

# The Balanced Scorecard Information to Drive Performance

## ***Introduction***

Every organisation recognises the importance of measuring; as well as providing the means of monitoring the achievement of the organisation's strategy, it is a vital means of communication and motivation.

That, at least is the theory!

In reality many organisations have yet to successfully implement a performance measurement system that adequately fits the bill. They focus on financial performance and pay the price:

- Most financial indicators are backward looking - it has been likened to "steering the ship by watching the wake"
- Financial performance tends to be measured over the short term and induce short term 'fixes'
- Financial measures alone cannot communicate the organisation's strategy and priorities to its managers and staff

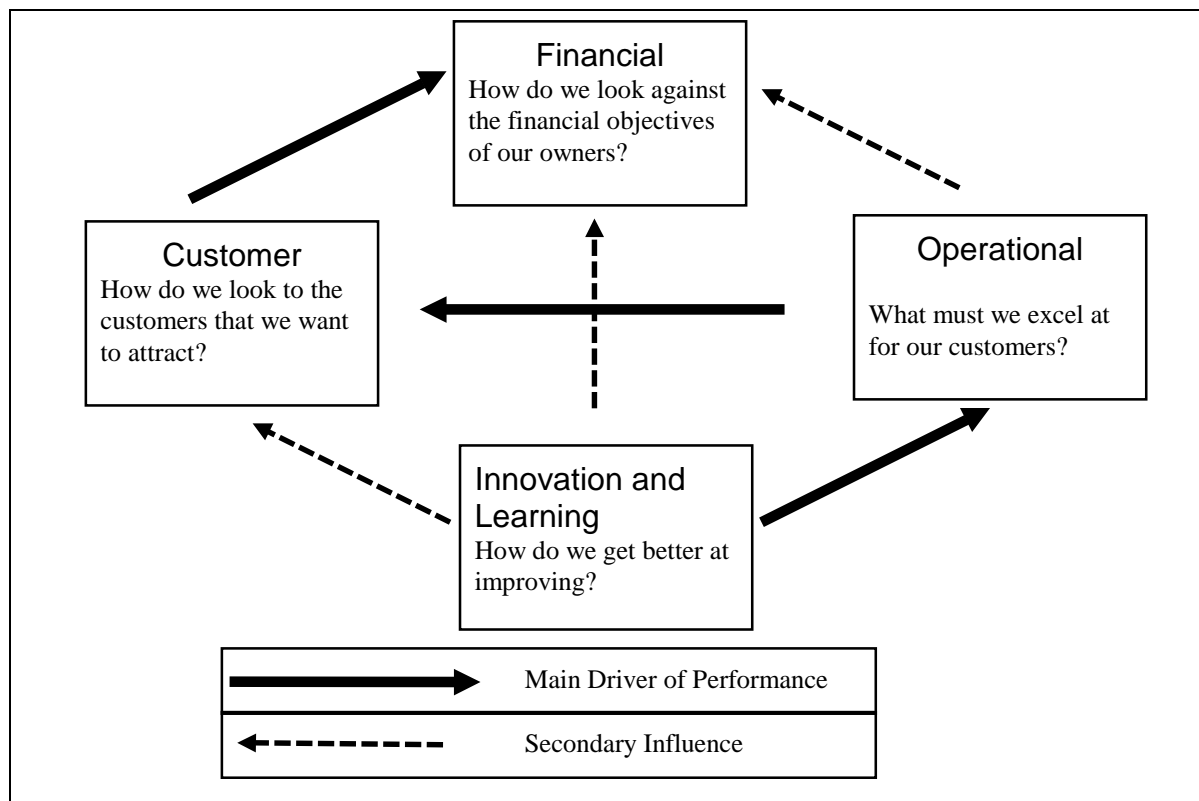
What managers increasingly need is a performance measurement capability

that supports a long term, forward-thinking strategic view across the entire organisation. They need a performance measurement framework that provides a view across a range of measures that encompass all of the key issues for continued financial success. A measure framework that itself helps improve performance by changing what people do, one that:

- Communicates priorities and direction
- Focuses on improving processes, not functions
- Aligns operational activity with strategic goals
- Provides the necessary leverage for change

The benefits of such an approach can be financially dramatic. The impact of adopting a balanced approach to measurement have been variously estimated as a profitability increase of between 15% and 30% for a typical FT-SE 100 company.

The Balanced Scorecard (R. Kaplan and D. Norton, Harvard Business Review 1992) is one such a framework.



*The four perspectives of the classic Balanced Scorecard*

### **Balanced Scorecard Perspectives**

The Balanced Scorecard enables managers to view the well-being of the business from four important perspectives or quadrants. Each quadrant of the scorecard reports performance measures directly related to the corporate vision in the form of key performance measures or indicators (KPI). The Balanced Scorecard is a mechanism for translating an organisation's vision and strategy into a coherent set of objectives and performance measures. It uses measurement to communicate the drivers of current and future success.

The four perspectives of the Scorecard provide a balance between short term and long term objectives, between desired outcomes and the drivers of those outcomes, and between objective and subjective performance measures.

Many measurement frameworks advocate a balanced range of measures. The Balanced Scorecard is prescriptive about this range, and about how one perspective defines the drivers of the next.

### **Financial Perspective**

The Balanced Scorecard encourages organisations to identify their specific financial objectives and link the corporate strategy to these objectives. The financial objectives serve as the focus for the objectives and measures of the other three perspectives.

Every measure should be part of a cause-and-effect relationship that culminates in improving long term sustainable financial performance. The Balanced Scorecard is an illustration of the strategy, starting with the long term financial objectives and then linking them to the customer focused initiatives, internal operational processes and investments in employees and systems that combine to produce the desired economic performance.

Clearly it is important to get the 'right' measures. For although it is peoples decisions and actions that change performance, measures set the goal, and the old adage "you get what you measure" is still true today.

Leading organisations are now finding new financial measures, as well as the non-financial measures.

Rather than simply considering the obvious financial measures of revenue, profit, share value or dividend cover, consideration is being given to a recently developed measure: Economic Value Added. This expresses the amount of value added by the efforts of the organisation. It also takes into account the value that could otherwise be earned, without risk, by the owners capital being deployed, for example, in gilts.

What is also then of leading consideration is what phase the business is in, start-up, investment, growth, harvest or managed decline. The owners financial strategy, should be matched by the choice of measure and target.

### **Customer Perspective**

The driver of financial success, except in a few rare cases, is customer satisfaction. Satisfied customers mean retained customers, and referrals and new business.

How an organisation performs from its customers' point of view is clearly a top priority for management. It is important however to focus again on the right type of satisfaction, and particularly, whose satisfaction.

All businesses have their best customers, the ones that deliver the maximum contribution to the specific type of financial measure which matters most to them. All businesses also have their average customers, and also the customers whose money they just can not turn away, but in reality cost the business too much to service, are perhaps never quite satisfied, and frankly, the business would be better off without.

To maximise financial return then it is the customer satisfaction of the 'target' customer profile which should be addressed. Customer satisfaction measures that reflect the issues that really matter to these customers need to be developed. From these, the key objectives, and measures, for what the company does can be established.

In this way an even more powerful link can be established between customer focused objectives and improved financial performance.

Research indicates that by increasing sales volume by 1% with a corresponding increase in prices, an improvement in profitability of nearly 15% could be achieved in a typical FT-SE 100 company.

### **Internal Operations Perspective**

Delivering customer satisfaction is achieved through the operational activities of the company. Through the Balanced Scorecard framework customer focused measures can be supported by measures of the internal processes that are most critical in meeting the target customers' expectations. The objectives and measures for this perspective thus enable a focus on maintaining and improving performance of those processes that deliver the objectives established as key to satisfying customers, which in turn satisfy shareholders.

With this approach, the Balanced Scorecard offers a vehicle to focus on a complete value chain of integrated business processes rather than just measuring performance within departmental structures. It is this that represents one of the major opportunities for benefits that the Balanced Scorecard can provide over traditional departmental performance measurement systems.

This top-down value-chain process can reveal entirely new areas within the business processes where an organisation can gain advantage.

The effect can be phenomenal; a reduction in process costs of 1% when combined with an identical reduction in wastage can typically deliver an increase in profits of over 15%.

### **Innovation and Learning Perspective**

The adage 'our people are our greatest asset' has been honoured more in the breach than the observance in all too many organisations. It is an issue that managers cannot afford to ignore, however. The operations of the organisation are undertaken by the people within it. The ability, flexibility and motivation of staff underpins all of the financial results, customer satisfaction and operational activities measured in the other quadrants of the Scorecard.

Customer expectations are constantly changing and organisations are, as a consequence, required to make continuous improvement. This relies heavily on an organisation's ability to innovate, learn and improve at an individual level, which collectively delivers the result for the whole organisation.

