Excellence in Financial Management

Course 11: The Balanced Scorecard

Prepared by: Matt H. Evans, CPA, CMA, CFM

This course provides a step-by-step guide on how to build a Balanced Scorecard. An understanding of strategic planning is recommended prior to taking this course. Refer to Course 10 on strategic planning. This course is recommended for 2 hours of Continuing Professional Education. In order to receive credit, you will need to pass a multiple-choice exam which is administered by installing the exe file version of this short course. The exe file can be downloaded from www.exinfm.com/training

NOTE: This short course includes the following supplemental materials:
- *Excel Templates: Set of basic templates for building the Balanced Scorecard*
- *PowerPoint presentation: Outlines overall development steps*
- *Case Study: Short case study on the Balanced Scorecard at UNUM Corporation*

Supplemental materials are posted on the internet at www.exinfm.com/training

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Chapter
1

Basic Concepts

Accountants communicate with financial statements. Engineers communicate with as-built drawings. Architects communicate with physical models. It seems that almost every profession has some means of communicating clearly to the end user. However, for people engaged in strategic planning there has been an on-going dilemma. The finished product, the strategic plan, has not communicated and reached the end user. Sure strategic plans are nice to look at, full of bar charts, nice covers, well written, and professionally prepared; but they simply have not impacted the people who must execute the strategic plan. The end result has been poor execution of the strategic plan throughout the entire organization. And the sad fact of the matter is that execution of the strategic plan is everybody's business, not just upper level management. Upper level management creates the strategy, but execution takes place from the bottom up.

So why do strategic plans fail? According to the Balanced Scorecard Collaborative, there are four barriers to strategic implementation:

1. Vision Barrier – No one in the organization understands the strategies of the organization.
2. People Barrier – Most people have objectives that are not linked to the strategy of the organization.
3. Resource Barrier – Time, energy, and money are not allocated to those things that are critical to the organization. For example, budgets are not linked to strategy, resulting in wasted resources.
4. Management Barrier – Management spends too little time on strategy and too much time on short-term tactical decision-making.

> Only 5% of the workforce understands their company strategy.
> Only 25% of managers have incentives linked to strategy.
> 60% of organizations don't link budgets to strategy.
> 86% of executive teams spend less than one hour per month discussing strategy.
>
> *– Balanced Scorecard Collaborative*

Therefore, we need a new way of communicating strategy to the end-user. Enter the Balanced Scorecard. At long last, strategic planners now have a crisp and clear way of communicating strategy. With balanced scorecards, strategy reaches everyone in a language that makes sense. When strategy is expressed in terms of measurements and targets, the employee can relate to what must happen. This leads to much better execution of strategy.

Not only does the Balanced Scorecard transform how the strategic plan is expressed, but it also pulls everything together. This is the so-called “cause and effect” relationship or linking of all elements together. For example, if you want strong financial results, you must have great customer service. If you want great customer service, you must have excellent processes in place (such as Customer Relations Management). If you want great processes, you must have the right people, knowledge, and systems (intellectual capital).

In the past, many components for implementing a strategic plan have been managed separately, not collectively within one overall management system. As a result, everything has moved in different directions, leading to poor execution of the strategic plan. Like a marching band, everyone needs to move in lockstep behind one overall strategy.

Therefore, you should think of the Balanced Scorecard as a management system, not just another performance measurement program. And since strategy is at the center of value-creation for the organization, the Balanced Scorecard has become a critical management system for any organization. In 1997, Harvard Business Review called the Balanced Scorecard one of the most significant business developments of the previous 75 years.

Balanced Scorecards provide the framework around which an organization changes through the execution of its strategy. This is accomplished by linking everything together. This is what makes the Balanced Scorecard so different; it captures the cause and effect relationship throughout every part of the organization. In the case of Mobil Oil, the truck driver pulls a balanced scorecard off the visor in his cab, outlining the five things he must do as a truck driver. Like a laser beam, strategy now has a clear path to everyone in the organization.

> Balanced Scorecards tell you the knowledge, skills and systems that your employees will need (learning and growth) to innovate and build the right strategic capabilities and efficiencies (internal processes) that deliver specific value to the market (customer) which will eventually lead to higher shareholder value (financial).
>
> *– “Having Trouble with Your Strategy? Then Map It” by Robert S. Kaplan and David P. Norton - Harvard Business Review*

Terminology

Throughout the entire process of building and implementing a balanced scorecard, we all need to speak the same language. Therefore, the first thing to get out of the way is to understand a few terms:

Cause Effect Relationship: The natural flow of business performance from a lower level to an upper level within or between perspectives. For example, training employees on customer relation's leads to better customer service which in turn leads to improved financial results. One side is the leader or driver, producing an end result or effect on the other side.

Goal: An overall achievement that is considered critical to the future success of the organization Goals express where the organization wants to be.

Measurement: A way of monitoring and tracking the progress of strategic objectives. Measurements can be leading indicators of performance (leads to an end result) or lagging indicators (the end results).

Objective: What specifically must be done to execute the strategy; i.e. what is critical to the future success of our strategy? What the organization must do to reach its goals!

Perspectives: Four or five different views of what drives the organization. Perspectives provide a framework for measurement. The four most common perspectives are: Financial (final outcomes), Customer, Internal Processes, and Learning & Growth.

Programs: Major initiatives or projects that must be undertaken in order to meet one or more strategic objectives.

Strategic Area: A major strategic thrust for the organization, such as maximizing shareholder value or improving the efficiency of operations. Strategic areas define the scope for building the balanced scorecard system.

Strategic Grid: A logical framework for organizing a collection of strategic objectives over four or more perspectives. Everything is linked to capture a cause and effect relationship. Strategic grids are the foundation for building the Balanced Scorecard.

Strategic Model: The combination of all strategic objectives over a strategic grid, well connected and complete, providing one single model or structure for managing the strategic area.

Strategy: An expression of what the organization must do to get from one reference point to another reference point. Strategy is often expressed in terms of a mission statement, vision, goals, and objectives. Strategy is usually developed at the top levels of the organization, but executed by lower levels within the organization.

Target: An expected level of performance or improvement required in the future.

Templates: Visual tools for assisting people with building a balanced scorecard, typically used for capturing and comparing data within the four components of the Balanced Scorecard: Strategic Grids, Measurements, Targets, and Programs.

Vision: An overall statement of how the organization wants to be perceived over the long-term (3 to 5 years).

Overall Process

Now that you understand the purpose and terminology behind the Balanced Scorecard, let’s describe the overall process on how we will build the Balanced Scorecard. The process consists of seven steps over three phases:

Phase I: The Strategic Foundation

Step 1: Communicate and align the organization around a clear and concise strategy. This is the fundamental starting point behind everything else. Your strategy is what “feeds” the Balanced Scorecard.

Step 2: Determine the major strategic areas or scope for getting the organization focused on those things the organization can actually do.

Step 3: Build a strategic grid for each major strategic area (step 2) of the business. Out of all the steps in the entire process, this can be the most difficult since we must take our entire strategy (step 1) and transform it into specific terms that everyone can understand. And everything must be linked to form one complete strategic model.

Phase II: Three Critical Components

Step 4: Establish Measurements: For each strategic objective on each strategic grid, there needs to be at least one measurement. Measurement provides the feedback on whether or not we are meeting our strategic objectives.

Step 5: Set Targets for each measurement: For each measurement in your scorecard, establish a corresponding target.

Step 6: Launch Programs: Things will not happen unless the organization undertakes formal programs, initiatives or projects. This effectively closes the loop and links us back to where we started – driving the strategy that was formulated in phase I.

Phase III: Deployment

Step 7: Once the Balanced Scorecard has been built, you need to push the entire process into other parts of the organization until you construct a single coherent management system. This pulls everything together, allowing successful execution of your strategy.

Don’t worry if all of this doesn’t make sense yet! The remainder of this short course will describe in detail each of the steps outlined above. Once you have completed this short course, you should have a solid understanding of what is required for building a great balanced scorecard.

Chapter

2

Phase I: The Strategic Foundation

When balanced scorecards were first introduced, it seems that everyone rushed to put a whole new set of measurements in place. However, this is **not** how to build a balanced scorecard. Strategizing is critically important to building a good balanced scorecard. In fact, it is so important that the authors of the book, The Balanced Scorecard, Robert S. Kaplan and David P. Norton, released a follow-up book titled: The Strategy Focused Organization. Therefore, we need to focus on building a strategic foundation, culminating with a set of strategic grids or maps. This is the watershed event within the entire process! The combination of strategic grids, measurements, targets and programs represent the four key components that makeup the Balanced Scorecard. All of these components will be described in detail as we work our way through the seven step / three phase process.

