

# **Strategic Performance with Balanced Scorecards**

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# Accelerating Strategic Performance

*The essence of strategy is choosing what not to do.*

Michael Porter

The rate of change in the business world is accelerating. To get ahead — in fact, to just keep up — organizations of all types must accelerate their strategic performance.

They have to work with higher performance, more precise focus, and better strategic alignment. For this to happen, all parts of the organization must clearly understand and be firmly aligned with strategic goals.

In the last two decades, a strategic management system has been developed that enables organizations to achieve the clarity and alignment necessary to accelerate strategic performance. That system is the Balanced Scorecard.

## Managing with a 500-Year-Old System

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Until recently organizations have used the same accounting system to track assets and value production that was used 500 years ago in Venice, Italy. In 1494 Fra Luca Pacioli, Franciscan monk and friend of Leonardo da Vinci, wrote *Everything about Arithmetic, Geometry, and Proportions* (see Figure 1.1). It was the first best-selling business book to come off of Gutenberg's printing press.



**Figure 1.1:** Over 500 years ago, Fra Luca Pacioli, on the left, documented the double-entry accounting system we still use today.

What made his book such a best-seller throughout Europe was that it contained detailed instructions on how the merchants of Venice kept their accounts using double-entry accounting. His book included sections on:

- Modern accounting cycles
- Double-entry accounting
- Journals and ledgers
- Assets, liabilities, capital, income, and expenses
- Closing
- Trial balances

The reason his book blazed through the halls of commerce in Europe was because for the first time it gave businesspeople a way to value their tangible assets and measure how they were producing value. But what is surprising is that we still use the same accounting system used by the merchants of Venice 500 years ago.

## **The Failure of Modern Management Systems**

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Research by Margaret Blair of the Brookings Institute into the market value of corporations listed in the Compustat database shows that the market value of U.S. corporations has shifted significantly from tangible to intangible assets. In the

ten years from 1982 to 1992, the contribution of intangible assets to market value has risen from 32 percent to 68 percent. As shown in Table 1.1, subsequent studies from multiple sources estimate that since 1998, intangible assets' contribution to corporate value is approximately 85 percent.<sup>1</sup>

**Table 1.1:** The growth of intangible asset contribution to corporate value

	INTANGIBLE	TANGIBLE
1982	32%	68%
1992	68%	32%
1998	85%	15%

How can intangible assets such as people, processes, patents, and data be monitored and managed effectively using a 500-year old system designed for use with tangible assets?

Ram Charan, international consultant and co-author of *Execution*,<sup>2</sup> wrote an article in *Fortune* magazine titled "Why CEOs Fail." In writing about highly experienced, well-known CEOs who lead their companies into failure, he said, "In the majority of cases — we estimate 70% — the real problem isn't the high-concept boners the boffins love to talk about. It's bad execution."<sup>3</sup>

Charan goes on to write how most CEOs are hard-working, experienced, brilliant people. His research found one problem common to all the failures:

"Yes, strategy matters. A good, clear strategy is necessary for success — but not sufficient for survival. So look again at all those derailed CEOs on the cover [of the magazine]. They're smart people who worried deeply about a lot of things. They just weren't worrying enough about the right things: execution, decisiveness, follow-through, delivering on commitments."

So executives and managers face two serious problems. First, the source of value production has switched from tangible assets that can be monitored with current accounting systems to intangible assets that are difficult to manage. Second, most corporations fail at executing their strategy.

## A Modern Strategic Management System

In 1992 Harvard professor Robert Kaplan and consultant David Norton published the article, "The Balanced Scorecard — Measures That Drive Performance," in the *Harvard Business Review*.<sup>4</sup> The ideas in this article sowed the seeds of a strategic management system to translate strategy into action, to monitor strategic execution, and to align organizations around strategy.

Initial attempts to use the Balanced Scorecard seemed to either propel organizations to success or burden them with administrative overhead and dismal results. The difference between failure and success was often in the selection of metrics used to measure strategic execution. In 2000 Kaplan and Norton published another article in the *Harvard Business Review* titled, “Having Trouble with Your Strategy? Then Map It.”<sup>5</sup> This article outlined how to build a visual map that shows the objectives and causal links necessary to execute a strategy. It was these causal links that enabled executives to identify the key metrics that drive success. The combination of these two ideas, the Strategy Map and the Balanced Scorecard, combined with more recent developments, has built a strategic management system that is an important part of modern business management.

The Strategy Map is a visual map of how an organization will execute its strategy. The Strategy Map shows the objectives needed to execute the strategy and the causal links between objectives. The Strategy Map is a tool for clear communication and helps identify the “critical few” metrics to monitor strategic execution. You can learn more about Strategy Maps in Chapter 4, “Step-by-Step to Building Your Strategy Map.”

The Balanced Scorecard is part of a system that translates strategy into action. The Balanced Scorecard gives a balanced view in four perspectives of how well an organization is driving execution and how successful the results are. The four perspectives in the Balanced Scorecard and Strategy Map give executives a more balanced view of their organizations, going beyond financial measures to include finance, customer and marketplace, internal operations, and learning and growth — which includes people, culture, intellectual property, and IT infrastructure.

The Strategy Map and Balanced Scorecard can take one to three years to implement in an organization, but the results can be impressive. The effects of a Balanced Scorecard are:

- **Clarifying Strategy.** The discussions and thought that go into developing the Strategy Map bring clarity and understanding to the executive team in terms of the strategy and interplay between departmental silos. The graphical Strategy Map pinpoints for employees how they contribute to strategic success.
- **Translating Strategy into Action and Executing It.** The Strategy Map, combined with a Tactical Action Plan and Implementation Plan, give a clear roadmap to everyone showing how the strategy will be translated into action. The Balanced Scorecard is used to stay on track and to monitor execution.

- **Aligning Business Units around the Strategy.** Most organizations develop “silos,” functional departments or divisions that are more concerned with their own success than they are with achieving success for the entire organization. But developing the Strategy Map and Tactical Action Plan requires that the walls between silos come down. Focusing on Strategic Themes forces departments to work together, breaking down silos even more.
- **Communicating the Strategy to All Levels.** The process of cascading the Balanced Scorecard through the organization gives each level the opportunity to contribute to organizational success. It gives executives the ability to communicate with functional managers about how to achieve strategic goals. It gives functional managers the ability to provide feedback to executives about capability and capacity.
- **Monitoring and Managing Strategic Execution.** Research has shown that most executive staff spend less than 10 percent of their time monitoring strategy and execution. Instead of leading through strategy, executive staff often become embroiled in operational performance, something better left to managers. Using the Balanced Scorecard as an agenda gives executive meetings a central focus on strategic leadership.

## Why Use a Balanced Scorecard?

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Building a Strategy Map and Balanced Scorecard for an organization follows much the same process as taking a trip to a specific location. To take a trip you need to:

- Select a destination
- Agree on the type of trip
- Agree on the route
- Map the route
- Plan time and resources
- Travel
- Stay on course

Leading a business in our high-speed world isn't that different from flying a high-speed jet. Imagine boarding a small jet, pausing at the entry, and asking the pilot a few questions:

*You: “What is our destination?”*

*Pilot: “The crew got together and talked about a destination. We couldn't come to an exact agreement, so we decided to go somewhere out West. If something better comes up while we're en route, we might change direction.”*

*You: “What route will we be taking?” (Maybe I’ll still go. It sounds adventurous, although it could be a waste of time and fuel. It shouldn’t be too dangerous.)*

*Pilot: “Well, we aren’t sure about the exact route, but I’ve been that general direction before, so I don’t need maps. I’m experienced.”*

*You: “I notice that your cockpit dashboard seems a bit sparse. There aren’t any flight instruments — just stacks of paper. How will you monitor the flight?” (This is starting to sound a bit iffy. The pilot may be experienced, but how will she communicate her experience to the copilot, the flight engineer, the steward, the ground crew, other aircraft, and the Federal Aviation Administration?)*

*Pilot: “Well, we’re comfortable with the detail of printed reports. While we’re in flight, I can request a short stack of printed reports that give me airspeed, altitude, attitude, and heading. The copilot gets a larger stack with operational data about radio settings, fuel, hydraulics, and technical details. We have to ask for the data, but it only takes a few minutes to get new reports — so we’re in pretty good shape as long as everything stays stable and we don’t have mechanical, weather, or crew problems.”*

*You: “Sounds like quite an adventure you’re about to embark on. Sorry I won’t be able to go with you.”*

The metaphor isn’t that far from how some organizations manage. Many start-ups and high-tech companies make their strategy going after any opportunity. Although the idea of a pilot flying with reference only to printed reports seems outlandish, consider how many organizations manage while looking only at financial reports. Financials show only lagging results from efforts that may date months before. Doing this is almost the same as flying by printed reports alone.

We know, and recent research confirms, that executives and managers with over ten years’ experience in an industry can have a good “gut instinct” for making decisions, but how can they communicate that “gut instinct” to the hundreds or thousands of people they must lead and manage? How can employees and managers without such experience understand the strategy and make good decisions?

The Strategy Map gives an organization an excellent visual tool to explain what is important for strategic success and how and where in the strategy each employee contributes. Executives and managers at multiple levels can use the Balanced Scorecard to monitor whether they are actually driving strategic success. If the results aren’t happening as planned, then the Strategy Map, Strategic Objectives, and Balanced Scorecard need to be revised until the organization has a valid model of what works.



## Building a Balanced Scorecard

The trip activities listed in the scenario in the previous section correspond to similar activities in building a Strategy Map and Balanced Scorecard, as shown in Table 1.2.

**Table 1.2:** Building a Balanced Scorecard is a journey.

TRAVEL	BALANCED SCORECARD	INTENT
Select a destination	Destination Statement	State in one page what your organization wants to be at the end of your strategic horizon.
Agree on the type of trip	Strategic Themes	Your trip's journey might have a theme of speed or low cost. Your Balanced Scorecard might have Strategic Themes such as customer intimacy or operational excellence. How you execute your Strategic Themes differentiates you from your competitors.
Agree on the route	Executive and Division Alignment	Leaders, managers, and employees must all be going in the same direction.
Map the route	Strategy Map	Identify the route and objectives that will get you to your destination.
Plan time and resources	Tactical Action Plan and Implementation Plan	Identify the measures, metrics, and initiatives, and who is accountable.
Travel	Prioritize, budget, and act	Execute the strategy.
Stay on track	Balanced Scorecard	Monitor your Balanced Scorecard to make sure your organization is on track.

## Does the Balanced Scorecard Guarantee Business Success?

There is no killer methodology that guarantees success in business. The Strategy Map and Balanced Scorecard do not guarantee success. Organizations can still fail by having the wrong strategy, by having a poorly built Strategy Map and Balanced Scorecard, by failing to use the Balanced Scorecard once it is implemented, or by failing to modify the Balanced Scorecard if their hypothesis of what works is wrong.

I occasionally meet consultants and executives who proclaim, “We tried a Balanced Scorecard and it didn’t work.” Their perception may be true — some research shows that approximately 30 percent of Balanced Scorecard attempts fail.

There are many reasons for failure, and the Balanced Scorecard fails in companies for a variety of reasons. Some of the most common are:

- **Lack of senior executive commitment.** An executive at the highest level in the strategic business unit must sponsor the Balanced Scorecard. Without the commitment of the senior executive, managers and employees feel that the Balanced Scorecard is just another “management fad of the month.” The senior executive must make a case for change in the organization that will light a fire under everyone.
- **Lack of a case for change.** Organizations are difficult to change. The Balanced Scorecard is used to create a culture of high performance, translating strategy into action. Without a driving need for change, and an organization-wide awareness of the need, the Balanced Scorecard will become just another performance management system that will fade.
- **Lack of an experienced consultant or facilitator.** Developing and implementing a Balanced Scorecard is difficult. It is critical to use an experienced facilitator or consultant to guide initial development and to train internal facilitators and managers who can carry on the work. You are betting the strategic success of your organization on this effort. You don’t want to use a general business consultant who has read a book or *Harvard Business Review* article on Balanced Scorecards. There are many bear traps to avoid, and you want someone who knows how to avoid them.
- **Too many metrics.** Too many metrics can create a confusing model of what drives strategic success. The Balanced Scorecard becomes an Operational Dashboard.
- **Wrong metrics.** Using the wrong metrics drives performance in the wrong direction.
- **Too long to develop.** Taking too long drains motivation and loses key resources.
- **Cultural mismatch.** Organizations with a cultural norm of low performance or organizations with dictatorial executives require a major cultural change before implementing a Balanced Scorecard.

Some executives and consultants have asked me if the Balanced Scorecard replaces Six Sigma, if it’s more productive than LEAN, or if it coordinates projects better than a Project Management Office. A Balanced Scorecard does not

replace any of these. It works as a strategic management system that acts as an envelope to keep Six Sigma and LEAN projects aligned with strategy. It works with accounting, budgeting, and the Project Management Office to optimize them for the organization, rather than just for individual silos.

Some organizational cultures just don't work well with a Balanced Scorecard. For example, some nonprofits, such as hospitals, work well with Balanced Scorecards and can use them to significantly increase their efficiency and performance. Other nonprofits, such as social service organizations, seem to have a great deal of difficulty working with measures and metrics. Some for-profit high-tech companies, especially startups, feel that their business changes too rapidly for a well-thought-out strategy. As mentioned, their strategy is "Go after any opportunity." Other for-profit high-tech companies, such as medical device manufacturers, have a focus that benefits greatly from a Balanced Scorecard.

I've seen organizations that have a cultural mismatch with a Balanced Scorecard and have no desire to change. Some of these organizations seem to have a culture of self-inflicted low performance. In particular, one director of an umbrella social services organization comes to mind. As part of a group of pro bono senior consultants, I volunteered to help the organization increase productivity and manage staffing problems. When our pro bono group presented our findings, along with numerous no-cost and low-cost solutions, the director scolded us with: "We are here to help people. We are not your Silicon Valley corporation concerned with measuring, planning, and performance." Those of us on the consulting team who gathered later for an After-Action Review felt a lot of sadness for the organization's clients. The director had the attitude that her organization couldn't increase performance and care for people at the same time. By enabling low performance under her management she was abandoning many children that might have had a head start on education. Low performance with no desire to change meant that many low-income families weren't being served by the health clinic under her control.

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## Does the Balanced Scorecard Really Work?

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The now famous quote, "What gets measured gets done," is most often attributed to the management guru Peter Drucker. Although it seems to be an obvious truth, a more direct proof of the value of Balanced Scorecards is its acceptance and use among corporations worldwide. Bain & Company, an international consulting firm, does an annual survey on management tools among its 6,200-plus large corporate clients. The results of Bain's 2006 survey show that Balanced Scorecards are used by 70 percent of their clients with a 3.5/5.0 satisfaction level. This makes the Balanced Scorecard one of the most widely used strategic tools and places it within the cluster of tools that garner high levels of satisfaction.

Although the Bain & Company survey shows the pervasive use of the Balanced Scorecard, many organizations don't talk much about their success to the press. But successes that have been published cover a wide range of industries.

- Duke Children's Hospital reduced costs by \$30 million and increased net margin by \$50 million in two to three years while increasing patient and staff satisfaction.<sup>6</sup>
- Delta Dental of Kansas, the largest dental benefits provider in Kansas, is a 90-employee company that saw its revenues jump from \$63 million in 2001 to \$172 million in 2006 (a 173 percent increase) while increasing employees' satisfaction and understanding of their job.<sup>7</sup>
- Crown Castle International, the world's largest owner of telecom infrastructure, needed a strategic shift from its acquisition strategy in 2001 to a strategy of operational excellence in 2003. Even as its competitors faced meltdown, it saw cash flow rise from negative \$300 million to positive \$100 million and its stock price beat market indices by more than 300 percent.<sup>8</sup>
- Keycorp, one of the nation's largest bank financial services organizations, has cascaded its four strategic themes through all 19,000 employees.<sup>9</sup> The Key Corporate and Investment Banking Group (KCIB) improved its ROE by 28.8 percent from 2002 to 2005, and its vendor satisfaction ratings also improved. In three years, its ratings went from 45–74 percent to 86–93 percent.<sup>10</sup>

