone, asset-centric teams commanded by a traditional top-down structure. Over time, a confederation of support and enabling functions has evolved, each designed to drive a specific process, system or function and help the asset teams achieve their goals.

The straightforward model of accountability has morphed into a complex matrix, with each function along both axes having its own objectives and performance targets. These support organizations include project management, operational excellence, continuous improvement, Lean Six Sigma, and a variety of technical authorities and subject-matter experts.

However, there are unintended consequences: Accountability has been diluted, end-to-end visibility and transparency are lacking, and there is a significant drag on the asset team's ability to make decisions and drive performance.

Another unintended consequence of the matrixed organizations across the E&P value chain? Each team or function comes with its own management system, scorecard, data source and performance targets—many of which are independent of the others.

This can lead to a “function-first” performance culture that develops from functional leadership that measures and incentivizes their respective KPIs (key performance indicators), whether or not that metric actually improves the performance and profitability of the asset.

Next to safety, the highest ranking strategic imperative is maximizing enterprise value.

Approval vs. veto authority

When overseeing projects, matrixed organizations have established governance structures with steering teams or decision boards that clearly identify who makes the decision to proceed. However, this structure has created a new dynamic that only succeeds in granting the ability to veto, not to proceed. The churn and rework associated with assuring there are no vetoes generates significant rework and engagement, further eroding decision velocity, time to value and overall project ROI.

E&P teams can become immersed in processes. Many of the E&P support functions are established to assure execution of a particular process (i.e., project management), losing value when the task of following the process becomes the goal. Lost in the shuffle are the results that drive enterprise value. Process compliance, by itself, is not a result.

In an industry driven by major capital investments that are ultimately executed by contractors, the phrase “time is money” could not be more applicable. The more time it takes to plan, decide and execute projects, the more expensive those projects will be. Time lost due to equipment delays, waiting on the next meeting to make a decision, scope creep, and rework that occurs during the project lifecycle are all drags on time to value and ROI.

Work smarter

It’s important to assess the value of meetings. Across many organizations, meetings become the place where people go to be “busy” and become proxies for productivity and progress. What is the objective of these meetings, and who really needs to be there? How well do we prepare for these meetings? Why can’t a project-steering team meet to make a critical decision in 30 minutes or less?

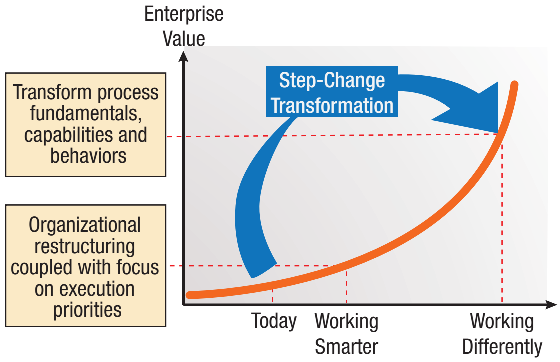
At meetings, people spend the majority of time reporting what they and their teams have been doing, not what needs to be done to support decisions that drive performance and value.

Restructure the organization and drive teams to focus on project and activity value. Prioritizing and rationalizing low-value projects assures the smaller organization delivers the high-return projects while low-value work is delayed or simply not executed.

It’s also critical to work differently. To achieve a step-change in enterprise value, an organization needs to work differently. This goes far beyond changing *how* work gets done (improvements to current processes and systems) to *what* work gets done. The management team can then aggressively identify, innovate and implement opportunities to unlock organizational capability and effectiveness (OCE), and achieve breakthroughs in efficiency (see graphic).

A truly LEAN organization (one that fosters continuous improvement) is not one that seeks efficiency by training staff around a set of

Unlock Organizational Capability Effectiveness (OCE) To Drive Step Change In Enterprise Value



OCE = ƒ(Org. Capability x Value Added Time)

LEAN tools, but rather one that is personified by LEAN leadership, behaviors and disciplines that identify and eradicate waste as part of its DNA. This includes time wasted in meetings, performing rework and waiting for decisions to be made.

Transparency is a cornerstone of performance awareness and accountability. The organization must deploy a singular hierarchy of performance metrics that cascade down to align with every function across the company. Each separate functional target needs to directly drive top-level metrics, with net earnings and cash flow at the top of this KPI tree.

