Performance Measurement, Strategy Formulation and Management
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Introduction

Performance measurement is designed to support organizational strategy and operations. It should be designed so organizations get better at managing and improving the value created from their intangible assets, such as corporate expertise, brand name, human resources and business networks. These are non-financial management related issues. Thus organizations need to move from purely financial measures to a mix of financial and non-financial measures.

Development of Balanced Scorecard

The balanced scorecard is a performance management system widely used by various types of commercial and public service organizations. More than half of the world's organizations use the balanced scorecard to measure their organizational performance. This technique of performance evaluation and management was developed by Robert Kaplan and David Norton in 1992. A balanced scorecard is a central list of numbers, which show major elements of an organization's success, such as people, operations, financials, suppliers, customers and management systems. The measurements record the factors which contribute to the organization’s performance.

The basic philosophy of the balanced scorecard is that managers and employees tend to focus on what organizations measure. It shows management care about more than obvious financial measurements. If management identifies what determines shareholder value – high customer loyalty, high quality or low price products, etc., then managers can work back to the issues that managers and employees should focus on. The balanced scorecard can direct the organization to focus on the issues which the management decides are keys to their success. There are other benefits, such as improved communication through scorecard measures, future strengths and opportunities, confined areas of information and greater information alignment.

The major issues in designing a balanced scorecard are to:

- Align all employees to realize the common goals and strategies;
- Link initiatives to the organization’s strategy, enabling prioritization;
- Provide feedback to people on key issues, such as sub-unit work places, where they can have an impact;
- Be an important decision-making tool for the organization.
If a single staff member tries to force a system into place, it will not reflect the organization’s key strategies, goals, strengths, and weaknesses. It is unlikely to get the support from staff that it needs. The appropriate steps are first to create a clear business model, and then to choose measurements based on that model. This enhances commitment, brings more agreement on the organization’s direction, increases the improvement speed, and aligns measures with corporate goals.

The balanced scorecard provides four measurement perspectives of measure:

1. Innovation and learning perspective – Linking employee incentives and rewards through the organization’s learning and growth development.

2. Process perspective – Achieving excellence in order fulfillment through continuous improvement in product development, service provision, accounts management and customer response.

3. Customer perspective – Offering complete sales and after-sales services to targeted customers.

4. Financial perspective – Improving sales revenues through expanding business to increase turnover.

Measurements

Financial accounting measures have dominated organizational performance measurement in the past. One problem with this is that they are lag indicators, only reporting on past performance. They are also measures of short-term results. Basically, financial measures promote short-term strategies at the expense of long-term value development. They reflect a limited perspective of the whole organization and factors influencing profitability. They ignore value of intangible assets, reporting mainly on financial outcomes and consequences of past actions.

Target Setting

Target setting is the performance goal or the rate of improvement required for a measure. Targets are set to represent excellent performance. These targets should, if fulfilled, make the company one of the best performers in the industry. These targets can create distinctive value for customers and shareholders.

The targets set are reflected as various measures in the balanced scorecard’s perspectives. Organizational strategy links sub-unit performance with organizational strategies at various stages of the business. Basically, an organizational strategy should fulfill two important functions:

1. Seek a competitive advantage by positioning the organization in its business environment with products and/or services to provide customers a better service than its competitors.

2. Provide clear guidance on how internal resources should be allocated to gain a competitive advantage in business.
Balanced Scorecard and Strategy Mapping

Kaplan and Norton (2000) developed the strategy map to transform the balanced scorecard from a performance measurement system to a strategic performance management system.

Strategy maps integrate the four perspectives of the balanced scorecard to provide a new framework for describing and implementing strategies. To Kaplan and Norton, a strategy map is a logical comprehensive architecture for illustrating strategies. It lays out the foundation for designing a balanced scorecard that acts as the cornerstone of a strategic management system (Kaplan and Norton, 2001).

Construction of strategy maps needs agreement, precision and assurance to be adopted as strategy at the executive level. This involves:

- Illustrating the desired state of development for the organization: desire and state the mission, vision and value drivers.
- Specifying objectives in the scorecard areas for contributing to the organizational strategy. The main contributions of the strategy map are the clarification and links between performance drivers and their impact on progress towards strategic success.

Strategy Map Development

From a balanced scorecard viewpoint, strategy maps are communication tools adopted to tell a story of how value is created. They provide a graphical presentation of the organization's primary objectives and the essential cause-and-effect relationships that are produced among them, finally leading to the organization's performance (Kaplan and Norton, 2000).

Strategy maps describe a step-by-step and logical connection between strategic objectives in the form of a cause-and-effect linkage. They start from the innovation and learning perspective as the foundation level, followed by the process perspective at the second level, then the financial perspective and finally the customer perspective at the top level. Strategy maps demonstrate how an organization makes use of its financial, management and human resources assets and then converts them into the desired outcomes (Kaplan and Norton, 2000).

Strategy maps are about the techniques of concept mapping. Figure 1 below is an illustration of such a concept map. Once maps have been drawn, linking actions and their impact operations can be managed to achieve desired outcomes. A strategy map illustrates the causal relationship among the strategic objectives across the four perspectives: innovation and learning, process, financial and customer.
The above strategy map links and integrates the development of the four perspectives of the balanced scorecard. Based on innovation and learning, organizations employ strategic information and develop strategic skills for conducting three processes:

1. **Product development** – be familiar with customers, provide responsive services, then launch innovative products.

2. **Attract customers** – launch innovative products.

3. **Manage accounts** – attract and move customers to cost-effective channels.

These product development and internal processes help organizations to cross-sell various related products, build customer confidence, and improve customer satisfaction. Finally, organizations improve sales revenue and return on investment. Their cost structure can be simplified as a result of learning and innovation. These continuous processes are gone through again and again, contributing to business improvement.
Concluding Remarks

The balanced scorecard integrates measures derived from an organization’s strategies. While maintaining financial measures of past performance, the balanced scorecard presents the drivers of future financial performance. The other drivers (innovation and learning, process and customer) are chosen from a rigorous and explicit translation of the organization’s strategy into specific objectives and measures. The advantages of adopting the balanced scorecard are that the organization can integrate the measurement system into management processes that communicate the strategy to employees, aligning employees’ individual objectives with successful strategy with the management processes: planning, budgeting, reporting, performance measurement and management control.

References: