Multidimensional Performance Measurement Using the Balanced Scorecard
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Executive Summary

- An organization's financial performance results from decisions made by its managers and employees.
- Managers and employees need operational performance metrics that are aligned with the daily decisions being made, rather than a high-level set of financial metrics that are reported on a monthly or a quarterly basis.
- The Balanced Scorecard (BSC) represents a set of financial, customer, operational, and organizational metrics that capture multidimensional aspects of performance.
- Using a BSC, top management can signal strategic objectives to managers and employees. Top management can then gather data that shows whether or not performance at the individual and the strategic business unit levels is aligned with the strategic objectives of the firm.

Introduction

For generations, many businesses have measured organizational success based on a narrow set of financial performance measures, such as operating and net profit, return on investment, and earnings per share of stock. Financial performance measures are valuable in that they capture the economic consequences of business decisions; however, they tend to be “lagging” indicators of performance that report the financial effects of operational business decisions weeks or months after the decisions have been implemented.

Organizational managers and employees typically manage their work in terms of physical flows and other nonfinancial resources. For example, sales managers focus on market size, sales volume, share of wallet, customer satisfaction, and similar measures. Production managers concentrate on production capacity, throughput time, quality, and productivity metrics. Human resource managers are responsible for hiring appropriately skilled personnel, maintaining a safe and legal workplace, and organizational development outcomes. Managers and employees throughout the organization make decisions and use resources that eventually impact the financial outcomes of the firm; to do so effectively, they need performance feedback that links the outcomes of their decisions to the strategic and financial goals of the firm. This feedback is most useful when it is a “leading” performance indicator, or one that is closely related to the work being performed. The Balanced Scorecard (BSC) was developed as a management tool to help managers better understand and link customer, operational, and organizational decisions to financial outcomes, and to the strategy of the organization.

BSC Basics

While General Electric has been credited with developing one of the first balanced scorecard performance models,1 the BSC concept was first described by Dr Robert Kaplan and David Norton in a series of Harvard Business Review articles in the early 1990s, and was subsequently expanded upon in books and articles by these and other professionals. The BSC as a management tool has gained widespread acceptance in the corporate world. In a survey of more than 700 companies operating in five continents, Bain and Company reported that 62% of the respondents used the BSC.2

BSC perspectives typically include financial, customer, operational (internal business processes), and organizational (learning and growth) aspects. By identifying key performance measures within each of these perspectives, top management signals strategic objectives and organizational goals to managers and employees. By receiving feedback on achieved outcomes for each of these measures, management is able to evaluate how closely performance is meeting strategic objectives.
As shown in Figure 1, the four traditional BSC perspectives are interlinked, and are linked to the overall vision and strategy of the organization. Each perspective reflects a focus area for the implementation of strategy and, therefore, for performance measurement.

**Figure 1. Linking of BSC perspectives**

- **Financial perspective**—focuses on financial aspects of performance, and links strategic objectives with financial impacts. Balance sheet, income statement, and cash flow performance measures are often included in this dimension. Some firms include alternative measures of financial performance, such as economic value added, recycling income, and sales growth by channel.
- **Customer perspective**—contains measures that reflect how the firm is creating customer value. Customer satisfaction measures are typical, but leading firms will include measures such as share of mind and share of wallet, consumption per capita, customer retention, and product accessibility measures.
- **Internal business processes perspective**—focuses on how a company is performing through an operational lens. Internal business processes encompasses many facets of operations, including engineering design, purchasing, manufacturing, distribution, and environmental and social performance. In a customer service organization, measures might include response time, process quality, employee productivity, and bridge to sales ratios.
- **Learning and growth perspective**—assesses how well the organization is preparing itself and its employees for the future. This perspective often includes measures of organizational practices, employee development and satisfaction, and systems development and deployment. Aspects commonly measured in this perspective include employee turnover, diversity, promotions from within, training hours or expense by employee, innovation measures, and surveys of corporate climate.

**Implementing a BSC**

The BSC is not a “one size fits all” management tool. Each BSC is unique to the strategy, objectives, and culture of the individual organization. However, the following guidelines are important to any successful BSC implementation.

