

CHAPTER 1

Overview



After reading this chapter, you will be able to

- Understand what the difference is between monitoring, measuring, managing, and direction setting.
- Understand why the essence of Balanced Scorecard is not measurement but direction setting.
- Know what the blind spots in business are.
- Understand the strategic paradox set up in business and how BSC assists as a solution.

Ancient cultures recognized the importance of measuring the passage of time, as well as the need for standards for recording transactions and communication. They were preoccupied with measuring time, size, and weight. Records show that the Babylonians and the Egyptians measured days and months more than 5,000 years ago. Many used the celestial bodies as a guide to these measurements.

The challenges of travel to far-off lands over the water brought about the greatest of all obstacles. Many a ship sank because its crew lacked the understanding of where they were with respect to land. By 150 A.D., however, Ptolemy had reduced the known world into 27 maps,¹ and created the first world atlas, which greatly aided ships in navigation. He knew of latitude easily because the equator was right in the middle of the earth. Zero degrees longitude was the true challenge.

Longitude had to be measured using time—that is, both time at land and current time. It took John Harrison, working between 1730 and

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1770, to look beyond the stars (the tools of Galileo and Isaac Newton) and find the mechanical timepieces that could withstand the hazards of travel.

Essence of Balanced Scorecard

Just as great ships must chart their position before undergoing ocean voyages, businesses must measure their position before knowing their direction. The challenge has been in finding the tools to measure these organization's "voyage." The true fallacy of measurement is that it is not an end but a means to a new beginning. Measurement is the driver of the next direction, not just the documenter of today's position.

But measurement has gotten a bad rap. It is viewed as punishment in management clothing. If you call it *accountability*, many believe it to be accounting and a precursor for layoffs. The operational value of measurement has been accepted in manufacturing but when accountants walk the floor, measurement takes an entirely new branding.

Business needs measurement that can sustain the changing tides of the climate of commerce. Businesses hunger for a framework to measure its location in the continuous journey to its final destination or goal. From this measurement comes the rudder of management, and from the rudder comes direction.

Balanced Scorecard (BSC) is born from this rich history of measurement and serves the same purpose to business as the timepiece served the ancient mariners. BSC attempts to move businesses from monitoring to measurement; from measurement to management and from management to direction setting:

- *Monitoring*. The art and science of observing employee behavior and coaching
- *Measurement*. The art and science of gauging, using numbers and metrics, performance to a task

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- *Management.* The art and science of motivating, coaching, and enabling individuals and teams in the achievement of an objective
- *Direction setting.* The art and science of discovering strategic directions that are unique and differentiating in the marketplace, communicating this to all levels in the organization in the form that they can identify and co-relate their day-to-day actions to the goals

Many organizations are fearful of measurement because it symbolizes accountability and, in some ways, documents a weapon to terminate employees.

But if we believed ourselves to be in the same boat, trying to take on a new journey to a new land, we would measure where we are and how far we have to go. The basis for any action plan is knowledge. Knowledge, using Balanced Scorecard, is purposeful and focused on strategic action—that is, translating strategy into day-to-day action plans and initiatives.

Why Balanced Scorecard?

Corporations, both big and small, can fail for several reasons. But the most significant cause of failure is not a lack of strategy, but the incapacity to execute on a balanced strategy. Balanced Scorecard exists to serve this incapacity.

Its founders, Professor Robert Kaplan, from Harvard Business School, and David Norton, a consultant, put together a research study to evaluate and understand new methods for measuring performance. They assembled key organizations to help them formulate this understanding. The teams set about to formulate a new method that would not rely so much on just financial metrics as measure but would show a balance of financial and nonfinancial perspectives. The outcome of this process is

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**TIPS & TECHNIQUES**

Now more than 50 percent of the Fortune 1000 and 40 percent of companies in Europe use a form of the BSC according to Bain & Co.^a In addition to this, Balanced Scorecard serves to bridge several other dichotomous elements of strategy. Organizations are asking fundamental questions about their strategy and have come to realize that balance in strategic objectives is key to making strategy actionable. Without this balance, most of the organization seems not represented in strategy. Consider the following key questions to understand if BSC is for your organization:

- Is our strategy one-sided and only focused on financial gains and targets?
- How do we know if the measures that we review are looking farther ahead or just lagging indicators of past performance?
- Do our measures and goals cover all aspects of the enterprise, or are they just based on the structure of our corporation, that is, are they just data from silos of business units measuring their unique targets?
- Do we really understand what drives our business?
- Do we have a handle on what actions cause other results?

