Balanced scorecard - A strategy management tool

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Companies today are in the midst of a revolutionary transformation as Industrial age competition is shifting to Information age competition. The cut-throat competition that businesses faced in the last two decades has made them to look for improvement initiatives like Total Quality Management, Just-in-Time (JIT) systems; Activity based cost management, Employee empowerment and Re-engineering. Though these initiatives resulted in enhanced shareholder value, their structure was disjointed and focused on the short-term survival and growth. The programs centered on achieving breakthrough performance merely by monitoring and controlling financial measures of past performance. This collision between the irresistible force to build long-range competitive capabilities and the immovable object of the historical-cost financial accounting model has led to a new blend the Balanced scorecard.

The Balanced scorecard retains the traditional financial measures and complements them with measures that are drivers of future performance. The objectives and measures of the scorecard are derived from an organizations vision and strategy and these view organizational performance from four perspectives: financial, customer, internal business process and learning and growth. These four perspectives provide the framework for the Balanced scorecard.

The balanced scorecard is a ***management system*** (not only a measurement system) that enables organizations to clarify their vision and strategy and translate them into action. It provides feedback around both the internal business processes and external outcomes in order to continuously improve strategic performance and results. When fully deployed, the balanced scorecard transforms strategic planning from an academic exercise into the nerve center of an enterprise.

Kaplan and Norton describe the innovation of the balanced scorecard as follows:

"The balanced scorecard retains traditional financial measures. But financial measures tell the story of past events, an adequate story for industrial age companies for which investments in long-term capabilities and customer relationships were not critical for success. These financial measures are inadequate, however, for guiding and evaluating the journey that information age companies must make to create future value through investment in customers, suppliers, employees, processes, technology, and innovation."

What is a Balanced Scorecard?

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First of all the balanced scorecard is a way of

- Measuring organizational, business unit or department success;
- Balancing long and short term actions;
- Balancing different measures of success and
  - Financial
  - Customer
  - Internal Operations
  - Human Resource Systems & Development (Learning & growth)

- A way of tying strategy to measures of action

The Need for the scorecard:

The objective of any measurement system should be to motivate all managers and employees to implement successfully the business units strategy. Those companies that can translate their strategy into measurement system will be able to execute their strategy because they communicate their objectives and their targets. The communication makes managers and employees focus on the critical drivers enabling them to align investments, initiatives and actions accomplishing strategic goals.

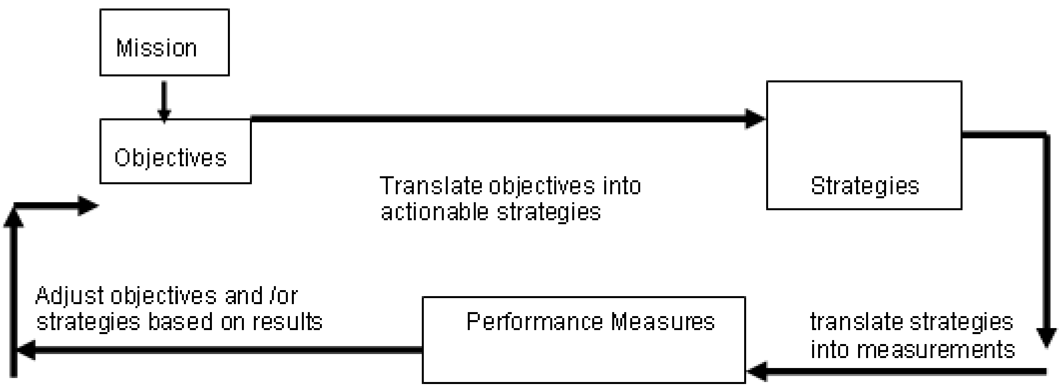
Historically, the measurement system for any business has been financial. Accounting was considered to be the language of business Innovations in measuring the financial performance of the industrial age companies played a vital role in their successful growth. And financial innovations, such as the Return on Investment (ROI) metric, and operating and cash budgets, were critical to the success of these corporations.

However, an over emphasis on achieving and maintaining short-term financial results can cause companies to over invest in short-term fixes and to under invest in long-term value creation, particularly in the intangible and intellectual assets that generate future growth. The pressure for short-term financial performance often causes companies to reduce the resources spent on new product development, process improvements, human resource development, Information technology, databases and systems as well as customer and market development. In the short run, the financial accounting model reports these spending cutbacks as increases in reported income, even when the reductions have cannibalized a companys stock of assets and its capabilities for creating future economic value. In short, these organizations use the financial and non-financial performance only for tactical feedback and control of short-term operations.

