

# Performance Measurement – an Executive Overview

By: Michael Tipping

## Why Performance Measurement?

“Would you tell me please which way I ought to go from here?” asked Alice. “That depends a good deal on where you want to get to.” “I don’t really know,” replied Alice. “Then it doesn’t matter which way you go,” said the cat.

Most organizations have already recognized that their strategic objectives are not purely financial in nature. And, even if they are primarily financial, the organization that ignores key ‘non-financial’ performance areas can be fairly certain that it will not achieve its long-term financial objectives.

## What’s wrong with traditional reporting and management systems?

Organizations that rely primarily on financial reporting systems have to recognize a number of shortcomings:

Financial systems do a reasonable job of delivering information to shareholders - and this, of course, is what they were designed to do. Unfortunately, they do a poor job of telling managers how they are doing in other critical areas such as Customer Service, Human Resources, New Product Development, and Process Improvement.

In fact, managing by financial systems has often been compared to ‘driving by using the rear-view mirror’. This analogy is very apt because:

- **you can’t see where you are going, only where you’ve already been**
- **although you just heard a bump, you are not sure what you hit!**
- **and you won’t know what you did hit until it shows up in the mirror sometime later!**

In other words, by the time issues show up in your financial results, they have already become problems.

Nowadays, in an effort to overcome this reliance on financial systems, many companies do track other key performance measures on a regular basis. But, this is typically done on an ‘ad-hoc’, piecemeal basis, rather than as an integrated and comprehensive approach to managing performance. As a result, even those financial systems, which have been enhanced by the addition of other key performance measures, will likely exhibit some or all of the following problems:

### **Problem#1: No indication of cause and effect**

Although your systems may give some approximation of what has happened, they will rarely tell you why it has happened. They also can’t tell you what you are doing right and what you are doing wrong.

For example, a reduction in sales revenue may show up quite quickly - and you may even be able to focus on specific geographical or product areas. But, if you don't have the information that can tell you the reasons for a sales shortfall, you won't know what corrective action is required.

In any area, there will be certain 'performance drivers' which can give you an early warning of problems ahead. In this case, if the factors which directly affect Customer Satisfaction - such as product quality, returns, on-time delivery and accuracy - had been tracked through internal systems and customer contacts, it would have been possible to take corrective action before there was a negative impact on sales.

*Solution:* A system which includes predictors of future performance ('drivers') as well as 'results' measures - and reinforces the links between them.

### **Problem#2: Reinforcement of organizational 'silos'**

Traditional systems tend to report results based on functional or departmental lines. Unfortunately, this reinforces reporting, or organizational, lines of authority, rather than encouraging team, process or other cross-functional approaches. This does not reflect the way that your customers, suppliers, employees or other stakeholders view your organization.

In addition, it is difficult for individual employees to understand how the measures which they own, or impact, fit into the overall goals of the organization.

*Solution:* A system that can present information on a 'process' or 'stakeholder oriented' basis, clearly showing the inter-relationship of performance measures and their linkage to corporate objectives

### **Problem #3: A blurring of key issues**

"...the areas requiring the most management attention will likely be the ones actually getting the least prominence."

Most management teams rely on a variety of information sources - and interpreting the myriad of reports, presented in many different formats, is a time-consuming task. Given the complication of this process, and the limited time usually available, analysis is often superficial at best. This may well mean that critical issues, requiring attention and corrective action, are ignored simply because of the way the data is presented.

*Solution:* A system which can present data in a consistent format, requiring minimal interpretation and allowing users to quickly focus on performance issues.

### **Problem #4: Unreliable or inaccurate data**

Because many information systems are 'ad hoc' in nature, consisting of special reports, extracts or 'add-ons' to existing systems, there is a real danger of receiving inaccurate or misleading information.