## **Do Small and Medium-Sized Businesses Benefit from the Balanced Scorecard?**

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Executives of small and medium-sized businesses (SMBs) may have the impression that the Strategy Map and Balanced Scorecard are just for large corporations. Actually, small and medium-sized businesses may find that Balanced Scorecards are easier for them to implement, and that the payoff comes quicker. Of the Balanced Scorecard Hall of Fame winners, 20 percent are small and medium-sized businesses.

SMBs may have even more to gain from Strategy Maps and Balanced Scorecards than large organizations, because of the limited resources that SMBs have. SMBs in particular have to make sure that they focus their efforts, provide better services, and drop projects that aren't aligned with strategy. The Balanced Scorecard is designed to align an organization around a focus and to make it easier to identify projects that aren't within that focus.

Communication and decision-making within SMBs can improve as well. Strategy Maps, freed by fewer layers of management and fewer employees, make communication easier and faster. Strategic issues can come to light faster when the Balanced Scorecard is incorporated into normal executive team meetings.

Many SMBs are opportunity-driven. SMBs providing high value in growing niches will see opportunity everywhere. Maintaining a focused strategic direction can be just as difficult as walking a kid in a straight line through a toy store. This is where a Balanced Scorecard can help. In the article “Why the BSC Is Just as Effective for Small and Medium-Sized Firms,” Tom Lefebvre, director of Strategic Planning for the Alaska Native Tribal Health Consortium (ANTHC), says that the Balanced Scorecard “has provided a framework that has created absolute clarity of our strategy and ultimate vision.” Because of the Balanced Scorecard, ANTHC has increased its cash flow and has seen an 80 percent drop in nursing turnover.<sup>11</sup>

Strategic plans in all organizations usually become far too complex to implement. This is where the Balanced Scorecard can help. By working through the Balanced Scorecard process, from Strategy Map to Balanced Scorecard to Tactical Action Plan to Implementation Plan, it becomes obvious which initiatives and projects contribute to strategy and how they must be scheduled and budgeted over time.

The work of developing a Balanced Scorecard is intense in an SMB in which everyone wears multiple hats. This is where an experienced consultant can help facilitators and managers get up to speed quickly and reduce the burden. Writeups from the Balanced Scorecard Hall of Fame winners show that the first year of development is hard work, that the second year gets easier, and that the third year is even easier — with benefits coming in.

## Is the Balanced Scorecard Worth Developing?

Is the Balanced Scorecard worth developing in your organization? It takes dedication and work, but ask yourself these questions:

- Would we be more successful if the executive team focused more on strategic leadership and less on operational problems?
- Would we be more successful if our executives and managers used Strategy Maps as a forum to constructively breach the walls between silos?
- Would our managers be more knowledgeable about what drives their business if they had to define the “critical few” metrics that drive and measure success?
- Would our employees be more proactive and satisfied if they understood how they affect strategic success?

If your answers to these questions are yes — if changes such as these would increase the success of your organization and its people — then you should find out how you can implement your Balanced Scorecard.

## Summary

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The rate of change in the world of business is accelerating. The only way for organizations to succeed is to execute their strategy. If your organization wants to succeed, you have to translate your strategy into action, aligning your organization with strategic objectives and making sure that every employee knows how he or she contributes to strategic success. The most powerful tools you can find for building a culture of high performance are the Strategy Map and Balanced Scorecard. Creating them and building a high-performance culture isn't easy, but it is a journey that can lead to organizational success.

## Notes

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