**Stakeholder participation in BSC development**: Every top management team employing a BSC must carefully translate the organization’s strategy into meaningful and actionable performance measures. This process requires the participation and input of the organizational stakeholders who are either impacted by the strategy or responsible for implementing the strategy. For example, building a set of customer-related performance measures is difficult without understanding customer needs and perceptions. Similarly, requiring a firm’s workers to focus on improving quality metrics without involving these employees in discussions about quality creates a disconnect with those responsible for implementing the improvements.

**Create cascaded scorecards that are organizationally appropriate**: At higher levels of the organization, management will be focused on performance outcomes that reflect the overall company strategic objectives. But, a high-level scorecard would not be appropriate throughout the organization. Some firms develop scorecards at the individual employee level. For example, a high-level objective in a firm’s BSC might be “increase market share.” In the marketing area, this objective might be broken down into mid-level objectives, for example, “increase market share in Europe,” “increase market share in Asia,” or “increase market share of customers aged 18–25 years old.” At the individual level, this objective could be further defined in a way that reflects the responsibilities of that marketer, such as “increase market share in France” or “increase market share in China.” Alternatively, the objective might be related to a specific product or service. The goal
of cascading is 1) to translate the strategic objective into specific objectives for the hundreds and thousands of employees throughout the organization that carry out the day-to-day work; and 2) to link the work of each employee and strategic business unit to the overall strategic goals of the organization by defining measures appropriate to the employee and business unit.

**Define linkages between measures:** Value creation in any organization is accomplished by understanding and creating synergies between the various aspects of organizational performance. Increasing sales without having the corresponding production or service capabilities will likely lead to loss of value rather than a long-term increase in value. Increasing production output at the cost of reducing product safety and reliability will negatively affect quality, costs, and reputation. An effective BSC explicitly shows the cause and effect linkages between key performance indicators. A leading insurance company was concerned about its market stock price. By evaluating company data, company managers determined that the amount of time it took a claims adjuster to contact the customer following an accident could influence market stock price. How was this so? The study showed that the length of contact time influenced customer satisfaction, which influenced policy renewal rates, which led to revenues from premiums, which ultimately influenced operating income and stock price.

**Choose a small set of focused measures:** Each BSC should contain a small set of performance measures, generally with not more than 15–20 recommendations for any single BSC. Developing a limited set of measures is challenging, but forces managers to focus on the most important aspects of organizational performance. Having too many measures tends to create “noise” in the process, both for the managers and for the employees who are working toward the stated goals, leading to uncertainty about which measures are key drivers of success.

**Create balance in the scorecard:** To be “balanced” does not mean to be equal in all dimensions. A balanced scorecard is one that contains:

- multiple perspectives of performance;
- leading and lagging measures;
- internally focused and externally focused measures;
- short-term and long-term measures;
- quantitative and qualitative measures.

**Link the BSC to employee compensation:** An effective BSC sends a message to employees that “strategy is everyone’s job.” If this is the case, then firms need to reward employees for carrying out the strategic intent of the organization. If the objectives and measures within the BSC are aligned in such a way that value is created by carrying out these actions, then employees should be rewarded for increasing the firm’s value proposition. Organizational development research has shown that linking reward systems to explicit and controllable expectations creates strong linkages between employee behaviors and the achievement of organizational goals.

**Figure 2. Revenue growth strategy**

**Case Study**

**Mobil Corporation**

In the early 1990s, Mobil Corporation’s North America Marketing and Refining group (Mobil) implemented a strategy that resulted in an increased return on capital from 6% to 16%, and an improved operating cash flow of over $1 billion per year.\(^4\) This dramatic improvement in financial results was achieved in just three years, and was aided by a BSC implementation to help focus and align the organization.

In 1994, Mobil began a BSC project as a means to help communicate and implement a strategic organizational change. Mobil’s new strategy was twofold:

1. increase volume and revenues of premium products; and
2. reduce costs and improve value chain productivity.