Often these reports are assembled using spreadsheets that have the unfortunate characteristic of looking very good, whether or not there are errors contained in the calculations. Everyone

thinks they know how to use spreadsheets, but remember that building a spreadsheet is, essentially, a programming activity without formalized quality control and testing. Every spreadsheet user will admit that, at some time or other, they have made an error in a formula, giving an incorrect result. The very candid will tell you that some of the reports containing errors were published!

Ironically, the information which is most important for your long-term success is probably coming from your least dependable systems.

*Solution:* A system that minimizes the amount of 'ad hoc' programming, spreadsheet usage, special reporting, PowerPoint presentations, etc.

#### **Problem #5: Time consuming and costly**

There is another problem with the assembly of a wide variety of reports. It is likely costing far more time and money than you think. If you investigate the true costs of assembling your monthly information package you will probably be in for a shock. In addition to the hidden costs of your 'spreadsheet programmers' (unfortunately playing with Excel is just too much fun - and, unlike playing video games, you look busy at the same time!), you'll have to add all that typing, photocopying, programming, preparation of electronic presentations, assembling binders, etc.

*Solution:* A system which can extract the data you need and present the information in a way that you can use it, without the need for costly and time-consuming manual intervention.

#### **Problem #6: Results can be 'filtered'**

Another implication of the lack of structure and consistency in reporting is that the individuals presenting information can choose to highlight certain items and ignore, or de-emphasize, others. It's even possible that, in some circumstances, the items that are emphasized are things that will make them look good and the downplayed (or ignored) items might be the ones that make them look bad! Of course, the implication of this behavior is that the areas requiring the most management attention will likely be the ones actually getting the least prominence.

*Solution:* A system that encourages a standard and consistent presentation of results, enabling management to highlight and react to performance variances.

#### **Problem #7: No linkage to Performance Management**

"...the information which is most important for your long term success is probably coming from your least dependable systems."

Given the underdeveloped nature of the performance reporting systems used in most companies, the majority of organizations base their employees' incentive packages on traditional measures such as sales or profit - and, not surprisingly, employees concentrate their attentions on achieving these, usually short-term, objectives. You can talk to employees all you like about the importance of your customers, but if you judge their performance simply on traditional measures their behavior will not reflect your strategic priorities.

*Solution:* A comprehensive and reliable system that will allow performance management to be linked to a wider range of key performance measures.

What are the characteristics of a good Balanced Performance Measurement solution?

It will be necessary to have some type of delivery mechanism; usually software based system, for your measurement solution. The factors affecting your choice of such a solution are discussed below. Keep in mind that, whatever your choice, you should ensure that these key design features are accommodated:

## **What are the characteristics of a good Balanced Performance Measurement Solution?**

It will be necessary to have some type of delivery mechanism; usually software based system, for your measurement solution. The factors affecting your choice of such a solution are discussed below. Keep in mind that, whatever your choice, you should ensure that these key design features are accommodated:

### **1. Clear definition**

- A 'view' should be constructed that aligns performance measures with the strategic objectives of the organization. You should be able to group measures into categories that make sense at an operational level.
- All measures are not created equal! The relative importance of your measures should be clearly defined to ensure a clear understanding of relative priorities.

### **2. Ownership**

All measures included should have 'owners' (individuals or teams) responsible for performance and data accuracy. As well, it should be possible to easily produce 'scorecard' reports for each owner to clearly indicate performance for their measures.

### **3. Clear communication of results**

In order to provide useful information, results must be put into a context. Actual performance should be indexed against one or more comparatives (e.g. target, plan, prior year, etc.). Color-coded results indicators will provide an immediate visual cue, enabling performance variances to be easily identified. For example, you may choose to indicate performance less than 95% of target in red, from 95-105% in yellow, and above 105% in green. You should also have the ability to 'switch' comparatives, so that you can say compare actual performance this year with your plan for 2001.

### **4. Flexible reporting**

In addition to being able to see the overall view of performance, users should be able to customize the information they receive, selecting the measures which are important to them, preferably by means of briefing books which they can configure for specific purposes.