Linking Strategy with Performance Measures

The essential thrust of the balanced score card is based on the fundamental proposition that within organizations what gets measured gets done however, organizations dont always get what they measure. If measurement, by itself, had that much impact on human behavior, then anyone that had weighing scales would never get fat.

An appropriate measurement system is one that energizes employees in the context of what the organization is trying to do. Thus, the logical starting point for the development of any performance measurement system for an organization must be a clear statement of mission, objectives and resultant strategy. An organizations mission is its basic function in society and is the reason why the organization exists. Related to this are the objectives to be achieved and they represent a precise statement of purpose for a specific period. Basically a strategy is a shared understanding about how the organizations mission is to be achieved in a competitive environment. Strategic thinking will focus on customers and competitors as well as internal capabilities and resources. It will include reference to the firms competitiveness, quality of output and levels of customer service. In turn, specified performance measures allow all employees understand what the strategy is and how their performance is linked to that overall strategy. The relationship between Mission, Objectives, Strategy and Performance Measures is depicted in Fig.1.



There are at least three reasons why organizations should, and often do, measure their performance:

1. To align mission, strategy, values and behavior
2. To improve the right things
3. To numerically define the meaning of success

The 4 perspectives of the Balanced Scorecard

The Balanced Scorecard method of Kaplan and Norton is a strategic approach, and performance management system, that enables organizations to translate a company's vision and strategy into implementation, working from 4 perspectives:

1. Financial perspective.
2. Customer perspective.
3. Business process perspective.
4. Learning and growth perspective.

This allows the monitoring of present performance, but the method also tries to capture information about how well the organization is positioned to perform in the future.

Benefits of the Balanced Scorecard

Kaplan and Norton cited the following benefits of the usage of the Balanced Scorecard:

- Focusing the whole organization on the few key things needed to create breakthrough performance.
- Helps to integrate various corporate programs. Such as: quality, re-engineering, and customer service initiatives.
- Breaking down strategic measures towards lower levels, so that unit managers, operators, and employees can see what's required at their level to achieve excellent overall performance.

1. The Financial Perspective

Kaplan and Norton do not disregard the traditional need for financial data. Timely and accurate funding data will always be a priority, and managers will make sure to provide it. In fact, there is often more than sufficient handling and processing of financial data. With the implementation of a corporate database, it is hoped that more of the processing can be centralized and automated. But the point is that the current emphasis on financial issues leads to an unbalanced situation with regard to other perspectives. There is perhaps a need to include additional financial related data, such as risk assessment and cost-benefit data, in this category.

2. The customer perspective

Recent management philosophy has shown an increasing realization of the importance of customer focus and customer satisfaction in any company. These are called leading indicators: if customers are not satisfied, they will eventually find other suppliers that will meet their needs. Poor performance from this perspective is thus a leading indicator of future decline. Even though the current financial picture may seem (still) good. In developing metrics for satisfaction, customers should be analyzed. In terms of kinds of customers, and of the kinds of processes for which we are providing a product or service to those customer groups.

If our aim is to be customer-centred, the following are the measures:

1. Customer desired outcomes
2. Undesired outcomes customers want to eliminate here include: Death, taxes, discomfort, wasted time and a host of unwanted conditions.
3. Product and service attributes customers want
4. Process characteristics customers want
5. Producer desired outcomes
6. Undesired outcomes producers want to eliminate
7. Product attributes producers want
8. Process characteristics producers want