^aAndra Gumbus and Bridget Lyons, "The Balanced Scorecard at Phillips Electronics," *Strategic Finance*, access at www.bettermanagement.com/library.

the Balanced Scorecard.² It is *formalism*, a method that translates strategic themes to actionable and measurable objectives that are ready for execution at all levels of the organization.

In good times, profits soar and corporations seldom care why or what causes success. Often, they believe that being in the "right place, right time" is O.K. When these businesses turn sour, they scramble for answers. It seems that, in great times, corporations don't listen to any-

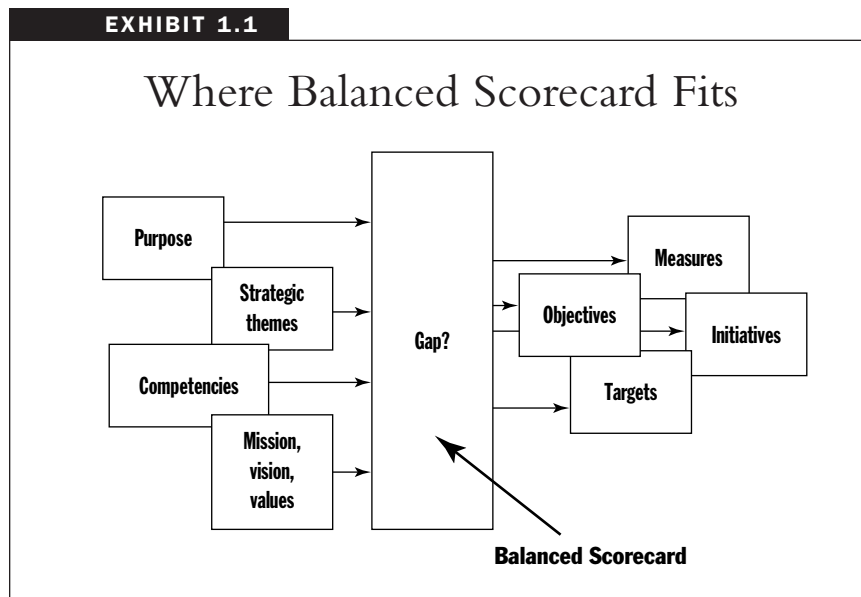
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thing. When times get rough, they seem to listen to everyone and use any method to get themselves out of trouble.

Management is the art of knowing how and what to deploy during both rough and good times because management is acyclic in behavior. Balanced Scorecard is one such methodology that identifies and formalizes the main drivers to the business and provides a quick view of your corporation's strategic health.

Balanced Scorecard is focused on uncovering the main nonfinancial drivers of the business, along with the economics of the business. Balanced Scorecard shows you a way to make strategy actionable. As a framework for action, it can be updated and creates a renewable methodology and framework.

Consider Exhibit 1.1, which illustrates the issues surrounding a strategic framework for action. Usually, strategic planning exercises drive for aligning *vision, mission, values, and strategy*. They also discuss items such as competencies, strengths, weaknesses and opportunities, and threats. This method is often called SWOT analysis, which is a way for organizations



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to ensure that all elements of the business are incorporated into a strategic plan in the marketplace. Hence, the exercise usually covers the internal and external challenges that a corporation is facing and will face, in an attempt to look ahead and find the next big thing.

Meanwhile, the corporation is running along driving to current measures at the operational level, and the challenge comes when the senior management wishes to drive new strategies into the organization. BSC fits this purpose of providing a framework for aligning strategy to the tactics, with corresponding objectives and measures. Exhibit 1.1 shows the gap filled by the BSC.

Business of Blindspots

Corporations have always measured things that matter to them. Hence, to claim that any methodology enables the measurement of the *right* things is ludicrous and somewhat condescending to preceding methods that have been introduced.