## **What are the benefits of a Balanced Performance Measurement solution?**

A properly executed solution can provide significant advantages to any organization. These can be categorized as follows:

### **1. Improved alignment and focus**

Day-to-day activities will be aligned with the organization's strategic focus, ensuring that people are on the right track - with appropriate feedback on their performance.

## **2. Better communication**

People will feel that they are being kept informed and can also share their own performance with others. This will help create a forum for 'non confrontational' performance dialogue and open communication.

## **3. Increased organizational efficiency**

Since relevant information on all areas of performance is easily available in a single system, it's possible to eliminate inefficient 'ad hoc' reporting, investigation and response activities.

## **4. Reduced risk**

When performance in all aspects of the business, both financial and non-financial, is clearly visible, you have assurance that nothing will 'fall through the cracks'. And, because issues are highlighted on a timely basis, they can be resolved before they become problems. You will also be providing a clear definition of priorities at every level, reducing the possibility of costly misunderstandings and miscommunication.

***"What gets measured gets done."***

## **How to define your measurement system**

The objectives of a balanced performance measurement system are to promote focus and alignment, encourage communication, and provide a 'forward looking' vision - in other words, to change people's behavior. A comprehensive view of performance should be developed to include all aspects of the organization's operation.

Performance measurement systems succeed when they provide relevant facts and data about current performance and show what needs to be improved, either immediately or in the future. And measures should be aligned with strategic objectives to ensure that employees' behavior is consistent with corporate goals.

Most EIS (Executive or Enterprise Information Systems) fall into disuse because they focus on such narrow areas as sales or cost breakdowns. Executives need to see 'the big picture', focusing on areas which need their attention. They will not (and should not) allocate time to a detailed analysis of one aspect of their business.

When you first build your measurement system, there's always a tendency to incorporate measures where data is easily available – which are not necessarily those which help people run the business. This is a temptation that must be avoided. Instead, you should go through a structured process of measure identification. This is normally done through meetings and workshops with the executive group, followed by sessions with each of the organization's functional or process managers and their key players.

*Chase Manhattan Bank aligns its performance measures with its strategic objectives of 'Employer of Choice', 'Investment of Choice' and 'Provider of Choice'.*

*SmithKline Beecham uses 'core values' of People, Performance, Customers, Innovation and Integrity.*

The process of defining the full scope of your measurement system consists of four main stages:

1. Defining your overall context (choosing a framework).
2. Identifying the top levels (key performance areas) of your performance view.
3. Selecting the measures to include.
4. Aligning measures to complete your performance view.

### **1. Defining your overall context**

There are a number of published "frameworks" which attempt to put measures into a pre-defined context, like the four 'perspectives' of the Balanced Scorecard, or the seven "pillars" of Baldrige.

We recommend a different approach. Your executive team will define the key strategic elements (or 'core values') - normally based on existing mission / vision statements. In almost all cases, these will include, in some form or other:

- People
- Customers
- Financial Performance

Other core values will be included which are important to your organization.

### **2. Identifying key performance areas**

Within each 'core value' there will be a number of key performance areas. For example, within the core value of 'Customers', you may want to differentiate various types of customers, and the key areas of performance, which are relevant to each type. This will be repeated for each core value and, at the end of this process, you will have an overall context that you can use to help define, and subsequently align, your performance measures.

### **3. Selecting the measures to include**

The next step is for managers and project / process teams to identify those measures that illustrate achievement of your business goals and strategies. Normally, this will be accomplished through a series of facilitated workshops that will include these key steps:

#### **A. Compile a list of measures**

Assemble a comprehensive list of measures covering all aspects of the organization's performance. This list should include:

- The measures which are currently used in executive, board and project meetings
- Measures incorporated in budgets and planning documents
- Measures which reflect performance for each of the key processes in your company
- Measures used internally by functional areas to measure their own performance
- Appropriate measures used by other organizations

## **B. Filter the list of measures**

You will now need to refine this measure list, filtering out those that are inappropriate. You should reject measures which:

- *Do not initiate action* - where a change in reported performance does not cause individuals or teams to act differently.
- *Do not provide good information.* - where it is unclear exactly what is being measured and how results should be interpreted.
- *Do not illustrate progress towards achieving strategic objectives.*
- *Do not have 'ownership'* - where no individual or team is responsible for performance.
- *Are duplicates.* Often a list will contain a number of measures covering the same basic performance parameter. Select the best, most widely accepted measures for inclusion.
- *Will never have data available*- where it is impossible or cost-prohibitive to capture the necessary data.
- *Are otherwise flawed.* Some measures may be 'trivial', they may not have general acceptance in the organization or they may be unsuitable for other reasons.

In addition, some other measures may be 'put on hold' (i.e. designated for future inclusion in the performance view) where:

- *Data is not currently available*, but could be in the near future.
- *Further investigation is required* to properly define the exact measurement criteria.

The remaining measures should be candidates for inclusion in your performance view.

## **C. Do a "reality check"**

You should critically review your measure list for completeness by asking the following questions:

Are there a reasonable number of important measures for each 'core value'?

- Do we have a good balance between financial and non-financial measures?
- Do we have 'drivers' as well as 'results' measures?
- Are there measures from all departments / functional areas?
- Are there measures representing each of your key processes?
- Do we have measures clearly illustrating the key issues of Time, Cost and Quality?

If there are omissions in any of these key areas, you should revisit part of the measure definition process.

## **4. Alignment of measures**

Having selected your list of key measures, you should align these with your key performance areas. As you go through this process, you will often need to create additional 'groupings' of measures as required.

### **Assign weightings and ownership**

In any area, some measures have a greater significance than others - either statistically or intuitively – and you should reflect their differences by distributing or ranking them with weightings that factor into an overall grouping.

As well, you should assign every measure an owner. A key objective is to communicate to other stakeholders the current situation and the associated implications. Measurement owners should provide periodic commentaries to update others about results and progress in strategic and operational activities.

### **Don't seek perfection - just do it!**

When you define your performance view, it will include areas that should be measured. You may not know exactly what to measure in these areas, choosing to allocate a team to work on this later. Some areas will have missing or inaccurate data you may have to set up totally new ways of capturing this data or to devise ways of extracting the data from existing systems.

*“...much of the benefit to be derived from performance measurement systems is from **going through the process** and evaluating the feedback from users. The clear message is ‘Just do it!’ “*

This should not stop your progress. Make sure that your reporting system is flexible enough to allow you to integrate these measures easily when accurate data does become available – and to show these measurement areas as ‘placeholders’ now to remind everyone of their importance.

Don't be disappointed if only 50 or 60% of the data is available at the outset. Having access to this information is a good start – and is certainly better than not using it. At least you are on your way.

In fact, our experience suggests that much of the benefit to be derived from performance measurement systems is from going through the process and evaluating the feedback from users. The clear message is ‘Just do it!’

### **How to select a software solution**

We believe that a software solution is essential for a successful performance measurement implementation. The right software solution can help you rapidly deploy your performance measurement system. Clearly displaying your measurement context and linking all of the facts, data and information into a single system will facilitate communication and eliminate tedious collection and reporting activities.

### **What are the options?**

There are two general categories of software solution – ‘Do it yourself’ or ‘Off-the-shelf’.

When selecting, or building, a solution you should ensure that it can satisfy the users’ requirements and the technical issues of your environment, as well as being cost effective and easy to maintain.

A successful implementation also requires a system which will enable clear communication of actual performance whilst reinforcing the alignment of measures with strategic objectives.

### **What are the important issues for management to consider?**

The management group should be primarily concerned with the ‘big issues’ and should ask the following questions:



- Does the system provide the necessary alignment and focus within the organization?
- Does the system require an excessive level of resources to develop, maintain, and continually enhance?
- Can we guarantee a successful implementation in a reasonable timeframe?
- What are the total costs of development, implementation, training, user support and future enhancements?