That everything else eventually depends upon the staff of an organisation could suggest that the ultimate single indicator of long terms sustainable success, if there were such a thing, would be the speed at which the organisation can learn to do new things successfully.

Used in this way the Balanced Scorecard framework gives consideration to the importance of investing for the future not just in traditional areas of investment such as equipment and R&D but in the human infrastructure of the organisation - creating a 'learning organisation' - if ambitious long term financial success objectives are to be achieved.

And there is no doubt that the effective development of staff can also have a direct impact on the bottom line. As well as underpinning all of the increases in profit possible through customer and operational improvements, simply increasing staff efficiency by 1% can often have the effect of improving profitability by twice as much.

### **Linking the Balanced Scorecard to Strategy**

The objective of any measurement system should be to motivate managers and staff to implement the organisation's strategy. By translating strategy into measures within the Balanced Scorecard, objectives and targets can be communicated to everyone. They can then focus on the critical drivers and align initiatives and actions to the meeting of strategic goals.

Why is it important for a Scorecard to communicate the strategy?

- It describes the corporate vision to the whole organisation
- It ensures that the meeting of performance targets contributes to achieving strategic objectives
- It focuses effort on the key objectives and measures

How can we build a Scorecard that translates a strategy into action?

- By establishing cause-and-effect relationships between measures e.g. increased training on products knowledge improves pre-sales support and matching with customer needs, which in turn leads to both higher revenue and fewer disappointed customers, driving increased profitability
- By creating a framework against which underpinning objectives and actions can be assessed, valued and prioritised

- By ensuring that cause-and-effect paths link through to on-going financial strength

An effective Scorecard enables an organisation's strategy to be inferred simply from the cause-and-effect links between measures. Outcome measures signal the ultimate objectives of the strategy and performance drivers indicate actions or initiatives that are required in order to create future value. Ultimately, though, the Scorecard retains a strong emphasis on outcomes, and financial outcomes in particular.

### **Benefits of the Balanced Scorecard**

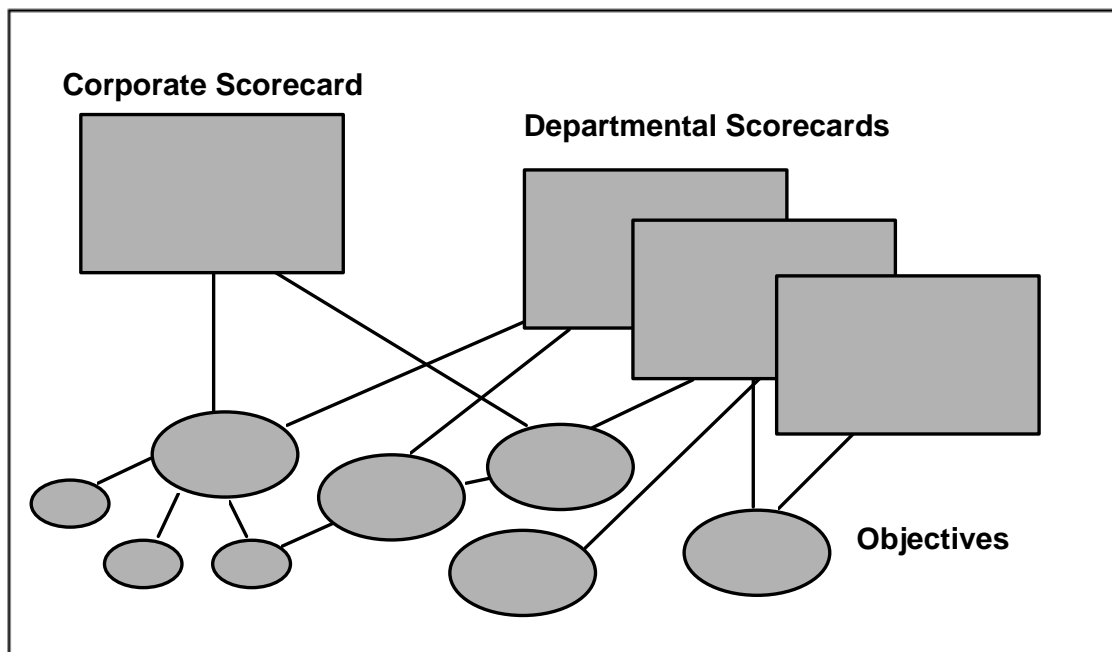
The Balanced Scorecard's prescriptive approach to performance measurement requires performance measures defined in each of the three non-financial perspectives to be linked to each other and to the financial measures, ensuring that the organisation's ultimate goal: that of continuing to be successfully in existence, remains paramount.