3. The Business Process perspective

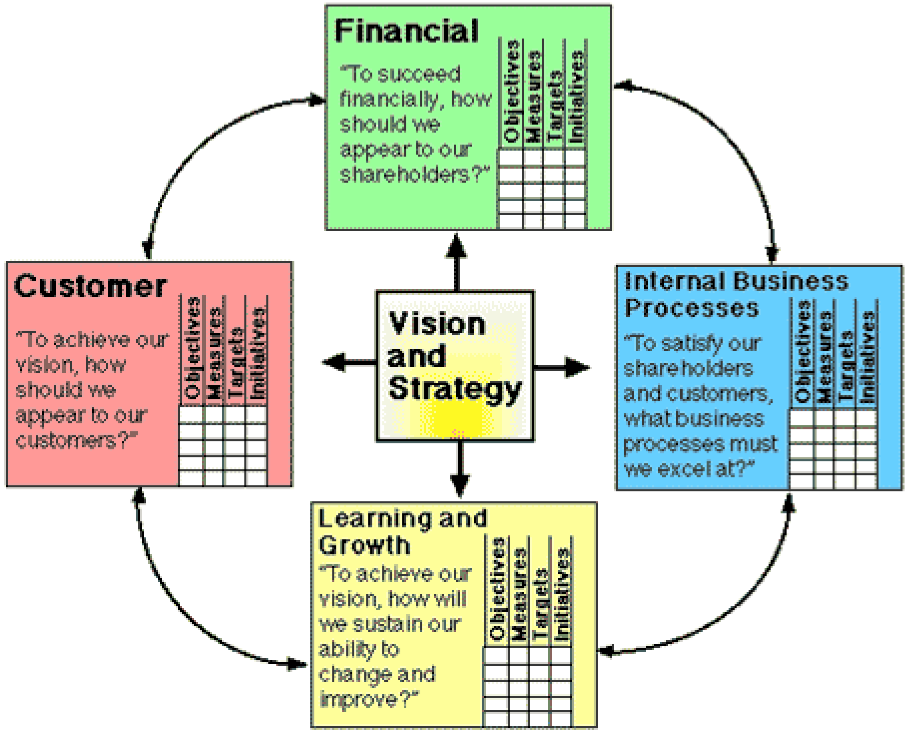
This perspective refers to internal business processes. Measurements based on this perspective will show the managers how well their business is running, and whether its products and services conform to customer requirements. These metrics have to be carefully designed by those that know these processes most intimately. In addition to the ***strategic management processes***, two kinds of business processes may be identified:

- ***Mission-oriented processes***. Many unique problems are encountered in these processes.
- ***Support processes***. The support processes are more repetitive in nature, and hence easier to measure and to benchmark. Generic measurement methods can be used.

4. Learning and Growth perspective

This perspective includes employee training and corporate cultural attitudes related to both individual and corporate self-improvement. In a knowledge worker organization, people are the main resource. In the current climate of rapid technological change, it is becoming necessary for knowledge workers to learn continuously. Government agencies often find themselves unable to hire new technical workers and at the same time are showing a decline in training of existing employees. Kaplan and Norton emphasize that 'learning' is something more than 'training'; it also includes things like mentors and tutors within the organization, as well as that ease of communication among workers that allows them to readily get help on a problem when it is needed. It also includes technological tools such as an Intranet.

The integration of these four perspectives into a one graphical appealing picture has made the Balanced Scorecard method very successful as a management methodology.



Implementation Issues & Difficulties:

There are 3 issues that contribute to the success of any measurement managed organization.

- First, in order to be successful, a mission statement, objectives and related strategy needs to be in place. These provide a preliminary focus.

- Second, there needs to be a great deal of communication and training prior to the introduction of a corporate scorecard. It is advisable to implement a pilot project before introducing the scorecard since this allows one to learn some valuable lessons. Also, a scorecard should not be introduced unless its is clear what is to be achieved. No organization should allow itself to drift or be pressurized by the literature into implementing a scorecard unless it has a very good idea of what it expects to get out of it.

- Third, at the outset, top management must be committed to the project and must send that message out to the rest of the organization. The importance of top management commitment and motivation cannot be sufficiently emphasized. They must be totally committed to the entire process and ensure that the task is given adequate priority. It is also essential to involve as many opinion leaders as possible in the initial process, particularly for the purpose of recruiting a number of highly motivated missionaries for the work later on.

Actual usage of the balanced scorecard

Kaplan and Norton found that companies are using the scorecard to:

- Clarify and update budgets
- Identify and align strategic initiatives
- Conduct periodic performance reviews to learn about and improve strategy.

Balanced scorecards have been implemented by government agencies, military units, corporate units and corporations as a whole, nonprofits, and schools; many sample scorecards can be found via Web searches, though adapting one organization's scorecard to another is generally not advised by theorists, who believe that much of the benefit of the scorecard comes from the implementation method.

Conclusion:

It is now generally accepted that performance measures should be an integral part of modern internal reporting system. The performance measures (or indicators) should:

- Be linked with corporate strategy;
- Mirror both internal & external concerns;
- Include financial and non-financial dimensions; and
- Be both leading and lagging indicators of performance.

It has recently been reported that companies who use suitable performance measurement systems were much more likely to achieve leadership positions in their industry and were almost twice as likely to have successfully implemented a major organizational change. Management accountants who grasp the very simple idea of the BSC will considerably increase the capacity of their organizations to survive and prosper. The important issue for management accountants is to reflect on what Albert Einstein once remarked: Not everything that counts can be counted, and not everything that can be counted, counts.