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# The Balanced Scorecard

## Concepts and Cases

a Latin-American approach  
by

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activus  
Business Engineering

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## 1. Abstract

The planning process does not end when the company decides what strategy or strategies to follow. One must transform the strategy into action. This translation is much simpler if managers and employees understand the business, feel part of the company, and through the involvement in the formulation of it, helps the company to be successful.

Deployments affect the organization from the top to the bottom, and impact on all areas, functional and divisional. The implementation phase is the key. However, it's easier "to say" than "to do".

Implement the strategy is the act of turn words in action. It is the ability to manage people and resources to achieve the objectives outlined above. This step is so important that, even though, an excellent strategy had been made, poor implementation could put you in risk. The techniques and control systems are essentially the same, either to control production processes, administrative procedures, quality of a product or other. The faster deviations are detected, more easily and cheaply corrective actions could be taken. That is why the importance of measuring, from the beginning, any type of process.

Planning and control are increasingly treated as an interrelated system. Performance is, theoretically, a multidimensional variable that expresses the degree of success or failure of an entity in relation to another or, itself at an earlier time.

The wider and more comprehensive set of performance indicators the better the process of monitoring and control the business, and consequently, better capacity to respond to the challenges of a competitive environment. The BSC is the answer to it.

## 2. BSC as a Management and Control tool

## 2.1. Concepts

The traditional financial reporting systems were developed by companies from the industrial era, and are based on past events.

This type of system does not reflect the factors that determine the future performance, which is essential for modern businesses.

The ability of a company to create value in the future depends on four perspectives:

1. - Financial Perspective: for a company to achieve financial success, how it should look to shareholders?
2. - Customer Perspective: for a company to achieve its vision, how has it to present themselves to their customers?
3. - Internal business processes perspective: to provide services that meet the expectations of customers and stakeholders, which business processes must excel?
4. - Learning and growth Perspective: for the company to achieve its vision, how to sustain their ability to change and improve?

These four Perspectives are represented in the Balanced Scorecard (BSC). Once the company has developed its own BSC, it can be used as a management system for managing long-term strategies. This involves also four steps:

1. - Senior management translates Business Unit Strategies into specific strategic objectives:
  - Financial goals
  - Customer goals
  - Internal business processes goals.

- Growth and learning goals.
2. - The objectives and specific strategic systems which are measured are communicated throughout the business unit, so everyone is aligned with them.
  3. - Managers identify which are the changes required to meet the objectives. They develop plans to implement the changes, including the budget and the mechanisms required.
  4. - Management receives information on how they are progressing achievement of objectives. This feedback can force realigning the objectives in intermediate stages.

## 2.2. How to Build a successful BSC?

### 2.2.1. Financial Perspective

The long-term financial objectives of any company is to provide superior returns on invested capital. For most organizations, financial goals are clearly defined, and include:

- Increase returns.
- Improve productivity
- Reduce costs.
  - Improve asset utilization.
  - Reduce risks.

In any business, financial strategy (and hence, the factor to be measured by the BSC), depends on the phase where the company is located and the strategic topic:

	Strategic Issue		
	Return increase and Marketing Mix	Costs Reduction and Productivity	Assets Utilization Strategy
Growth	Growth	Revenues per employee	Investment
	Segmentation		
	New Products Revenues		
Sustainability	Revenue - Market Share	Indirect Costs	ROA
	New Apps Profitability	Cost Reduction Rate	ROE
Harvest	Profitability	Cost per Unit	
	Customer Percentage of no profitable ones	Cost per Trasaction	Production Process

Illustration 1 – Finance Strategy

### 2.2.2. Customer Perspective

At the end of the planning according to this view, managers should be familiar with the market segment and profile customers pursuing. In turn, should have a clear idea of how it will be structured the value proposition that the company offers.

Here are some measures that can be used:

- Market Share
- Level of customer retention
- Number of new customers acquired
- Attainment of customer satisfaction.

- Customer profitability.

Companies should establish specific objectives in each of these areas, and develop marketing goals, operations, logistics, products and services, which in turn will offer support and improve these objectives.

It's not enough to focus on past performance, managers should focus on the value proposition that the company will offer its customers. This should include:

1. - Product and service attributes: regarding the functionality of the product or service, price and quality.
2. - Customer Relationship: regarding the delivery of the product or service, response time and customer sentiment on interaction with the company.
3. - Image and reputation: refers to the intangible factors that attract the customer to do business with the company.