> When designing a balanced scorecard, we always start by asking: "What is your strategy?" Once we understand the strategy, we can build a new framework for describing the strategy, which we call a strategy map.
>
> – *The Strategy Focused Organization by Robert S. Kaplan & David P. Norton*

Step 1: Strategic Alignment

So let's get started with step one; namely by establishing our strategy for driving the rest of the process. If you took course 10 (and I am assuming you did), then you already have an understanding of how to construct a strategic plan. However, we want to make sure that we have a crystal clear and sharp strategic plan for feeding our balanced scorecard. A clear strategy requires two things: Specific objectives that tell people what to do and a set of targets for communicating what is expected.

Objectives need to communicate the action people must undertake. As strategy guru Michael Porter of Harvard University points out – "The essence of strategy is in the activities, choosing to perform activities differently or to perform different activities than rivals." We must define what these activities are if we expect to have a clear and sharp strategy.

Exhibit 1: Strategic objectives expressed in relation to action and activities

Three examples of strategic objectives
Over the next six months, delivery times will decrease by 15% through more localized distribution centers.
By the year 2003, customer turnover will decline by 30% through newly created customer service representatives and pro-active customer maintenance procedures.
Operating downtimes will get cut in half by cross training front line personnel and combining all four operating departments into one single service center.

The second key ingredients for a clear strategy are targets. Targets put teeth into a strategy by imposing criteria that the organization must achieve. For example, the strategy needs to be clarified by defining market share, revenue growth, new products introduced, and other specifics that set forth the end results of our strategy. In order to have targets, we need measurements. Since both targets and measurements are critical components of the Balanced Scorecard, we will defer discussion of targets and measurements until we get into the design phase (phase II). However, suffice it to say that if you have measurements and targets as components of your strategy, then building the Balanced Scorecard will be much easier.

Once you have defined a clear strategy (objectives and targets), then you must rally the organization around it. This requires a major communication initiative. A good starting point is to develop a communication plan. A communication plan outlines how you will communicate the strategy to each stakeholder group:

Exhibit 2: Basic Communication Plan

Stakeholder Group	Form of Communication
Shareholders	**Press Conference**
Division Managers	**Management Retreat / Presentation**
District Managers	**Site to Site Visits / Handouts**
Operating Staff	**Site to Site Visits / Handouts**
Administrative Staff	**Site to Site Visits / Handouts**
Suppliers	**Personal Contact / Mailing**
Distributors	**Personal Contact**

Effective communication is the Achilles Heel in this entire process. Therefore, extensive and continuous communication is vital to getting the organization aligned around its strategy.

> "I sure wish I'd done a better job of communicating with GM people. I'd do that differently a second time around and make sure they understand and shared my vision for the company. Then they would know why I was tearing the place up, taking out whole divisions, changing our whole production structure . . . I never got this across."
>
> *Roger Smith, CEO of General Motors*
> *– Strategic Choices by Kenneth Primozic, Edward Primozic, and Joe Leben*

Finally, you need to align and re-configure the various parts of the organization around the strategy. This may require changes to the organizational structure, selling off assets, making sure you have a "productive" culture, and other significant changes. Strategy is about closing the gaps between the present position of the organization and where the organization wants to be. Therefore, you must make changes to the organization if you expect success with your strategy.

Once the organization is set around its strategy, then and only then can you begin building the balanced scorecard system. In the case of Mobil Oil, it took over one year to create the right number of operating divisions around its new strategy.

> "One of the mistakes companies make is coming up with a list of measures of what they could measure instead of what they should be measuring. If a company thinks about what it needs to achieve to be successful in the eyes of its shareholders, clients and internal stakeholders, that will yield operational activities that the organization needs to do well to achieve those strategies."
>
> *Vicki Elliott, Principal, William M. Mercer*
> *"Putting the Scorecard to Work" – Business Finance Magazine*

Step 2: Strategic Areas

Before we start designing the Balanced Scorecard, we need a "fence line" of strategic areas. This restricts the organization to a selected area for achieving strategic success; otherwise the organization may find itself trying to do too many things. Strategy is about choices and making decisions on those things the organization can do vs. those things the organization cannot do. Or to put it another way: A few successes are better than a lot of failures.

Therefore, the strategic thrust of the organization needs to be confined to a few major areas. This will provide the "scope" we need for building a set of balanced scorecards. For most organizations, the strategic thrust of the organization will revolve around stakeholder groups; such as customers, shareholders, and employees. For example, most publicly traded corporations will have "shareholder value" as a major strategic area. This becomes one of the strategic areas for building the Balanced Scorecard. Additionally, each strategic area will flow across all four perspectives of the Balanced Scorecard: Financial, Customer, Internal Processes, and Learning and Growth. The following exhibit illustrates how shareholder value flows up across the four perspectives of the Balanced Scorecard:

Exhibit 3: Basic flow of Strategic Area within the Balanced Scorecard

Shareholder Value	
Financial	**Revenue Growth**
Customer	**More Customers**
Processes	**Customer Marketing & Service Programs**
Learning	**Support Systems & Personnel**

Notice how each lower perspective layer supports and enables the upper perspective layer; such as More Customers will enable Revenue Growth. Keep in mind that we are trying to link everything together. This is critical to building a great balanced scorecard; i.e. capturing the cause effect relationship.

Collectively, we want to limit our strategic areas to no more than five areas. This helps ensure successful implementation of our strategy. Some common strategic areas are: Customer Service, Shareholder Value, Operational Efficiency, Product Innovation, and Social Responsibility. We can refer to our strategic goals (created from our strategy in phase I) to help us isolate our strategic areas. The following exhibit illustrates how a strategic goal leads us into a strategic area:

Exhibit 4: Example of linking a strategic goal to a strategic area

Strategic Goal =>	**By the year 2005, our company will have the most innovative product line of hand held computers**
	▼
Strategic Area =>	**Product Innovation**

Finally, there is the possibility that one strategic area may conflict with another. For example, Operational Efficiency may require cost reductions while Market Share may require more expenses. If such conflicts do exist, make sure all stakeholders involved are fully aware of these conflicting areas and how they fit within your strategic plan.

Step 3: Strategic Grids

Now that we have a strategy in place (step 1) and now that we have defined our strategic areas or scope (step 2), we will translate the specifics of our strategy into a set of grids. As you may recall, we noted that balanced scorecards are structured over four perspectives or layers: Financial, Customer, Internal Processes, and Learning and Growth. Strategic grids include these four layers. Within each layer, we will place our strategic objectives, making sure everything links back. Trying to develop strategic objectives and placing them into the correct layers for all strategic grids is probably the most difficult step in building the Balanced Scorecard. Consultants sometimes refer to this step as straw modeling; trying to string connecting lines over a map that presents an overall strategic model.

Building a strategic grid starts at the very top – strategic goals and areas. As we indicated earlier, most publicly traded companies have shareholder value as a strategic area. In order to improve shareholder value, the organization can do things like grow revenues or increase operating performance. Once you decide on your strategy for improving shareholder value, then you have to decide on how you will grow revenues or improve operating performance. The following exhibit illustrates this bottom up flow within the Financial Perspective:

Exhibit 5: Flowing strategic objectives within the Financial Perspective

Shareholder Value			
Grow Revenues ↑		↑ Operating Improvements	
↑ New Sources of Revenues	↑ Increase Customer Profitability	↑ Lower Costs	↑ High Utilization of Assets

We will flow our strategic objectives down each perspective within a grid of boxes, making sure everything is linked. This grid will serve as the foundation for constructing the Balanced Scorecard.

Next, we move down to the Customer Perspective. In order to construct the customer perspective, we need to understand the value(s) we provide to our customers. For example, Federal Express is extremely efficient in getting packages delivered on time. Therefore, on time delivery is the specific value that Federal Express delivers to its customers. Companies that emphasize operational efficiency usually provide certain value attributes, such as competitive pricing, on-time delivery, or superb quality. Other companies may create value for customers through their great relationship with the customer. Finally, some companies may add value by emphasizing innovative and unique products and / or services. It is extremely important to define your customer and the values you provide; otherwise you run the risk of building a scorecard that doesn't fit with the capabilities of the organization.

Once you have clearly defined your customer values, you can define strategic objectives within the Customer Perspective, linking these objectives to the financial perspective objectives. For example, suppose we have a strategic goal that stipulates that our company will be the price leader in long distance phone service. We can flow this goal within the scorecard grid as follows:

Exhibit 6: Linking customer objectives to financial objectives

Financial	**Shareholder Value**
	↑ Grow Revenues
Customer	**↑ Acquire More Customers**
	↑ Leader in Pricing

Notice how "Leader in Pricing" is the driver behind acquiring more customers. In turn, more customers will flow up to the next layer of growing revenues. And growing revenues is our strategy for meeting our strategic thrust or area of creating shareholder value.