Make performance visible by highlighting plan vs. actual variances through a lens of root causes and corrective actions. When the performance hierarchy is effectively deployed and transparent, the organization can drive success.

Assets first or function first?

E&P shareholders are not particularly interested in how many wells were drilled or how much water was hauled. They measure an E&P’s enterprise value by maximum hydrocarbons produced at the lowest cost, in the safest manner.

Function teams need to understand this, but they also must recognize that trade-offs need to be made in service of overall asset profitability. This may require keeping a rig idle for a week or waiting until warmer weather to build well pads. Next to safety, the highest ranking strategic imperative is maximizing enterprise value—everyone in the organization, regardless of function, must understand their role in that.

In the world of E&P capital projects, no one will argue the fact that a $3 billion project is several orders of magnitude larger and more complex than a $3 million project. If that is the case, why should companies use the same project-management process and tool set? Establish a fit-for-purpose and scalable project-management framework, and support it with disciplines and behaviors that can vary with project size, risk, complexity and enterprise impact. This sliding scale should apply to decision authority, administrative and compliance requirements, governance, and critical management of change.

Done is better than perfect. In other words, don't let perfect get in the way of good enough to achieve the desired result. Outcomes, not activity (being busy), are what drive value. Recognize when redundant analyses are providing diminishing returns. Coach leaders to apply 80/20 thinking when it comes to decision making and checking the veto authority of teams.

During project execution, deploy and reinforce a simple *Plan–Execute–Review* mantra across the organization. Perform regular look-backs, share learnings, deploy improvements and keep moving forward. Incentivize teams to take accountability for learning and sharing learnings with the team. Celebrate success and reward innovation.

Top quartile E&P operations are successful not because they have the best tools, processes or systems, but because they use those tools, processes and systems better than anyone else.

At the core of this difference are behaviors supported by leaders who are comfortable challenging the status quo. A successful and winning culture is not something that is acquired through training. It must be learned, practiced and experienced over time.

E&P executives must lead from the front for a successful operational transformation. For a successful journey, they must establish a coalition of the willing: leaders who are committed to the change despite cultural resistance.

It was not that long ago that major E&P companies were earning billions each year. Recent memory of that performance only adds to the challenge of getting experienced functional leaders to learn new ways of working. □

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A LEAN-ED CASE STUDY ON LOCATION

Consider a global shale operator that was just ramping up a development program in western Alberta when oil prices started to fall. However, with a four-month delay in the custom rig it had ordered, it was committed to meeting the milestone of getting first production online before the end of 2015.

Looking through a lens of past development paradigms and processes, achieving first production before the end of the year would be impossible, but the clock was ticking, literally. To raise awareness and assure everyone on the team was working toward the common goal, a massive countdown clock to first production was hung in the main production office.

Necessity drove the operator to challenge the organization to tear up the old playbook and develop a plan for success. Here is what they did:

• Adjacent work activities were decoupled and streamlined, getting some of the facility and infrastructure construction off the critical path and onsite *before* the well was drilled.

• Processing facilities were prefabricated offsite and installed modularly as time and space on the well pads would allow. That alone shaved six weeks from the historic cycle times.

• Water pumping for completions, typically a bottleneck to productivity, was LEAN-ed out significantly. Applying SMED and other waste recognition tools, the team could better recognize and mitigate the drivers of lost productivity (waiting, set-up time, crew change-overs, truck maintenance, etc.). This unlocked nearly 40% of additional capacity within a given day.

Now, all of the sudden, the impossible seemed possible. The rest of the corporation started to notice. Demonstrating a safety-first attitude, but with a relentless pursuit of eliminating waiting times and waste, the previous benchmarks of cost and cycle time were broken. First production was actually met before the end of October—two months ahead of schedule.

While other projects in the portfolio are being shut down in 2016, this asset was given a full go-ahead for continued development and has become a shining star in upstream capability and performance. The innovative practices and methodologies learned through this challenge are now being shared across the organization. Cost and cycle-time targets for 2016 are being rewritten with some projects actually being pulled ahead of plan, to accelerate revenue and keep the E&P company cash-flow positive across a continued price trough expected in 2016.