It would seem that corporations sometimes measure too much of some things and too little of others. It would also seem that many of these measurements are unintegrated, serve the wrong goals, and form a paradox within the corporation where forms of measurement compete with each other, falling short of the overall strategic goals of the corporation. Many corporations lack an overarching model for monitoring, measuring and managing the business. Balanced Scorecard offers a broad and overarching skin to the structural architecture of the business.

Avoiding Strategic Paradox

There are two forms of *strategic paradox* in strategy formulation and execution:

1. Mistakenly viewing strategy as operational effectiveness
2. Mistakenly assuming that strategy and actions in an organization are always aligned

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According to Professor Michael Porter, strategy has been viewed in the context of *operational effectiveness*. Using the language of activities, he has outlined a way to differentiate between strategic positioning and operational effectiveness.³ Using activities, operational effectiveness is performing similar activities better than rivals, while strategic positioning is performing different activities or performing similar activities differently. When organizations do anything that appears to be a competitive advantage using operational effectiveness, others often follow. W. Chan Kim, Boston Consulting Group Bruce D. Henderson professor of International Management at INSEAD in Fontainebleau, France, and Renee Mauborgne, a senior research fellow at INSEAD, put it well: "The trouble with forging a highway is that if you are right, imitators will follow. Then you are back into protecting your base and become subject to conventional wisdom."⁴ Professor Porter emphasizes that benchmarking only makes companies similar. Porter emphasizes the value of strategic positioning over operational effectiveness (see Chapter 4). Just using Balanced Scorecard to identify and improve the activities in a company of the business does not forge a competitive advantage. However, there is tremendous value in using BSC to align the entire organization to strategy.

Finding Competency in Strategy Alignment

Many executives lock themselves in conference rooms or resort hotel rooms to uncover their organizational strategy. But strategy formulated with no regard to strengths and weaknesses in capability is blind strategy. The true power of strategy can only be expressed in work performed. Hence, the real challenge seems to be, not only strategy formulation, but also the ability to create an operational framework to execute the strategy. Many executives tell me that the most important competency of all is the competency of being able to execute on goals.

Furthermore, the business world is guided by *change*. And change can affect business models drastically. Mergers and acquisitions can transform

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the competitive landscape as power shifts. Hence, sticking to a good-looking strategy when strategic variables change can be dangerous. For companies to be effective, they must have as much ability to change their strategy as to formulate one. This is characterized by several capabilities:

- The ability to formulate strategic thrusts or themes—that is, several key strategic differentiable objectives for focus and strength
- The ability to institutionalize and operationalize these thrusts into key activities or sets of activities if performed would enhance and enable the key strategy
- The ability to change the emphasis and manage resources of these strategic thrusts adapting the underlying set of activities quickly

Strategy without strategic alignment to key organizational activities renders organizations impotent. The strength of a resilient organization comes from its ability to change its strategic thrust and reflect it in actions and corresponding performance measures. This connection between strategy, strategic thrusts, and activities can be achieved using BSC. For example, consider a high-technology CRM company that competes in the fast-paced contact information business. This company might have the following elements to strategy alignment:

- *Strategy.* Dominate, with 60 percent share, the XYZ market by building a direct consumer focus.
- *Strategic thrusts*
 - Be the leader in direct consumer marketing.
 - Establish and dominate in customer service.
 - Align with larger player by providing the most reliable CRM subsystems for them.
- *Key activities.* Activities serving strategic thrust are
 - (a1, a2, a4)
 - (a4, a5, a8)
 - (a4, a9, a7) where a = key activity like “provide contact management at lowest cost”

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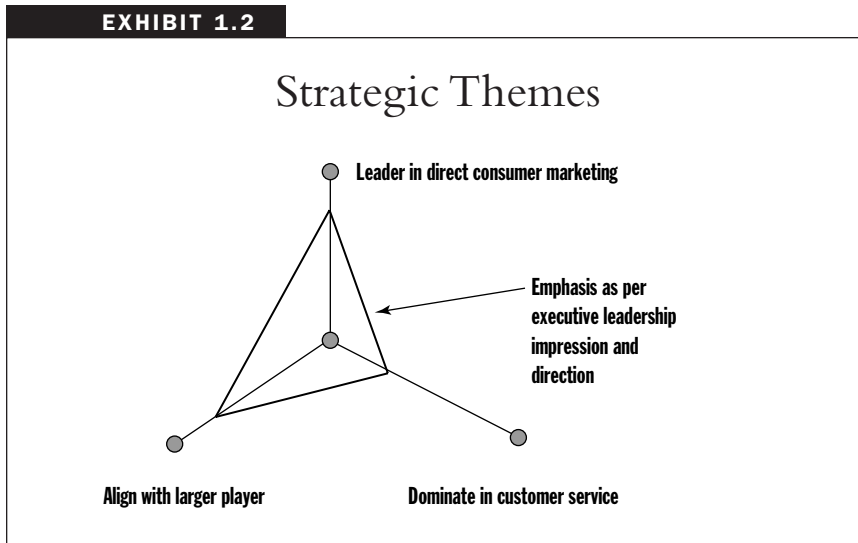