Next, we need to ask the question: How will we become a leader in competitive pricing for attracting new customers? This brings us down to the next perspective: Internal Processes. Internal Processes represent the collection of activities that give a company a competitive advantage in the marketplace.

Referring back to the Customer Perspective, we could choose between three strategies:

1. Operational Efficiency – Value for customers through competitive pricing, superior quality, on-time delivery or diverse product lines.
2. Customer Relationships – Value for customers through personal service, building trust, brand loyalty, providing customized solutions, and other one-to-one relationships.
3. Innovative Products & Services – Inventing new products and features, fast delivery of products and services, forming partnerships to expand product lines, and other product leadership initiatives.

If we go back to our example on price leadership in long distance phone service, we need to emphasize operational efficiency within our strategy since this will enable competitive pricing. Next, the company must define its strategic objectives for operational efficiency (which leads to competitive pricing). This can include numerous objectives: Supply chain management, cycle time improvements, cost reduction programs, and any objective aimed at operational excellence. Once we decide on objectives, we can extend our strategic grid down into the next perspective as follows:

Exhibit 7: Linking objectives down to Internal Processes

Financial	**Shareholder Value**		
	Grow Revenues		
Customer	**Acquire More Customers**		
	Become the Price Leader		
Internal Processes	**Improve Operational Efficiency**		
	Cost Reduction Program	**Knowledge Based System**	**Reduce Non Core Activities**

This brings us to the final perspective, Learning and Growth. Learning and Growth is the foundation that enables us to deliver on strategic objectives defined in the Internal Processes Perspective. Like the other perspectives, we need to look at different strategies that fit with our current strategic grid:

1. Competencies – Skills and knowledge of the work force.
2. Technologies – Applications and systems for execution of internal processes.
3. Change Culture – Organizational alignment, employee motivation, executive leadership, communication, and other qualities of empowering the organization.

If we go back to our strategic grid (Exhibit 7), we must decide on what strategic objectives are required for meeting the three objectives defined in the Internal Processes Perspective. Therefore, we can extend our grid as follows:

Exhibit 8: Strategic objectives defined for all four perspectives

Financial	**Shareholder Value**		
	Grow Revenues		
Customer	**Acquire More Customers**		
	Become the Price Leader		
Internal Processes	**Improve Operational Efficiency**		
	Cost Reduction Program	**Knowledge Based System**	**Reduce Non Core Activities**
Learning and Growth	**Training - Best practices in cost management**	**Database network on operational performance**	**Re-align organization with core competencies**

Once you have completed the strategic grid, go back and make sure everything fits with your overall strategy. A set of strategic grids should provide the strategic model for running the business, outlining the specifics of the strategy. All stakeholders should be able to look at your grids and follow the flow of your strategy. Don't forget that you are trying to limit your objectives (and grids) to a critical few strategic areas. If possible, keep the total number of objectives on the grid to no more than 20 to 25 objectives.

We have completed the foundation of the Balanced Scorecard, a set of strategic grids for each strategic area that captures and links objectives across four or more perspectives. We can now move forward and populate each grid with: Measurements, Targets, and Programs.

Exhibit 9: Summarize Phase I

Five Major Milestones – Phase I	
1st	**Establish a clear strategy (objectives & targets)**
2nd	**Communicate the strategy**
3rd	**Align the organization around the strategy**
4th	**Limit the strategic areas to no more than five**
5th	**Link strategic objectives into grids across four perspectives**

Chapter

3

Phase II: Three Critical Components

Once we have completed the strategic foundation (phase I), we are set to measure our objectives, establish a target for each measurement, and initiate programs that will make all of this happen. This will effectively complete the building of the Balanced Scorecard.

Step 4: Measurements

For each strategic objective on your strategic grid, you need at least one measurement. If you have several measurements for a strategic objective, then chances are you have more than one strategic objective. Can you have an objective without a measurement? Yes, it is possible, but not having a measurement makes it difficult to manage the objective. It's best to revisit this objective and ask the question: Why is this an objective?

Measurement allows us to quantify our strategic objectives, asking the question: How well are we doing? So how do you build your measurements? Here are some basic guidelines:

Linked: Measurements communicate what is strategically important by linking back to your strategic objectives.
Repeatable: Measurements are continuous over time, allowing comparisons.
Leading: Measurements can be used for establishing targets, leading to future performance.
Accountable: Measurements are reliable, verifiable, and accurate.
Available: Measurements can be derived when they are needed.

The following template can be used to help build an appropriate measurement:

Exhibit 10: Measurement Template

Strategic Objective =>	
Describe the Measurement =>	
Define Type / Formula =>	
Unit of Measurement =>	
Frequency of Measurement =>	
Assumptions =>	
Sources =>	
Availability =>	**___ Available ___ Not Available ___ Requires Change**
Support Required =>	**___ IT Support ___ Finance Support ___ Other**

In addition to the above criteria, you need to understand some concepts related to measurement. For example, some measurements will lead to change in your organization. These types of measurements are called leading indicators since they drive or push final outcomes within the organization. Examples include customer contracts executed, competitive pricing index, employee feedback indicator, service response time, and time spent with customers. If your organization needs to change rapidly, then you need to include some leading type measurements into your balanced scorecard. A common place to use leading measurements is within the Learning and Growth perspective since this is the principal "driver" perspective behind the Balanced Scorecard.

The other side of measurement is looking back, historical type measurements that show us a final outcome or result. These measurements are referred to as lagging indicators and they dominate most performance measurement systems. About 70% of all measurements tend to fall into this category. Examples include most financial type measurements (return on equity, sales growth, economic value added, etc.) and many non-financial type measurements (production breakeven, customer retention, employee productivity index, etc.). Lagging type measurements are common within the Customer and Financial perspectives since these are outcome related.

Almost half of your measurements can be extrapolated from existing systems and procedures. Some common type measurements include ratios, percentages, rankings, and indexes. Ratios are good for expressing critical relationships while percentages are good for expressing an overall trend over time. Rankings work well for highly ranked companies trying to move up in the ranking. However, lower ranked companies usually cannot move easily within a ranking system and therefore, this form of measurement may be too ambitious.

Another way to look at measurement is to understand the relationship between leading and lagging indicators for the three lower perspectives.[1] For example, the Customer Perspective can be broken down into two groups of measurement: Lagging Indicators such as customer satisfaction, retention, and market share; and Leading Indicators such as competitive pricing, excellent quality, outstanding reputation, image, and customer relationships. For example, in order to retain customers, we must provide one or more value attributes to the customer.

Exhibit 11: Cause Effect Relationship between Leading and Lagging Indicators

<table>
<tr><th rowspan="4">Customer Perspective</th><th colspan="5">Lagging Indicators are desired results:</th></tr>
<tr><td colspan="5">Customer Satisfaction   Customer Retention   Market Share</td></tr>
<tr><th colspan="5">Leading Indicators – Value Attributes to Customers:</th></tr>
<tr><td>Quality</td><td>Time</td><td>Price</td><td>Image</td><td>Reputation</td></tr>
</table>

The Internal Process Perspective can be broken down into three result categories:

[1] These relationships are described in the book: The Discipline of Market Leaders by Michael Treacy and Fred Wiersema, Perseus Book Group.

- **Pre Delivery Results =>** Innovative Processes that meet customer needs, provide solutions, and address emerging trends. **Example of Leading Indicator =>** Number of new products introduced.
- **Delivery Results =>** Operations that produce and deliver products and services to customers. **Example of Leading Indicator =>** Delivery Response Time to Customer.
- **Post Delivery Results =>** Value added services provided to customers once products and / or services have been delivered. **Example of Leading Indicator =>** Cycle Time for Resolving Customer Complaint.

The Learning and Growth Perspective will emphasize three result categories: Employees, Systems, and Organization.

- **Results for Employees =>** Employee satisfaction, productivity, and retention. **Example of Leading Indicator =>** Percentage of Key Personnel Turnover.
- **System Results =>** Engaging to the end user, accessibility, and quality of information. **Example of Leading Indicator =>** Percentage of employees who have on-line access.
- **Results for the Organization =>** Climate for change, strong leadership, empowering the workforce, and other motivating factors. **Example of Leading Indicator =>** Number of Employee Suggestions.

One of the major challenges in building your balanced scorecard is to keep the number of measurements to a manageable few. Throughout building the balanced scorecard, we try to follow the "4 to 5 Rule." This rule says that we build balanced scorecards with four to five layers, four to five measurements per layer, resulting in no more than 20 to 25 measurements per scorecard (strategic grids). If you have too many measurements, you can index your measurements into one single measurement. For example, you can apply weighted percentages to calculate a single measurement.

Example of indexing a measurement:

Measurement Description	Value	Weighted Importance	Index
Customer Satisfaction Rating	.78	50%	.39
Customer Compliment Index	.89	25%	.22
Quality Satisfaction Indicator	.72	25%	.18
Single Measurement used in Balanced Scorecard			.79

However, indexing is a sword sharp at both ends. It helps reduce the number of measurements, but it also buries the results making it difficult to clearly see what is going on. The best approach is to use stand-alone measurements wherever possible.

One of the best benchmarks to apply to your measurements is to ask the following question: Can I understand your strategic objective by simply looking at your measurement? Keep in mind that you are trying to capture the best "cause and effect" relationship that you can. This is what makes a great balanced scorecard. For example, what does this measurement say: % sales growth. This measurement implies that we have a strategic objective that must be related to growing sales revenues. Suppose your strategic objective was not to increase sales revenues, but to increase return on shareholder equity. This changes your measurement to return on equity. Remember everything must be linked as you build your balanced scorecard.

Step 5: Targets

Measurement alone is not good enough. We must drive behavioral changes within the organization if we expect to execute strategy. This requires establishing a target for each measurement within the Balanced Scorecard. Targets are designed to stretch and push the organization in meeting its strategic objectives. For example, suppose the strategic objective is to improve customer satisfaction and the measurement is based on number of customer complaints. The average number of monthly complaints is 45 for the last 12 months. A target of no more than 40 complaints could be established.

Targets need to be realistic so that people feel comfortable about trying to execute on the target. Therefore, targets should be mutually agreed upon between management and the person held responsible for hitting the target. One good place to start in setting a target is to look at past performance. Past trends can be extended for modest improvement. Your strategic goals can also give you clues as to what your targets should be. Another good source for targets is benchmarking for best practices.

Exhibit 12: Setting targets based on strategic goals

Current Year Sales Revenues	Goal: We will grow sales by 40% over the next 3 years		
	Year 2002 Target	Year 2003 Target	Year 2004 Target
$ 160,000	$ 172,000	$ 195,000	$ 224,000

Make sure your targets match your measurements one to one, communicating what needs to change in relation to the measurement. Also be aware that targets may require considerable research. Finally, if past targets have not resulted in much change, then you should consider setting more aggressive targets.

Exhibit 13: Adding Measurements and Targets to the Balanced Scorecard

Perspectives	Objectives	Measurements	Targets 2002	Targets 2003
Financial	Maximum Returns	Return on Equity	12%	13%
	Utilization of Assets	Utilization Rates	7%	8%
	Revenue Growth	% Change in Revenues	+11%	+11%
Customer	Customer Retention	Retention %	75%	75%
	Customer Service	Survey Rating	85%	88%
	Customer Relations	% Self Initiated Calls	35%	40%
Internal Processes	Fast Delivery	Turnaround Time	15m	14m
	Effective Service	1st Time Resolvement	68%	69%
	Optimal Cost	% cost of sales	66%	64%
	Resource Utilization	Productivity Indicator	77%	80%
Learning & Growth	High Skill Levels	Skill set ratio	65%	68%
	Employee Satisfaction	Survey Index	75%	77%

	Outstanding Leaders	**5 point ranking**	**4.5**	**4.8**

Step 6: Programs

The final design step is to close the loop and put specific programs in place to make everything happen. This is perhaps the fun part in the entire process. How do we actually hit these targets and meet our strategic objectives? What major initiatives must the organization undertake to make all of this happen? Programs are the major projects that facilitate execution of everything downstream within the scorecard. Some typical examples of programs include quality improvement programs, marketing initiatives, enterprise resource planning, customer relation's management, and supply chain management.

Programs usually have certain characteristics:

- Sponsored by upper level management
- Utilizes designated leaders and cross-functional teams
- Consists of deliverables, milestones, and a timeline
- Requires resources (people, facilities, allocated budget, etc.)

Once programs have been established and sold to various stakeholders, they tend to add some degree of strategic value or impact. However, getting a major program initially launched can be difficult due to funding, apprehension, politics, and other obstacles. If existing programs lose funding, then you need to work back through your scorecard, adjusting your targets and making sure everything still fits.

One of the critical steps in selecting programs is to plot programs against all strategic objectives and assess the strategic impact. This can be extremely important since executive management will routinely demand cost reductions. You don't want to cut programs with the biggest strategic impact. This would undercut your ability in meeting strategic objectives. Programs with little or no strategic impact should get lowest priority within the organization.

Exhibit 14: Compare Programs with Strategic Objectives for Strategic Impact

Instructions: List all strategic objectives for each perspective in the Balanced Scorecard. Plot any program that helps achieve a strategic objective. **Programs** **Strategic Objectives**	Global Market Program	Leadership Building	Quality Control Review	IT Complaint Tracking	Prod Yield System	Asian Production Plant	Customer Management	Knowledge System	Community Awareness	Employee Rotation	Enterprise Planning
F1: Maximum Return on Equity											
F2: Positive Economic Value Added											
F3: 15% Revenue Growth											
F4: 5% Reduction in Production Cost			■		■						
C1: Secure 1% market share in Asia	■					■					
C2: Obtain competitive pricing			■								
C3: Develop new market partnerships	■										
C4: Integrate service process w/customer							■				
P1: Improve production workflows					■						
P2: Flawless manufacturing					■						
P3: Expand knowledge distribution								■			
P4: Integrate financial / production											■
P5: Link processes to customer inputs							■				
L1: Engage workforce into the business										■	
L2: Expand leadership capacities		■									
L3: Become a customer driven culture							■				

In the above example, notice that the Production Yield System and the Customer Management program impact three different strategic objectives while the IT Complaint Tracking program and the Community Awareness program fail to impact any strategic objective. Additionally, since the Financial Perspective is the final outcome, there are usually no programs associated with driving financial related strategic objectives.

Our balanced scorecard now has the final key component (programs). Referring back to Exhibit 13 we can supplement the scorecard with those programs that have been screened and selected for launch:

Exhibit 15: Supplement the Balanced Scorecard with Programs

Objectives	Measurements	Targets 2000	2001	Programs
Maximum Returns	Return on Equity	12%	13%	
Utilization of Assets	Utilization Rates	7%	8%	
Revenue Growth	% Change in Revenues	+11%	+11%	
Customer Retention	Retention %	75%	75%	Customer Relations Management (CRM)
Customer Service	Survey Rating	85%	88%	Customer Relations Management (CRM)
Customer Relations	% Self Initiated Calls	35%	40%	Customer Relations Management (CRM)
Fast Delivery	Turnaround Time	15m	14m	Cycle Process System
Effective Service	1st Time Resolvement	68%	69%	Customer Relations Management (CRM)
Optimal Cost	% cost of sales	66%	64%	Cycle Process System
Resource Utilization	Productivity Indicator	77%	80%	Cycle Process System
High Skill Levels	Skill set ratio	65%	68%	Open Corp University
Employee Satisfaction	Survey Index	75%	77%	Quality Time Initiative
Outstanding Leadership	5 point ranking	4.5	4.8	Special Training Program

Chapter
4

Phase III: Deployment

Once we have designed the Balanced Scorecard, we need to implement it throughout the entire organization. This requires careful planning and coordination with all parts of the organization. We should have learned several lessons from our first stage scorecard:

- How to organize and kick off the process
- How to coordinate and gain consensus
- How to identify the benefits and difficulties associated with the Balanced Scorecard
- An understanding of project deliverables

Also, we should have knowledge about what factors influence implementation of the Balanced Scorecard, such as:

- Time required to develop a balanced scorecard
- Availability of data and resources for building the Balanced Scorecard
- Degree of support from upper level management

The deployment phase will involve reviewing and aligning the first scorecard with other parts of the business (divisions, operating units, departments, etc.). We want to integrate the Corporate or Business Unit Scorecard into lower level scorecards. As we move the scorecard forward, a more formal collection and reporting system should emerge for the Balanced Scorecard. Once we get more and more scorecards working, we will begin to explore the possibility of linking compensation to the measurements within the Balanced Scorecard.

Since strategizing takes place at the upper level of the organization, one place to start building the Balanced Scorecard is at the corporate level. Once again, we can go back to our four to five rule: Build your scorecard at the upper layer of the organization, corporate; work your way down to the second layer, operating; then work your way down to shared service departments; next work your way down to the lowest levels such as department, teams, and individuals. By following this process, we ensure alignment.