*Our experience suggests that a 'packaged' solution, like the pb views product from Panorama Business Views, will typically be far less demanding on internal resources, be deliverable in a shorter timeframe, and be far more cost effective than any attempt to build a similar system in-house.*

### **What are users looking for?**

Ultimately, it will be the users who determine whether or not the system gets used, and if it doesn't get used, your performance measurement initiative will undoubtedly fail. We can't overemphasize the importance of choosing a system that people actually want to use. For this reason, your system must demonstrate that it can answer these questions:

#### **Is it clear?**

Users must be able to easily understand the information shown and to quickly identify problem areas. Desirable characteristics are color-coded displays to indicate performance issues, data trend graphs and performance commentaries, all of which will aid users in their interpretation of the data being presented.

#### **Does it give access to the information users need?**

Users should be able to view the information presented, as if it were a printed report and also interact with the system in various ways. They should be able to select the information that interests them, look at performance on an 'exception' basis, 'drill down' into further levels of detail when they want, and look at other information, documents, internet sites, etc. which are relevant to the measure or topic which is being viewed.

#### **Is it easy to learn and use?**

In order to achieve widespread acceptance within your user community, your selected system will have to be easy to use and learn. If not, usage will be restricted to only those users who are technically sophisticated, excluding a large proportion of the key players in your organization. Training should demand no more than a couple of hours of a 'non-sophisticated' user's time – and more advanced users should be able to use the system with little more than a quick introduction.

### ***WARNING - Beware the spreadsheet expert!***

*In every organization there's a spreadsheet (or Lotus Notes, or whatever) guru who can promise to deliver a fantastic performance measurement solution at a fraction of the cost of an alternative in-house or packaged solution. You should ask these questions before allowing such a system proposal to proceed:*

- *Are you taking account of the cost of the weeks or months of 'high-priced programming' involved?*

- *Is the system documented and maintainable?*
- *Is the result networkable, distinguishable & multi-user enabled?*
- *Has it been thoroughly tested?*
- *How easy is it to make changes?*
- *Who's going to continue to refine and develop the system - and at what cost?*
- *Most importantly, is this a solution that users will actually want to use?*

### **What are the technical issues?**

Your Information Technology department may well have some very strong views about any system that can have such a major effect on the direction of the organization.

The temptation to develop your own in-house system should be approached with caution. You would not even think about developing a Word Processing, Project Management or Spreadsheet package. Why would you develop a Performance Measurement solution?

In practice, most IT professionals understand this principle and take a pragmatic approach. They realize the need to devote internal resources to other priorities related to legacy systems – or even potential ‘crises’ like the year 2000!

However, an IT department will want re-assurance on a number of technical issues, which any system you develop or purchase should satisfy.

A ‘packaged’ solution should be technically sound, following industry norms and avoiding conflicts with other programs in the environment.

It should also require minimal ongoing maintenance. The programs should generally be loaded from a server and provide a simple installation procedure. The installed components should be automatically replaced when a new version of the program is installed on the server, and databases should be robust and require the minimum possible amount of IT attention.

### **How to translate measurement into management**

The sole purpose of implementing a Performance Measurement solution is to positively impact people’s behavior. To do this successfully, you need to follow a well-structured implementation process and to take account of some simple guidelines.

#### **Define the full scope of your Performance System**

Our experience suggests that there are definite advantages in mapping out the full scope of your Performance Measurement initiative at an early stage. While this first attempt cannot be expected to be perfect, it will nonetheless help generate ideas and involve all the key players.

You should also prepare a ‘situational assessment’ to give an indication of the availability of data in each area of your Performance View.

#### **Start with a pilot view**

Experience with many large and small organizations has shown that the best approach is to start with a relatively small ‘pilot’ area, rather than attempting to implement the full system in a

single concentrated effort. We recommend that you select an area for your pilot view that has the following characteristics:

- Has measures which are well defined and widely recognized.
- Includes a wide variety of measure types and does not focus primarily on financial data.
- Requires input from a number of functional areas.
- Good availability of data.