Exhibit 1.2 illustrates such a strategy with emphasis in order of priority.

Michael Tracy and Fred Wiersema,⁵ authors of *Discipline of Market Leaders*, list three strategic thrusts to market leaders:

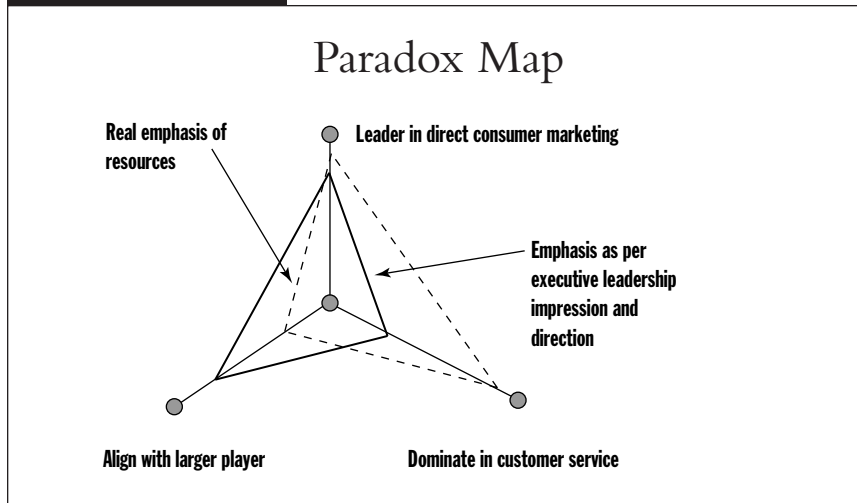
- 1.** Operational excellence
- 2.** Product leadership
- 3.** Customer intimacy

Various sets of activities, if optimized and combined in the right way, can make these themes actionable. Meanwhile, management will establish the priority of the strategic thrusts as shown in the Exhibit 1.2.

In actual truth, the emphasis of activities with respect to the themes is shown by the dashed lines in Exhibit 1.3. This exhibit illustrates the organization's focus with respect to its emphasis on one axis or the other. For example, the organization states that its focus is customer over operational power. A Paradox Map compares where resources should be emphasized to achieve the strategy of the company against what work is currently being performed.

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EXHIBIT 1.3



One of the greatest challenges that BSC solves is misalignment between the strategy and the real work being performed. BSC avoids the strategic paradox in which the CEO thinks the strategy is working in action when in actuality, the strategy and the real work, as defined by the activities of the organization, are not working in concert.

As Craig Weatherup of PepsiCo claimed, eventually strategy leads to processes because “capability comes only by combining a competence with a reliable process.”⁶ Strategy is realized in the unique combination of activities and processes, but the key tool for aligning strategy and the primary activities of an organization is the Balanced Scorecard.

Summary

Balanced Scorecard serves the needs of a large portion of the Fortune 1000 who are in deep need of making strategy actionable. BSC is also designed to ensure that performance metrics and strategic themes are balanced with financial and nonfinancial, operational and financial, leading and lagging indicators.

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Organizations seek to translate strategy to key actions. A syndrome among many companies called strategic paradox can slow progress. This syndrome manifests itself in the form of disparate, disconnected actions in the core of a company when the upper management believes that the company is acting on a strategy and that the strategy and actions in the organization are always aligned. The paradox expresses itself as a misunderstood strategy. Balanced Scorecard attempts to remove this paradox and align all activities to the true purpose of the strategy.