However, most organizations elect to build their first scorecard at the strategic business unit level (such as operating units or divisions within the business). The reason is simple. You want to build a balanced scorecard that covers the entire value chain; i.e. customers, production, sales, innovation, and all elements that go into making a “complete” scorecard. Also, by letting other business units start the process, you may get stronger “buy in” to the Balanced Scorecard. For example, if executive management pushes the scorecard down to divisions, the divisions may see the scorecard as just another phony management program. By letting each division review the scorecard first and report back to executive management, the organization is better positioned for full-scale deployment of the Balanced Scorecard.

Best Practices

Balanced Scorecards often require continuous testing and modification to see if the technique really fits. This can be frustrating for executives who routinely expect perfect solutions right out-of-the-box. Keep in mind that you are testing something that has never been applied before and you must revisit the construction of your scorecard, adjusting and re-aligning it to fit with the organization. It is not unusual to postpone the rollout of additional scorecards for more than one year until the first scorecard is well established and working. Therefore, companies that have been successful with the Balanced Scorecard have a high tolerance for making change happen in a positive way. For example, linking part of employee compensation to the Balanced Scorecard should be postponed until such time as you have the correct set of measurements.

Some other attributes of companies that have been successful with the Balanced Scorecard include the following:

- A strong commitment from the top to the Balanced Scorecard.
- A process for transforming strategies into balanced scorecards.
- A cross-functional process for moving strategy down into the lower parts of the organization.
- Leveraging the Balanced Scorecard by using it with other processes and activities, such as budgeting, project management, and regular management meetings.

These principles are often cited as components for shifting the organization into a strategic mindset. And this is the ultimate goal behind implementation of the Balanced Scorecard. However, reaching this big “pay-off” is incredibly difficult for almost every organization since it means moving from a “strategic planning” organization to a “strategic thinking” organization. The following exhibit highlights the difference:

Exhibit 16: The ultimate payoff – going from strategic planning to strategic thinking

Strategic Planning	Strategic Thinking
A formal structured process of researching and analyzing the competition in an effort to identify strengths, weaknesses, opportunities, and threats.	**A natural and intuitive process of seeing through the competition, anticipating future trends, and comprehending future changes required for the organization.**

Since programs are the final component within our balanced scorecard and since programs require budgets, we need budgeting to follow right behind completion of the Balanced Scorecard. This extends linking to the next related activity. Therefore, linking budgeting to the Balanced Scorecard is another best practice. It’s worth noting that budgeting occurs at the tail end of the process and not at the beginning. For many organizations (especially government agencies), the reverse is often true. Budgeting drives decision-making and as a result, strategic implementation becomes exceedingly difficult.

Automation

Deploying a balanced scorecard is more about strategic alignment, communication, and change management. However, many organizations prefer to use a software application to help pull together the Balanced Scorecard. Unfortunately, most existing software applications cannot manage the information contained in the Balanced Scorecard. This is due to the fact that most systems are transaction oriented, such as Enterprise Resource Planning (ERP) programs. It is estimated that less than half of the information for feeding the scorecard can be derived from transaction-based systems, such as ERP systems. Most of the information is stand-alone, such as customer surveys, employee suggestions, and other independent sources. Therefore, full automation of the Balanced Scorecard can be somewhat of a challenge.

However, for companies seeking to deploy the Balanced Scorecard through automation, there are several advantages:

- Provides users with rapid access to exception alerts.
- Allows easy drill down to more details about measurements and targets.
- Easy to follow dependency paths show cause and effect relationships.
- Flexibility on making changes to the scorecard, including organizational changes.
- Graphical reporting of measurements and relationships.
- Facilitates control over who can see what within the scorecard system.
- Wide on-line distribution of company vision and strategy.
- Analysis of strategy on-line.
- Test relations against actual data for fine-tuning the scorecard.
- Integration with other desktop applications.
- Pre-defined templates and other applications make it easy to change and update different components of the scorecard.
- Drives rapid deployment of the scorecard with minimal manual effort.

Some of the “best of breed” applications for balanced scorecards include Gentia (www.gentia.com), Panorama Business Views (www.pbviews.com), and QPR Software (www.qprsoftware.com).

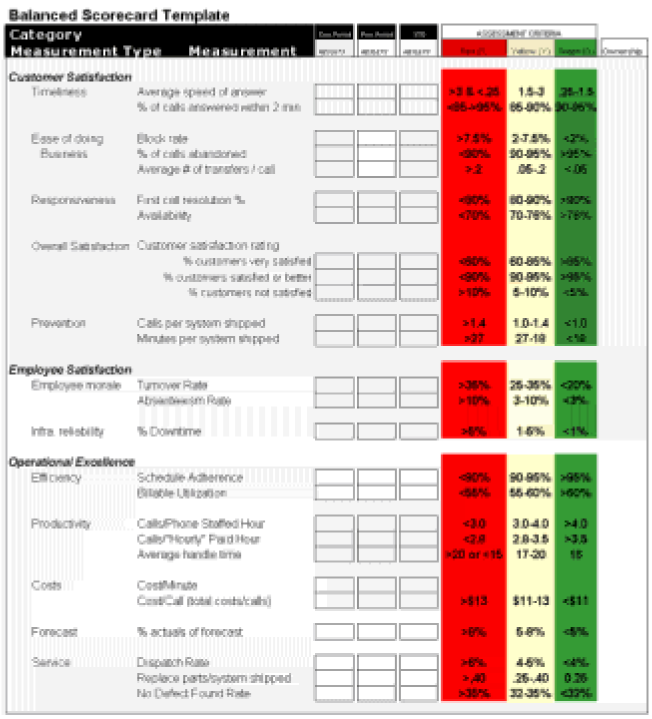
Cross Functional Team Approach

Since balanced scorecards cut across the entire organization, they are usually developed by cross-functional teams. The cross functional team consists of middle level management since they can serve as the bridge between the executive level where strategic thinking takes place and the lower levels where the strategy gets implemented. Obviously, we need executive management to sponsor the Balanced Scorecard and support the cross-functional team. And at the same time, we need feedback from lower levels of the organization, especially on the specifics of the scorecard. Managing teams is a big part of any balanced scorecard project since it touches all levels of the organization.

Cross Functional Development of the Balanced Scorecard		
Executive Level	**Middle Management**	**Lower Levels**
Sponsors the Balanced Scorecard, approves the final scorecard, and advocates the concept to other parts of the organization.	Manages the overall project, builds the scorecard, coordinates the process with other levels within the organization.	Delivers critical data used within the Balanced Scorecard, such as measurements.

Templates

One of the most common tools used for building balanced scorecards is the template. Templates are usually spreadsheets, organized to capture, compare, and report data used in constructing the Balanced Scorecard. If you refer back to many of the exhibits used in this short course, they represent very basic templates for organizing the data that makes up our balanced scorecard. For example, Exhibit 10 is a template for capturing attributes associated with measurement while Exhibit 14 was used to assess the impact of programs on strategic objectives. More formal templates can be used to actually report your balanced scorecard:



Balanced Scorecard Template

Category / Measurement Type	Measurement				Assessment criteria			Ownership
Customer Satisfaction								
Timeliness	Average speed of answer				>3 & <.25	1.5-3	.25-1.5	
	% of calls answered within 2 min				<85->95%	85-90%	90-95%	
Ease of doing Business	Block rate				>7.5%	2-7.5%	<2%	
	% of calls abandoned				<90%	90-95%	>95%	
	Average # of transfers / call				>.2	.05-.2	<.05	
Responsiveness	First call resolution %				<80%	80-90%	>90%	
	Availability				<70%	70-78%	>78%	
Overall Satisfaction	Customer satisfaction rating							
	% customers very satisfied				<60%	60-85%	>85%	
	% customers satisfied or better				<90%	90-95%	>95%	
	% customers not satisfied				>10%	5-10%	<5%	
Prevention	Calls per system shipped				>1.4	1.0-1.4	<1.0	
	Minutes per system shipped				>27	27-18	<18	
Employee Satisfaction								
Employee morale	Turnover Rate				>35%	25-35%	<20%	
	Absenteeism Rate				>10%	3-10%	<3%	
Infra. reliability	% Downtime				>6%	1-6%	<1%	
Operational Excellence								
Efficiency	Schedule Adherence				<90%	90-95%	>95%	
	Billable Utilization				<55%	55-60%	>60%	
Productivity	Calls/Phone Staffed Hour				<3.0	3.0-4.0	>4.0	
	Calls/"Hourly" Paid Hour				<2.8	2.8-3.5	>3.5	
	Average handle time				>20 or <15	17-20	15	
Costs	Cost/Minute							
	Cost/Call (total costs/calls)				>$13	$11-13	<$11	
Forecast	% actuals of forecast				>8%	5-8%	<5%	
Service	Dispatch Rate				>6%	4-6%	<4%	
	Replace parts/system shipped				>.40	.25-.40	0.25	
	No Defect Found Rate				>35%	32-35%	<32%	

Source: Service Zone Inc.