Mobil began by defining its high-level financial objectives—return on capital employed and net margin—and then disaggregated these objectives into specific objectives related to its revenue growth and productivity strategies. An example of Mobil’s objectives in relation to its revenue growth strategy is shown in Figure 2.

After developing the financial perspective of the BSC, Mobil’s managers developed the customer, internal, and learning and growth perspectives. The customer perspective focused on customer satisfaction and dealer relationships, using specific performance measures to capture achievement on each objective. The largest set of measures were the internal business processes measures, which included new product volume and profitability, dealer quality, refinery performance, inventory management, order quality, and safety measures. In the learning and growth perspective, the firm focused on measures such as an employee climate survey, core competency achievements, and the availability of strategic information.

Each perspective contained a small set of focused and interlinked measures that were keys to achieving corporate strategy. The development of the BSC was accompanied by a realignment of organizational structures, the use and communication of the new measurement system, and linking compensation with meeting the explicit goals and objectives. The outcomes for Mobil were dramatic—surveys showed that employee awareness of strategy increased from 20% to 80%, safety and environmental statistics improved, lost yield was reduced by 70%, new products were being introduced, volume growth exceeded the industry averages by over 2% annually, cash expenses were reduced, and Mobil’s relative profitability within the North American oil industry improved from last to first in class. Each of these improvements had an impact on increasing Mobil’s operating cash flows and return on capital employed. The BSC helped management to communicate corporate strategy through a set of strategic objectives and specific goals, essentially aligning the organization toward a common set of objectives.

Conclusion

The BSC is a powerful concept that enables organizational change. The BSC is not just a performance measurement tool, but a multidimensional system that requires management to define strategy in operational terms, and to understand and communicate the cause and effect relationships between the work performed at all levels of the organization and the high-level strategic goals. An effective BSC communicates strategy throughout the organization, thereby signaling to the employees what achievements are needed to implement strategy. A BSC also serves to communicate results back to management, using measures that link into specific strategic objectives. By having such a detailed map of strategic intent and accomplishments, both managers and employees can become more effective in their work.

Making It Happen

- Top management involvement is key—The BSC is a strategic management system that is used to change organizational culture, making strategy everyone’s job. This change cannot happen without the involvement of top management.
- Translate strategy into operational terms—Strategic objectives must be linked to specific operational perspectives, objectives and indicators. In effect, the BSC “tells the story of the work.”
- Link measures within and between the perspectives—All measures should lead to increasing value for the organization. Management should be able to articulate the cause and effect relationships between the measures, and the paths by which the measures link to each other and to organizational value.
- Cascade the BSC throughout the organization—BSCs can be created for each strategic business unit, for departments within each business unit, and, ultimately, for each employee. These cascaded BSCs help to define the performance objectives into meaningful metrics that link the work being performed at all levels of the organization to the strategic goals of the firm.
- Link the BSC to compensation—By rewarding employees for specific performance outcomes that are linked to strategic objectives, alignment is created between the work being done and the broader strategic goals of the firm. There is a cause and effect relationship between “what gets measured, gets managed” and “what gets rewarded, gets attention.” By rewarding the specifically defined actions that create value, management is assuring that employees are focused on doing the right things.
More Info

Books:

Websites:
- Balanced Scorecard Institute: balancedscorecard.org
- *Balanced Scorecard Report:* harvardbusinessonline.hbsp.harvard.edu/b02/en/newsletters/news-bsr_home.jhtml
- Management and Accounting Web: www.maaw.info
- Optima Media Group Business Intelligence. See the “Performance Measurement Portfolios” for BSC information: www.business-intelligence.co.uk

Notes


2 Ibid.


See Also

Best Practice
- Enhance Competitive Performance via Critical Key Performance Indicators (KPIs)
- Everything You Need to Know About Benchmarking
- Value Creation—Perspectives and Implications

Checklists
- Assessing Business Performance
- Understanding Strategy Maps
- What Is Benchmarking?

Finance Library
- Balanced Scorecard: Translating Strategy into Action
- Cost and Effect: Using Integrated Cost Systems to Drive Profitability and Performance

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