For these reasons, in a larger organization, you may want to focus on a relatively narrow area (like Customer Service) or else select a small operating unit, or division.

The Pilot View will typically result in a fully operational reporting system, and should be followed by training and a review session to evaluate learning experiences from the process. Using appropriate tools and expert assistance, a pilot view can be completed within 2-4 weeks.

### **Develop a rollout strategy**

Following a successful pilot view implementation, you should plan a rapid rollout of Performance Measurement throughout your organization.

Each new area should follow the basic structure of the pilot view, and should be reinforced by appropriate training and post-implementation review sessions to ensure consistency throughout the entire process.

### **Success guidelines**

There are a number of factors that can help to make your implementation a success:

#### **1. Demonstrate commitment from the top**

- A performance measurement system can only succeed if the company's leadership is committed to direct the initiative throughout the organization.
- There will always be players with an interest in 'scuttling' the process. They may be more comfortable with the status quo and anxious to dismiss this initiative as a 'passing fad', or they may fear more accountability because of the increased visibility of their own performance. The best way to bring these people on board is to demonstrate why and how this measurement system is useful for everyone wanting to improve performance.
- Management must illustrate how it will make performance measurement an integral part of business. Clear communication from the top management team will help convince all stakeholders that the initiative will succeed.

#### **2. Daily use**

Any performance measurement solution needs to become an integral part of the corporate culture in order to be successful. We all know what can happen to a poorly executed strategic plan – a huge amount of effort can go into its preparation and then it can sit gathering dust on a manager's shelf. If you want your solution to be accepted, it must be constantly visible. Your objective should be to have the key players in your organization constantly referring to the information you are capturing – and to make your system their primary mechanism for accessing key performance data.

### **3. Training and Education**

- Do not underestimate the importance of a well-structured training and education program in achieving a successful outcome.
- Education focuses on the principles and advantages of a balanced approach to performance measurement. It emphasizes the link between everyday activities and achievement of the organization's strategic objectives.
- Software training for system administrators, who will handle the more technical aspects, and for end-users, will also be required.

### **4. Link to Performance Management**

Getting people to use any performance measurement solution depends on how well the solution links measurement to management and work practices. One way of ensuring that this linkage is clearly recognized is to tie performance incentives to achievement of desired targets.

Remember, 'what gets measured gets done'. You could extend this analogy further to 'tell me how I'm rewarded and I'll tell you what my focus is'.

You should ensure that there are regular updates to individuals on the key measures on which they are being judged. Waiting until the end of the year (or even quarter) will result in less opportunity to take any corrective action that may be required.

### **5. Communication**

We suggest that you make your interactive computer reporting system as widely available as possible. Typically, the costs of adding users is quite small in relation to the upfront acquisition or development costs, and this will help foster an environment of involvement rather than exclusion.

However, there will always be employees who do not have access to suitable technology and you should maintain their attention on Performance Measurement by the use of newsletters, bulletin boards, employee meetings etc. You might also consider putting in place a suggestions / complaints system to further enhance the quality of the information being captured in your system.

#### **Motivation**

The information that you are now capturing will drive improved focus and better performance, but, mishandled, could also be a demotivator.

Performance shortfalls should be treated as opportunities rather than problems and equal emphasis should be given to positive performance. If this is not done, the system will likely not be widely supported and used.

You need the support of all players to make this initiative a success. People have ways of undermining the credibility of systems that they regard as threatening.

### **Continuous improvement**

Remember that your Performance Measurement system will never be complete. You should plan a periodic review process to question:

- *Are we measuring the right things?*
- *Is performance measurement changing the way we do business?*

- *What improvements and additions can we make to the system?*

In order to ensure that you are not continually 'moving the goalposts', we recommend that you make changes on an annual or semi-annual basis, and explain to the key players what is being changed and why. Ongoing involvement of the key players in your organization will ensure their buy-in to the performance measurement solution, and position you for long-term success.

***“If you aren't measuring it, you are only practicing.”***

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