Other Organizations

Since balanced scorecards are an extension of strategy and since strategy is essential to all types of organizations, balanced scorecards are appropriate for any organization concerned about the execution of its strategy. For example, the City of Charlotte, North

Carolina decided to use the Balanced Scorecard as a framework for managing the city. The scorecard was built around five strategic areas:

- Community Safety
- Transportation
- City within City (preserve and improve older urban neighborhoods)
- Restructuring of Government
- Economic Development

Many of the reasons why government agencies (such as the City of Charlotte) turn to the Balanced Scorecard are quite similar to those reasons cited by businesses. For example, the City of Charlotte decided to meet new expectations of government by:

- Focusing more on customers
- Allowing decisions to be made through self-managed work teams
- Responding faster to changes in technology
- Solving problems through more innovative approaches
- Emphasizing leadership as opposed to traditional supervision
- Becoming more competitive with the private sector

These principles are not unlike any other business. Additionally, the City of Charlotte encountered common issues when implementing the Balanced Scorecard:

- Pilot scorecards were needed to help adjust the organization to the Balanced Scorecard and work out “bugs” in the process.
- The highest levels of government served as “champions” behind the Balanced Scorecard.
- All levels of the organization were involved since the Balanced Scorecard impacts everyone.
- Full-scale implementation required several years since the entire organization was shifted into a more “strategic” type organization.

Therefore, balanced scorecards are not limited to businesses since the fundamental issues associated with the Balanced Scorecard are almost identical to all types of organizations.

Additional Examples

Finally, here are four more examples of balanced scorecards (Objectives and Measurements):

Exhibit 17: Balanced Scorecard Example – Electronics Company

Electronics Company		
Customer	Quality	Number of Defects
	Price	Competitive Comparison
	Delivery	Number of On time Deliveries
	Shipments	Sales Growth
	New Products	Number of new products to support
	Support	Customer Satisfaction Survey
Internal	Efficiency in manufacturing	Cycle Time
	New product introductions	Rate of new introductions
	New product success	Number of orders
	Sales penetration	Actual vs. Plan
	New businesses	Number of new businesses each year
Inno-vation	Technology leadership	Product performance benchmarking
	Cost leadership	Quarterly Manufacturing Overhead
	Market leadership	Market share (all markets)
	Research & Development	Number of new products
Finan-cial	Sales	Annual growth rate
	Cost of Sales	Annual trend line
	Profitability	Return on capital employed
	Prosperity	Cash flows
Empl oyee	Competitive Salaries	Local area comparisons
	Opportunity	Satisfaction rating
	Citizenship	Contributions to community

Source: Applying the Balanced Scorecard to Small Companies by Chee W. Chow, Kamal M. Haddad, and James E. Williamson - Management Accounting, August 1997

Exhibit 18: Balanced Scorecard Example – Food Ingredients Company

Food Ingredients Company		
Financial	Capture additional industry growth	Comparison to industry growth
	Maintain base business / continue to be preferred supplier to customer	Volume trend line / gross margin
	Expand into global markets	Ratio of domestic to international sales
	Commercialize new ingredients and services that are profitable	Percent of sales from launched products / gross profit from new products
Custo-mer	Lowest cost supplier	Total cost relative to competition
	Products and services customized to meet local needs	% of products in R & D in test phase
	Customer satisfaction	Customer surveys

Internal	Maintain low cost base	Total cost relative to competition
	Maintain consistent production	First pass success rate
	Continue to improve distribution efficiency	Percent of perfect orders
	Build capability to screen profitable products and services	Change in economic value
	Integrate acquisitions	Revenues per salary dollar
Learning	Link strategy to reward system	Net income per dollar of variable pay
	Foster culture that supports innovation and growth	Annual assessments / Quarterly reviews
	Develop competencies critical to overall gaps that must be filled	Percentage of competency deployment filled on tracking matrix

Source: Applying the Balanced Scorecard to Small Companies by Chee W. Chow, Kamal M. Haddad, and James E. Williamson - Management Accounting, August 1997

Notice that some companies prefer to re-arrange their perspectives in order of what they consider most important to least important.

Exhibit 19: Balanced Scorecard Example – Commercial Bank

Commercial Bank		
Shareholder	Achieve returns of 1% on assets and 15% on equity	Net interest margin / non-interest expense
	Achieve efficiency ratio of 68%	Overhead expenses
	Achieve asset growth of 15%	Asset growth rate
	Loan loss rate of .5% or less	Number of problem loans
	Loan delinquencies of 2% or less	Number of bad loans made
Customer	High personal quality service	Number of complaints / customer satisfaction rating
	Competitive product offerings	Number of product offerings per year / Sales volumes
	Competitive pricing	Cost of doing business / competitive price comparisons
	Customer satisfaction	Customer surveys
Employee	Competitive compensation	Annual market review
	Participation in organization	Bonus pay per personal performance
	Enhance job skills	Training completed
	Quality evaluation of performance	Comparison to best standards
	Increased upward career movement	Number of internal promotions
Com-Munity	Provide community support activities	Extent of employee participation
	Act as a good corporate citizen	Extent employees vote / extent employees support outside activities

Source: Applying the Balanced Scorecard to Small Companies by Chee W. Chow, Kamal M. Haddad, and James E. Williamson - Management Accounting, August 1997

Exhibit 20: Balanced Scorecard Example – Biotechnology Company

Biotechnology Company		
Customer	New products	Percent of sales from new products
	Early purchase of seasonal products	Percent of sales by early purchase date
	Accuracy in invoicing	Percent error free invoices
	Early payment	Percent of customers who pay early
	Product quality	Product performance vs. standards
	Customer satisfaction	Customer satisfaction surveys
Inter-Nal	Low cost producer	Unit cost vs. competition
	Reductions in inventory	Inventory as % of sales
	New products	Number of introductions vs. target
Inno-Vation	New active ingredients	Number of new ingredients identified through discovery program
	Proprietary position	Number of patents that create exclusive marketing rights
Finan-cial	Growth	Percent increase in top line revenues
	Profitability	Return on Equity / Earnings per share
	Industry leadership	Market share

Source: Applying the Balanced Scorecard to Small Companies by Chee W. Chow, Kamal M. Haddad, and James E. Williamson - Management Accounting, August 1997

Chapter 5

The Performance Prism

One of the reasons behind the enormous popularity of the Balanced Scorecard is how it simplifies measurement into four or more perspectives. These perspectives break us out of the “financial only” mindset. However, this view of the business (from four perspectives) may not be all-inclusive. Perhaps we need to see things from a different facet of the business, namely by looking at all of our stakeholder groups. By focusing on stakeholders rather than perspectives, we more clearly identify what we need to measure. This raises one of the fallacies within the Balanced Scorecard – measuring only those things that fit within the confines of the model. And those things that are most important to the business, such as innovation, receive little emphasis within the measurement model.

> The Balanced Scorecard's shortcomings also include the fact that many stakeholders – suppliers, intermediaries, regulators – are not included. Hence it is not uncommon to end up with what has been dubbed a "biased scorecard" – that is, a scorecard biased towards only certain, often easy to measure, stakeholders.
>
> – 24 / 7 Innovation by Stephen M. Shapiro, McGraw-Hill

In order to address this "restrictive model" of the Balanced Scorecard and break out into measuring real sources of value-creation, Accenture (formerly known as Andersen Consulting) and the Center for Business Performance have developed something called the Performance Prism. The Performance Prism has five sides or facets of how we should view the business:

- Stakeholder Requirements (top layer)
- Strategies
- Processes
- Capabilities
- Stakeholder Contributions (bottom layer)

Each facet of the prism flows from the top to the bottom, linking stakeholder requirements to strategy, strategy to processes, processes to capabilities, and capabilities to contributions made by stakeholders. The key is matching up the capabilities of the organization against each stakeholder group. In his book, 24 / 7 Innovation, Stephen M. Shapiro describes the total range of stakeholder groups as:

- Employees: All employees, including part-time, contract or others who serve in a role similar to an employee.
- Suppliers: Providers of materials, labor and other resources to the business.
- Customers: The ultimate consumers of the product and/or service.
- Shareholders: Owners of the business.
- Complementors: Partners and others who add value to the final products and services that otherwise cannot be achieved by the business alone.
- Intermediaries: Consultants, quasi-customers, and other specialist that fill in gaps for meeting strategic and operating objectives.
- Regulators: Governmental entities and other groups that have some degree of control or influence over the business.