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### **2.2.3. Internal Business Process Perspective**

Every company has a chain of value by which it is created and delivered to the customer. The BSC approach requires aligning the different steps in the chain through specific strategies to meet the expectations of shareholders and customers.

Internal processes that create value chain are:

1. - Innovation processes critical to the future success of the company. Focus on customer benefits that can be valued in the future, and how to offer a unique way.

2. - Operational delivery related to an efficient, consistent and timely products and services.
3. - After sales service: include processes payments and guarantees, activities to ensure customer satisfaction, etc..

During the BSC approach, the performance requirements of internal processes should be derived from the expectations of the external entities. It should establish and monitor specific parameters along the chain.

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#### **2.2.4. Learning and Growth Perspective**

The primary objective in this perspective lies in the infrastructure. It should be developed so as to achieve excellent results in the above three perspectives.

The possibility for an organization to achieve its objectives will be directly proportional to the ability to learn new skills and grow in the business.

In order to achieve excellence in this perspective, are of great importance:

1. - Employees: Employee skills are very important, especially when a lot of work has been automated.

The skills of the employees must be aligned with organizational objectives. In general, the measures for employees are: satisfaction, retention and employee productivity.

2. - Systems: information systems that provide rapid, timely and accurate information, which can be used to interact with customers, is a primary requirement for organizations that aspire to grow.



3. - Organizational Alignment: highly competitive employees using information systems will not be productive unless they have the freedom to make decisions and execute. The system needs to allow employees to take the initiative to create satisfied customers.

The prospect of growing and learning requires investment in human resources, systems and processes that enhance organizational capabilities.

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#### **2.2.5. Key Issues for sucesess**

A good BSC is more than a compendium of financial and nonfinancial measures. The BSC should include the history of the business strategy, in a unique blend of:

1. - Outcomes: are indicators that reflect the result of management decisions made in the past. Although financial measures are not the best, are of great importance.

2. - Motivators of performance measures: reflect the originality of the organization and its business strategy. When combined with the outcome measures, highlight if a trading strategy is being implemented successfully to build better relationships with customers.

3. - Cause and effect relationships: there must always be a direct connection between a breeding program and financial performance. For the BSC to be successful from the corporate point of view, in the end, the improvement should be reflected in the numbers.

A strategy can be described as a theory of cause and effect. The cause-effect relationships can be described in phrases such as "If ... then ..." if a condition occurs, then they will turn out.

### 2.3. Cause-Effect Relationship

One of the key for a good construction of a BSC, is to analyze the cause-effect relationships/relation, starting with the ultimate goal to be reached.

If you want, for example, to improve the Return on Investment (ROI) it can be done improving profits by adding value. Then, customers notice that value and pay more for it. In order to do that, in example, we must improve customer loyalty.

One way to do that would be improving delivery times of the products and/or services. In turn, to improve delivery times, it should be improved the quality and timeliness of the process. To achieve that, the staff should be train so as to improve their skills.

Through this diagram, we are covering the four different perspectives of a BSC.

All this is seen in the following illustration:

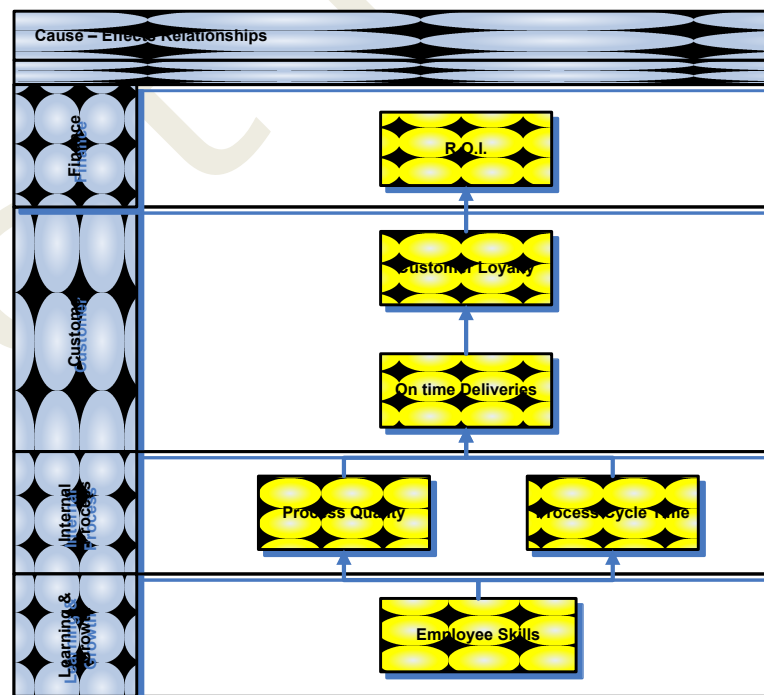


Illustration 2 - Cause - Effect Relationships

## **Customizing a BSC**

For a BSC was useful must reflect the structure of the organization in which it is applied. Not only should apply to a business unit, should also apply to:

Corporations with multiple units: almost always the best approach is to develop a corporate level of BSC to establish the issues, objectives and financial measures; it is expected that each business unit adheres to it.