The extent to which business results can be improved by decisions taken based on a Balanced Scorecard view of the organisation is significant. Furthermore, these business results tend to be very sensitive to minor improvements in performance in key areas.

The table following illustrates the point.

Balanced Scorecard Perspective	Potential Impact	Typical Profit Impact(*)
Customer	1% increase in prices	11.4%
	1% increase in business volume	3.5%
Internal Business	1% reduction in costs	7.9%
	1% reduction in wastage	7.9%
Innovation and Learning	1% reduction in payroll costs	1.9%
	1% improvement in efficiency	1.9%
<b>TOTAL</b>		<b>34.5%</b>

(\*) Based on a typical FT-SE 100 company.  
Derived from *Business Excellence, IoD, 1997*



*Integrated Balanced Scorecards with Underpinning Initiatives and Objectives*

### ***Extending the Balanced Scorecard Approach***

Scorecards work well at the corporate, divisional and business unit level, although different measures will matter to different entities.

At the departmental or functional level, care must be taken to ensure that they do not become a means of confirming “functional silos”. As more and more emphasis is rightly placed upon processes and value chains, it may be counter productive to focus measurement within an individual function. Mitigating this effect can be achieved by also establishing measures that link that function with process value chains, or ensuring there is strong association with both the functional scorecard and the corporate scorecard where there is a strong process related element, or making use of another process oriented measurement system at the same time. For example some leading UK organisations combine the use of the Balanced Scorecard with the Business Excellence Model which has a high degree of focus on process.

### ***Team and Personal Scorecards***

Implementing the scorecard at the team and individual level can be problematic: individual roles may not have measures that correspond readily to all of the perspectives of the Scorecard, and trying to force a match may lead to unnecessary measurement for measurement’s sake. When this happens it can also undermine the perceived strength of the strategic value of the Scorecard framework.

In these instances it may be more beneficial in practice to identify the cascaded and required dependency objectives driving the measures in each scorecard perspective and have individuals relate to the key performance measures of achieving those particular objectives. For each objective the measures may, or may not, fit into each of the four Scorecard segments.

### ***Information Systems to Support the Balanced Scorecard***

Information systems play an invaluable part in assisting managers to analyse beyond the summary level Balanced Scorecard measures.

When an unexpected signal appears on the Balanced Scorecard, managers need access to underlying data to investigate the cause of any problem or to analyse trends and correlation.

If the information system is unresponsive, however, it can significantly impact the effectiveness of performance measurement.

Such an information system must, therefore, incorporate all of the following features:

- At-a-glance exception alerting
- Rapid access to summarised data
- Drill down to successive levels of detail
- Easy to follow dependency paths to identify the causes of performance other than drill-down
- Reporting of initiative, objective and process information including responsible owner, team members, and definitions as well as current status
- Reporting of impacts of underlying objectives upon scorecard measures
- Reporting of the impacts of objectives upon each other
- Graphical creation and modification of objectives, measures and relationships
- Support for dynamic re-planning for change
- Integration with office tools
- Inclusion of rich text information
- Graphical trending and tabular representation of data
- End user configuration and analysis options
- Integration with existing corporate data sources - with support for additional direct entry of values and annotations

INPHASE *PerformancePlus™* provides these facilities. *PerformancePlus™* is specifically designed to support the implementation and ongoing evolution of a Balanced Scorecard measurement system, alone or integrated with other performance management approaches and initiatives, such as business planning, team and individual objectives setting, organisational and personal development, process review and change initiatives.

INPHASE offer expert consultancy for strategy, training, implementation or skills transfer to your own internal or external consultants.

The *PerformancePlus™* approach to performance management and the Balanced Scorecard has been designed to enable managers to put into every day use the best practice recommendations that in the past may have seemed impossible to achieve, with minimal additional overhead of time and resource.

By creating a single, unified model, in which information about performance can be explored from many perspectives and shared throughout the organisation, *PerformancePlus™* can maximise the benefits to be attained from the effort that an organisation already puts into performance measurement and management.

The Balanced Scorecard, with a comprehensive information system to support it, provides a means to make a real difference throughout the organisation from individual employee satisfaction right through to significant improvements in the bottom line.

For further details and local support information call

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