Building the right capabilities is critical to successful execution of the strategy. Capabilities are the collection of people, technology, products, and all those things that the business must do to meet the expectations of its stakeholders. In its simplest form, capabilities are the functional areas of the business – production, marketing, sales, finance, distribution and all organizational components. However, author Stephen M. Shapiro offers a more all-encompassing definition of capabilities:

1. Strategy at all levels of the organization, including customer strategies.
2. Measurements for changing organizational behavior and hitting targets.
3. Processes on how the work gets done.
4. People – The skills, knowledge, structure, and culture of the organization.
5. Technology – The information and related infrastructure.

Integrating capabilities with stakeholder groups is how strategy is executed and this is the power behind the Performance Prism. It captures the cause and effect relationship over five facets or sides, linking stakeholders to strategy, processes, and capabilities:

Exhibit 21: Cause Effect Relationship for the Performance Prism

5 Steps to Developing the Performance Prism
1st: Identify your stakeholders and determine their requirements.
2nd: Once you understand your stakeholders, develop strategies to meet their needs and requirements.
3rd: Next, identify the business processes to execute your strategies.
4th: Next, determine the required capabilities that must be developed for implementing the processes identified in step 3.
5th: Finally, align the organization around stakeholders, building alliances so that the organization can create the capabilities identified in step 4.

Unlike the Balanced Scorecard where we started with strategizing as our initial step, the Performance Prism starts with a comprehensive understanding of stakeholders. You must first understand your stakeholders before you begin to strategize; otherwise strategizing is too subjective.

The Performance Prism also views measurement differently than the Balanced Scorecard. For example, more emphasis is placed on balancing lagging indicators with leading indicators. By using leading indicators, the organization can better focus on what should happen as opposed to looking at things that have already happened. For example, by using a measurement for repeat customers, a company can identify trends that indicate declining sales into the future.

For organizations with diverse stakeholders, the Performance Prism offers a more complete model for performance measurement than the Balanced Scorecard. For example, the so-called "virtual corporation" tends to outsource almost everything and thus, it would have a wide array of stakeholder groups. Therefore, the Performance Prism is a preferred measurement model where stakeholders are changing or broad in scope.

> Any approach to strategy quickly encounters a conflict between corporate objectives and corporate capabilities. Attempting the impossible is not good strategy. It is just a waste of resources.
>
> *– Bruce Henderson, CEO, Boston Consulting Group*

Course Summary

Strategy is the foundation around which all other activities take place. You need a framework for integrating strategy into all parts of the organization. Balanced Scorecards provide the framework by which an organization executes its strategy. The groundwork for building your balanced scorecard is to set the organization around a clear and concise strategy. From this strategy, you can translate your strategic objectives into a set of grids, connected over four perspectives:

Financial – Delivering expected financial results for investors.

Customer – Delivering value and benefits for customers.

Internal Processes – The set of processes that must be in place in order to meet the requirements of customers.

Learning & Growth – The set of values and principles related to intangibles (employees, systems, and organization), supporting and providing the required internal processes.

The Financial and Customer perspectives tend to represent the deliverables; i.e. those things the organization must deliver on whereas the Internal Processes and Learning and Growth perspectives tend to represent those things the organization must do.

Completing the strategic foundation (phase I) is the most important step in designing the Balanced Scorecard. And this requires considerable effort before you can start to build the three primary components of the Balanced Scorecard: Measurements, Targets, and Programs. Measurements control the process through communication and learning. Targets are the specifics of the strategy. Finally, we must have major initiatives or programs to make all of this stuff happen. Once you have populated the scorecard with measurements, targets, and programs, then you have successfully translated your strategy into operating terms. This completes construction of the Balanced Scorecard.

Once completed, we can move to the final phase of deployment. Deployment requires careful planning and coordination with other parts of the organization. Keep in mind that we are testing a whole new way of managing and therefore, you must readjust, modify, and revisit the design of your scorecard. Eventually, every employee should be able to look at their balanced scorecard and say: I understand what this means and what I need to do to make it happen.

In conclusion, strategy is about change and getting an organization to change is one of the most difficult things to do. When you can successfully get the organization to change, then you have removed one of the biggest obstacles to execution of your strategic plan. This is why balanced scorecards are so important – you must get your organization to change if you expect to execute your strategies. The Balanced Scorecard is the definitive management tool for making this happen.

Review Questions

The following questions are for review purposes. Answers appear at the end of this short course.

Discussion Questions:

1. Most organizations tend to have good strategic plans, but they fail to successfully implement their strategic plans. Identify at least two reasons why organizations fail to implement their strategic plans?

2. Briefly describe the “strategic foundation” for building the Balanced Scorecard?

3. What two ingredients are important for creating a “clear and concise” strategy?

4. What is the recommended maximum number of strategic areas, objectives, measurements, and targets for a balanced scorecard?

5. What is the ultimate goal behind full-scale implementation of the Balanced Scorecard?

6. The Performance Prism represents an alternative to the Balanced Scorecard. How does the Performance Prism differ from the Balanced Scorecard?

Multiple Choice Questions:

1. In order to get the most out of the Balanced Scorecard, it should **not** be thought of as a:

a. Stand alone performance measurement program.
b. Framework for communicating and executing strategy.
c. Tool for shifting emphasis from short term thinking to strategic thinking.
d. Strategic management system.

2. The very bottom perspective of the Balanced Scorecard is the ultimate "enabler" for the three top layers. This bottom perspective is called:

a. Internal Processes
b. Market Share
c. Learning & Growth
d. Shareholder Value

3. Which of the following goals relates to the strategic area of Efficient and Seamless Delivery Systems?

a. We will grow revenues by 20% each year over the next four years.
b. We will expand our customer share in the marketplace by 10% over the next three years.

c. We will attract the best and brightest people by adopting an entrepreneurial culture.
d. We will improve production delivery times by 30% over the next two years.

4. The measurement, % of market share, would most likely be placed in which perspective of the Balanced Scorecard?

a. Financial
b. Customer
c. Product Innovation
d. Learning & Growth

5. The Customer Perspective of a balanced scorecard has the following objective: Retain High Value Customers. Which objective within the Balanced Scorecard should fall below this objective?
a. Increase customer profitability through higher volumes.
b. Improve customer relations with more personal one-to-one service.
c. Increase employee awareness of strategies through new leadership program.
d. Improve financial system access to operating management personnel.

6. Lispon Industries has a balanced scorecard with the following measurement: Number of new product introductions. Which of the following strategic objectives would this measurement relate to?

a. Lispon will improve our customer relations through expansion of customer relation's management.
b. Lispon will increase revenues through more competitive pricing of high volume products.
c. Lipson will attract more customers through a broader and more diverse product line.
d. Lipson will retain the best talented people through empowerment, work teams, and above average industry compensation packages.

7. JT Corporation has the following strategic areas related to its strategy:

A = Shareholder Value
B = Personal Customer Service
C = Employee Involvement and Commitment

How should each of the following objectives fit within these strategic areas?

	More Service Centers / Broader Coverage for Targeted Customers	Higher Operating Margins	New work groups and cross functions for all departments
a.	C	B	A
b.	A	C	B
c.	B	A	C
d.	A	B	C

8. Which of the following is an example of a measurement?

a. Growing Revenues to Improve Shareholder Value
b. Number of Employee Suggestions
c. Operational Efficiency
d. Product Leadership & Innovation

9. Morton Company is currently measuring delivery times to customers. Over the past three years, Morton's average delivery time has been 60 minutes with a delivery time of 50 minutes for the most recent year 2001. A recent survey of customers indicates a need to improve delivery times. Competitive research related to the current year shows that industry average delivery times are 40 minutes and "best in class" delivery times are 20 minutes (min). Industry trends show that over the next few years, only minor improvements will occur in delivery times. The President of Morton has set the following strategic goal: By the year 2005, Morton Company will be ranked at the very top in the industry for customer delivery time. Which of the following targets (delivery time in minutes) should be established for Morton?

	Current Year	Year 2002	Year 2003	Year 2004	Year 2005
a.	50 min	45 min	40 min	35 min	30 min
b.	60 min	55 min	45 min	35 min	25 min
c.	50 min	40 min	30 min	20 min	15 min
d.	50 min	45 min	40 min	35 min	20 min

10. An organization's first balanced scorecard should try to cover all aspects of the value chain; i.e. sales, service, innovation, production, customer, etc. Therefore, the best place to start building the Balanced Scorecard is at the:

a. Corporate level of the organization.
b. Operating unit of the organization
c. Functional Department within the organization.
d. Individual personal level within the organization.