Once the issues are resolved at the corporate level, each business unit can develop its own version.

Alliances and mergers: in many of them, it is difficult to define the goals that both sides have. Therefore, it is useful to develop a BSC that is used to define an agenda and measures under which the merger or alliance will operate.

The BSC of a merger can facilitate the creation of unique and sustainable value added as a result of teamwork. The link between an outcome and performance engines must have value for both parties.

Support departments in corporations: a corporate group BSC (maintenance, purchasing, human resources, information technology, etc..) can be very useful because it allows the corporation to identify where they are offering low-cost services or differentiated, and what services can be outsourced without much impact on competitiveness.

A BSC makes groups develop and communicate a strategy based on the value proposition that they will provide to the other business units. The BSC provides a mechanism by which internal business processes can be aligned to a large number of groups.

- Nonprofit companies and government: developing a BSC can also facilitate better focus, greater motivation and greater accountability in government and in nonprofit organizations. Can be used to give a logical explanation for the existence of these organizations, it is also useful for these groups to communicate with external entities, about their results and performance.

#### 2.4. The BSC as a Strategic Management tool

There are four main barriers to implementing the BSC:

1. - Visions and strategies that are not actionable: if an organization can not translate their vision and mission to accompany your terms that everyone can understand and act, the programs are inefficient.

The process of developing a BSC can develop consensus among management about the direction the organization should take, should translate that vision into strategic issues that can be communicated throughout the organization.

2. - Strategies unrelated to the team and individual goals: the concept of BSC will add value to the organization only if:

- Communicates effectively with all employees
- The strategy is translated into goals for the business units.
- There is alignment between compensation and goal achievement.

The BSC provides an ideal opportunity for organizations to strength the link between the objectives of the Scorecard and compensation programs. Such links can be

explicit (using a predetermined formula) or intentionally applied by management. To strength that bond gives advantage to employees and management.

Similarly, the development of a BSC encourages companies to educate and involve staff who will be responsible for executing strategy.

3. - Strategies that are not tied to the location of resources: when the budget process is separate from the BSC, problems arise. The operating budget must be aligned with strategic planning for success.

To achieve this integration, you must:

- Setting targets: the BSC will identify cause and effect relationships that can be exploited to achieve total increases in performance.
- Identify and justify strategic initiatives: when there is a gap between current performance and the strategic objective, managers can set priorities for capital investments and action to close these gaps. Resources can also remove programs that do not have significant impact on the achievement of the strategic objectives specified.
- Identify important initiatives between units: in large organizations, the BSC budget can provide managers to identify and encourage the initiatives that provide tangible benefits to the achievement of strategic objectives and other business units within the organization. Typically, these programs are difficult to describe and measure.
- Manage the link between the placement of resources and budgets: the BSC approach can link the strategic plan with the application of discretionary funds. You can specify milestones for future budget

periods. The progress of the organization towards its strategic objectives can be recorded using the landmarks as midpoints.

These four processes have the effect of increasing management commitment to achieve the vision of the organization. They also provide a practical framework by which progress can be measured.

4. - Tactical feedback rather than strategic: feedback on how the strategy is being implemented is very valuable, but rarely used.

The BSC approach provides an excellent framework around which can be developed significant revisions of strategic performance.

Feedback is vital if an organization wants to test and refine its strategy, this can be achieved with a strategic learning process consisting on three steps:

1. - The development of a common strategic framework.
2. - A feedback process that collects performance data.
3. - A team based on problem solving processes.

### 3. Case Study: The BSC as a Management tool in an Argentine IT Service Company

#### 3.1. The Company: "NV"

"We've have got professional experience of 20 years allows us to contribute to the effective management of information technology. NV's mission is to minimize IT risks to which they are exposed organizations we work for and avoid, thus, the loss of critical data. Our goal is to make technology and information security in a business opportunity for our clients. We

specialize in the diagnosis of computer processes, technological and legal needs of organizations to meet them through the integration of technology solutions and professional services”.