11. The specific steps for making the Balanced Scorecard an overall management system includes:

A = Establish a clear and concise strategy
B = Launch programs to meet strategic objectives
C = Restate your strategy into a set of grids
D = Deploy and cascade the scorecard to other parts of the organization
E = Define a measurement for each strategic objective

The sequence or order of these steps is:

	Step 1	Step 2	Step 3	Step 4	Step 5
a.	C	B	A	E	D
b.	A	C	E	B	D
c.	A	E	B	C	D
d.	A	E	C	B	D

12. For organizations with highly diverse or changing stakeholder groups, the Balanced Scorecard may not represent the best performance model. Which of the following performance measurement models is a better choice than the Balanced Scorecard where stakeholder groups are extremely diverse?

a. The Performance Prism
b. The Service-Tracking Model
c. The EVA Model
d. Benchmarking Grids

Final Exam

In order to receive credit for this short course, you will need to download and install the exe file version of this short course, located on the internet at www.exinfm.com/training. The exe file includes a self-grading final exam and certificate of completion. In order to receive a certificate of completion, you must answer at least seven of the following ten questions correctly:

1. Balanced scorecards consist of four inter-related perspectives. Which perspective or layer will be the main driver or enabler for outcomes within the financial perspective?
    a. Learning & Growth
    b. Customer
    c. Programs
    d. Templates

2. The Balanced Scorecard process captures a cause and effect relationship based on having all parts linked together. Strategic areas link down to goals, strategic goals link down to strategic objectives, and strategic objectives are linked to:
    a. Mission
    b. Goals
    c. Budgets
    d. Measurements

3. Mason Corporation has developed the following three strategic objectives for its balanced scorecard:

    A = Employee involvement will be enhanced through a new matrix realignment of the organization.
    B = Customer confidence will be expanded through more personal approaches to service.
    C = The product delivery system will be expanded to include all new product lines.

    Where should Mason Corporation place these three objectives within its strategic grid?

	Customer	Internal Processes	Learning & Growth
a.	A	C	B
b.	C	B	A
c.	B	C	A
d.	B	A	C

4. There are two types of measurements: Leading Indicators (lead to end results) and Lagging Indicators (the end results). Which perspective of the Balanced Scorecard would most likely use leading type measurements?
   a. Financial
   b. Customer
   c. Internal Processes
   d. Learning & Growth

5. Triple K Construction is developing a balanced scorecard. One of the goals for Triple K Construction is: We will meet or exceed the expectation of our customers by providing commercial construction projects that are on time and on budget. Which of the following strategic areas fits with this goal?
   a. Commitment to Community
   b. Customer Satisfaction
   c. Shareholder Value
   d. Employee Productivity

6. Triple K Construction has the following strategic objective: We will meet the completion dates on all new construction projects beginning in the year 2003. Which of the following measurements provides the best fit with this strategic objective?
   a. Percentage of projects completed on time
   b. Total number of projects in progress
   c. Construction cost to revenue ratio
   d. Overall customer satisfaction index

7. JGT Enterprises has compared its existing programs against its strategic objectives. If a program impacts a strategic objective, then the intersecting box is filled in on the following template:

Assess Strategic Impact of Programs against strategic objectives **Objectives** / **Programs**	Automated Distribution	Capital Additions	Market Study	Cross Functional	Product Research
Improve Delivery Times	■				
Introduce New Product Features					■
Reduce Distribution Costs	■				
Retool Production Process		■			
Enhance Quality Control	■	■			
Increase Employee Involvement				■	

Which program has the most (highest) strategic impact and which program has the least (little or no) strategic impact on the strategic objectives?

	Most Strategic Impact	Least Strategic Impact
a.	Product Research	Cross Functional
b.	Automated Distribution	Market Study
c.	Product Research	Market Study
d.	Automated Distribution	Product Research

8. ______________ are tools (usually spreadsheets) for capturing and organizing much of the data that goes into building the Balanced Scorecard

   a. Templates
   b. Indexes
   c. Goals
   d. Ratios

9. Balanced scorecards are appropriate for which type of organization?

a. Private sector businesses.
b. Non-profit organizations.
c. Government agencies.
d. Any organization concerned about the execution of its strategy.

10. Unlike the Balanced Scorecard, the Performance Prism captures the cause and effect relationship of strategies, business processes, and capabilities against:

a. Customers
b. Stakeholder Groups
c. Global Competition
d. Employees

Answers to Review Questions

Discussion Questions:

1. There are several reasons why strategies fail. One fundamental problem is that most people do not understand the strategies of the organization. Another major problem is that budgets control decision-making and how people are rewarded. Instead of linking decisions and people to budgets, the link should be to how well we are doing in executing our strategy. Other problems include insufficient time spent on strategic decision-making and poor alignment between different parts of the organization.

2. The Strategic Foundation begins with a very clear strategy. Next, we translate the strategy into a set of strategic grids. A strategic grid or map pulls together all of the strategic objectives around some strategic area important to the organization. The end result is a complete strategic model that serves as the foundation for populating the scorecard with measurements, targets, and programs.

3. Two key ingredients of a “clear and concise” strategy are objectives that outline action to the organization and targets for communicating the expected results of the strategy.

4. The recommended number of strategic areas is no more than five. For each area, we will have a complete scorecard. Each scorecard should consist of no more than 20 to 25 strategic objectives. For each objective, there should be one measurement and for each measurement there should be one target. Therefore, the recommended number of measurements and targets is the same as the recommended number of strategic objectives; namely 20 to 25.

5. The purpose of implementing a balanced scorecard should be to shift the organization so that it no longer is dominated by operating decisions and decision-making is now strategic. Several principles are often cited for making this transformation a reality:

   - Align and set the organization around a clear and concise strategy.
   - Express the strategy in terms that make sense to people, such as measurements, targets, and programs.
   - Make strategic thinking a core competency of the organization.
   - Push strategic decision-making into lower levels of the organization (such as the Mobil Oil Truck Driver who pulls a scorecard from the visor in his cab).

6. The Performance Prism does not rely on perspectives for mapping a strategy. Instead, the Performance Prism relies on a solid understanding of stakeholders and how they interact with the capabilities of the organization. The focus is on building capabilities and measuring these capabilities to reach strategic goals and objectives.

Multiple Choice Questions:

1. a Although it is easy to think of the Balanced Scorecard as a performance measurement system, it is actually the framework or model for strategic management within the organization.

2. c The ability of employees and management to learn and grow (Learning & Growth) is at the foundation for driving or "enabling" much of what takes place in the top three perspectives: Internal Processes, Customer, and Financial. For example, the organization must be able to improve and innovate existing processes. This leads to better customer service and this in turn leads to improved financial performance.

3. d The goal of improving delivery times would relate to Efficient and Seamless Delivery Systems. Answer a would relate to a financial area such as Shareholder Value,

answer b would relate to a customer objective that leads to revenue growth, and answer c would relate to Leveraging Employees.

4. b Measuring the percentage of market share would relate to the Customer Perspective. The % share of customers provides some indication of acquiring more customers vs. losing existing customers.

5. b If the objective is to retain high value customers, the best leader of this objective would be to emphasize more personal one to one service to these customers. Answer a puts emphasis on all customers, regardless of value added. Answers c and d relate more to the Learning and Growth perspective and not specifically to a customer objective.

6. c One of the objectives listed by Lispon is to attract more customers by introducing a more diverse product line. In order to drive this objective, we will need to introduce more products. Therefore, measuring new products introduced would fit with this strategic objective.

7. c The objective of increasing service centers for targeted customers would relate to better personal customer service or B. The objective of higher operating margins is a financial area, namely shareholder value or A. Finally, the objective of reorganizing departments around cross functional groups would relate to more employee involvement and commitment or C.

8. b The number of employee suggestions is a measurement. The other three are examples of strategic areas.

9. c We need to start with our most current level of performance or 50 minutes and we need to move to "best in class" of 20 minutes since this is a major goal for our company. Additionally, over the next few years, we can expect to see some minor improvements in this benchmark and therefore, by the year 2005, we should have a delivery time below the current best in class benchmark of 20 minutes. If we map all of this out, a logical set of targets from year 2001 to 2004 would provide incremental improvements of 10 minutes each year leading up to a final delivery time below 20 minutes in year 2005.

10. b The most logical place to start building a balanced scorecard is where you can capture all business processes (product innovation, customer service, production, distribution, sales, etc.). Operating business units should cover most if not all of these business processes.

11. b Step 1 is A or define your strategy; Step 2 is C or restate your strategy into grids; Step 3 is E or define measurements; Step 4 is B or launch programs; and Step 5 is D or deploy the scorecard to other parts of the organization.

12. a For organization’s with numerous stakeholder groups, the Performance Prism provides a better choice than the Balanced Scorecard since important measurements could get overlooked.