### 3.2. Needs

That company was facing strong growth, and its staff was concerned about the lack of indicators, mainly the non-financial ones, run into the need for a management tool, simple but effective, to evaluate the company performance, not only present but future.

Evaluating different systems learnt that the BSC is a simple and effective way for achieving that goal.

One of its biggest concerns was the lack of enough information beyond basic sales indicators, and fear of the difficulty of obtaining other measurements, while still being useful not complicate or make management their processes somewhat slower.

So, come to the decision to implement a BSC according to their needs, and based on its core business of equipment supplies and services in IT Security.

### 3.3. Result: New management Tool

If you don't measure it, you can't improve it

*W. Edwards Deming*

After sustainable growth through the years, the company realized that the management methods of evaluating and monitoring their performance were no longer sufficient.

It was when senior management decided to implement a BSC, which would allow them to do with a long-term perspective of where the company was heading. Similarly, they looked for detecting early enough those deviations which may be connected on the road producing path to achieving its objectives.

It was there that they decided to formulate goals and indicators from the four BSC perspectives suggests.

So far, they were based on the measurement and monitoring of traditional indicators, primarily financial perspective "according to the definition of a BSC."

The same can be seen below:

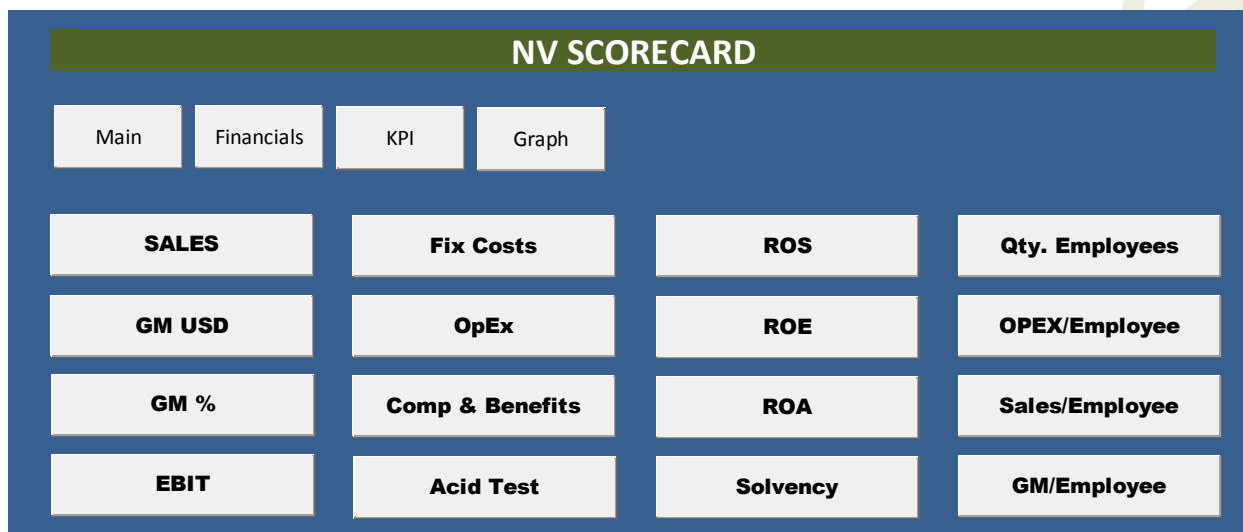


Illustration 3 – Traditional Scorecard

It took time to formulate new metrics contemplating these four perspectives.

Using a spreadsheet, they got putting together a basic outline of the new management system.

There are detailed goals, Lag indicators, Lead indicators, and columns for actions and reports.

It shows the same in the following illustration:



F C I H		ISO 9000		
Balanced Scorecard				
Mision: To be a leader in the "Information Technology Security" market by virtue of a superior technical specialization and the permanent preeminence in the incorporation of added value to the solutions for our customers.				
GOALS	LAG INDUCATORS	LEAD INDICATORS	ACTIONS TO BE TAKEN	REPORTS
<b>F</b>	<b>Financial:</b>			
F1:	Aggressive Growth	Net Sales Direct and Services	Offers, New Pojects, Orders.	
F2:	Increase Margins	Service GP, Direct GP, GPs/GPL	Service Offers / Total Offers. Billed Service Hs/Total Service Hs.	
F3:	Improve Operating Profit	OP x BUS, Expenses x BUs.		
F4:	Profitable Company	ROE, NIAT, Acid Test.		
F5:	Positive Cash Flow.	Cash, cash-cash cycle.		
<b>C</b>	<b>Customer:</b>	<b>LAG INDUCATORS</b>	<b>LEAD INDICATORS</b>	
C1:	Excellence in Service	Repurchasing, account profitability, account share.	Ctm. Satisfaction index	
C2:	Complete Security Solutions	Mix of sales.	Time devoted to Services/ Total T.	
C3:	To be Technologically Superior		Tech. Satisfaction index	
C4:	Added Value	Service/Product ratio	#Post-Sales/#employees	
C5:	Image and Reputation building	Marketshare on target segments	Mindshare in total potencial market. New Accounts opened. A&P/revenues	
<b>I</b>	<b>Internal Process:</b>	<b>LAGS INDUCATORS</b>	<b>LEADS INDICATORS</b>	
I1:	Customer driven			
I2:	Innovative Security Solutions	Cty. New Services and solutions per year.		
I3:	Productivity	Cty employee claims (No conformidades internas - ISO 9001)	process cycle time.	
I4:	Total Quality	Cty ctm. claims (No conformidades clientes - ISO 9001)		
I5:	Knowledge data base	Volume of key data		
<b>H</b>	<b>Human Resources:</b>	<b>LAGS INDUCATORS</b>	<b>LEADS INDICATORS</b>	
H1:	Effectiveness	Salesmen Close Rate.	Employee performance in accordance to Finction Profile.	
H2:	Develop Strategic Skills	Employee profile/Evaluation rate		
H3:	Align Personal Goals	Cty. Certif.Eng.		
H4:	Key employees retention	Key employee turnover	Employee Satisfaction	
H5:	Use of Strategic Information			

Illustration 4 - BSC in spread sheets

In turn, for each indicator, each of said detailed metric, for example, for the first financial target, referred to herein as F1, detail various leads and lags indicators having tracked both weekly and monthly.

Back to BSC      Back to Admin

F1 Aggresive Growth

METRICS

F11 Lag Indicators		Jan	Feb	Mar
F111	Gross Sales Total	436343	459396	544710
F112	Gross Sales Services	103753	152983	122628
F113	Gross Sales Direct	332590	306413	422082

F11 Lead Indicators		WEEK		
		1	2	3
F121	New Projects			
F122	Offers	184000	234000	278000
F123	Orders	1000	95000	43000

GOALS

F11 Lag Indicators		Jau	Feb	Mar
F111	Target Total	500000	555000	610000
F112	Target Services	100000	105000	110000
F113	Target Direct	400000	450000	500000

F11 Lead Indicators		WEEK		
		1	2	3
F121	New Projects			
F122	Offers	570000	570000	570000
F123	Orders	190000	190000	190000

Illustration 5 - Detailed Finance Indicators

Thus it was working with each of the metrics in each of the perspectives.

The problem was that it had been done in traditional spreadsheets, and while it could make use of the graphs and macros tools, the presentation was not enough professional when submitting reports.

Remarkably, a good graphical interface helps dramatically in rapid interpretation and diagnosis. It is for the latter suggested the use of tools to facilitate management reporting presentations making them much more professional.



Illustration 6 - The four perspectives

As seen in Figure 6, a graphical representation of the four perspectives with corresponding metrics is much clearer than just a list of statements.

Radar charts or bar type, are also much more practical to detect deviations or outliers.

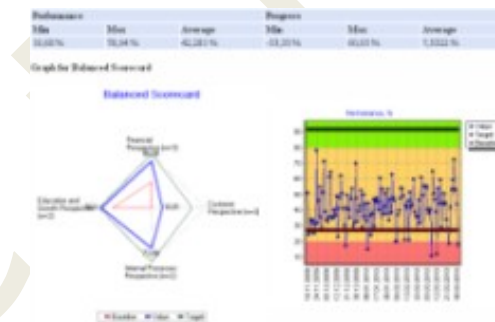


Illustration 7 – Graphs

#### 4. Conclusions

Management needs measurements. In order to measure, it must be quantified, and hence, the importance of the Scorecards.

It's much better to evaluate the organization's performance from other perspectives beyond the financial ones. It gives its benefits.

Those perspectives should be balanced. Balanced between financial and non-financial indicators, between the short and long term.

The "Balanced Scorecard" offers all those benefits, and a suitable software tool that facilitates the construction of reports and professional presentations turns management into a practice of excellence.

Sergio Salimbeni