The Balanced Scorecard

A Literature Review on
the Balanced Scorecard’s impact on performance

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Executive Summary
Since Kaplan and Norton introduced the Balanced Scorecard (BSC) in the early 1990s, it has become widely adopted by companies and divisions within companies. The BSC was conceived as way to operationalize a company’s vision and strategy. In this regard, it is a management system, or as the originators note, a tool for change within the firm or unit. Not surprisingly, the swift adoption and creation of BSCs has led to a number of different applications and variations of the tool. When implemented well, it appears that BSC is consistent with the principles of good management in that it promotes strategic planning, better definition of accountabilities, and more effective feedback.

Background
When Kaplan and Norton introduced the Balanced Scorecard in 1992, companies were already searching for new measurement systems to replace the age-old accounting measurements used for budgetary control. The BSC is an apparent antidote to the limitations of using lag measurements that are historically based and cannot be used to help the manager moving forward (e.g., financial ratios). In addition, the BSC attempted to bring objective value to non-financial measures such as customer satisfaction and operational processes. The BSC is an integrated tool that is designed to link sets of activities and outcomes by individuals and groups to broader strategic goals of the firm. Done correctly, the BSC is believed to help the troops see how their work impacts the important company goals.

The BSC is more of a conceptual tool, where the company and each unit within the company must customize the scorecard to their particular goals and strategy. In fact, the literature is clear by those that extol the use of the scorecard: executives and managers must spend plenty of time determining what the strategic goals of the company (or unit) are before BSC can be designed and implemented. Kaplan and Norton (2001) insist that a BSC program should be a change project rather than a metric or measurement tool. That is, instituting a BSC requires the critical involvement of executives who must determine and lay out a clear strategic direction. Under the BSC framework, once this strategic direction is clear, it can then be operationalized down through the structure. In this way, the lower level employee will be able to see the link between what he or she does and its impact on the company’s bottom line goals (e.g., results benchmarks like profit). And the scorecard becomes a management tool where employees receive feedback that is timely enough to impact current or future performance.
Although companies or business units are encouraged to identify and customize their own areas of measurement, four broad perspectives are associated with BSC—customer perspective, internal processes perspective, innovation and learning perspective, and financial perspective. Specifically, the measures that are chosen by the unit tend to fall under one of these categories. For example, under the learning growth category, there may be a measure for number of training hours employees receive (see Albright, Davis, & Hibbets 2001). This outcome measure could then be linked to employee knowledge and skill in an area (e.g., sales) that then translates into successful referrals or cross-sells, leading to customer satisfaction-retention leading to some bottom line financial number. In this way, a training manager or specialist could see how her activity linked to the larger business goals. See Figure 1 for visual example.

Figure 1. Example of how BSC flows through non-financial perspectives

While it is difficult to determine the actual impact of the BSC, it is projected that over half of the large firms in the United States use some kind of scorecard. Of the scant empirical data on the BSC’s effectiveness, a researcher named Claude Lewy claims that over 70% of BSC programs fail. Still, it is apparent that the BSC has broad appeal. Furthermore, it is written about and applied in just about all functional areas (CIOs, marketers, HR people, accountants, etc.).

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1 This example comes from Albright, Davis, & Hibbets, 2001
Discussion

Although not conceived as metrics system by the originators, BSC has become closely aligned with performance measurement and compensation systems. As an example, a CEO for a credit union who implemented a BSC for his firm is quoted as saying, “All the bonuses, from mine on down to the most entry-level employee’s, are tied to the scorecard” (Hanson and Towle, 2000). In fact, McKenzie and Shilling (1998) talk about balanced scorecards in terms of performance measurement systems that are tied to incentive or compensation plans—and all the problems this can create. Employees as well often think of the Scorecard in terms of performance evaluation or meeting the prescribed numbers (Albright, Davis, & Hibbets, 2001).

Similar to other feedback tools like 360 degree, the literature is replete with articles on the caveats for designing and implementing a successful BSC program. Among these caveats are having too many measurements, using the system as a top down control (i.e., coercive), over focus on the measurements rather than the performance, and lack of follow through with the results. Another danger cited was that the program can become an end in itself because of the significant time and expense required to implement it. In fact, the heavy front-end cost includes 1) designing the scorecard, which usually requires a pilot and 2) extensive training and communication of the program to employees and managers. After implementation, McCunn (1998) makes it a commandment that the implementing firms not underestimate the significant administrative cost in time and money for gathering information from the scorecard.

Ho and McKay (2002) compare two companies—one that abandoned its use of BSC and one that is succeeding. Among the critical differences cited was that the failed example emphasized individual performance measures. In fact, the use of the scorecard as an evaluation tool may compromise one of the supposed benefits of the program—focus on long-term instead of short-term results. In the firm where BSC was abandoned, the management system focused more on individual performance and tied compensation directly to the scorecard measures.
Discussion (Cont.)

Perhaps the most important feature of a successful BSC program is the use of timely feedback. In Ho and McKay’s (2002) comparison, the firm successful with the BSC was able to tie the measures to pertinent feedback structures. Furthermore, it was focused to teams rather than individuals. The literature in general extols the ability of BSC to provide lead indicators as a way to assist managers. For example, McCunn (1998) cites a plastics manufacturer that identified one of its scorecard measures as machine availability. Simply measuring this as a percentage and reporting it to the 15 business units (placed in a context so they were not competing against each other), allowed the units to move from 90% availability to over 98%. Although McCunn credited the scorecard with this boost—“without the scorecard, machine availability would not have been given such high priority . . .”—the effective use of feedback (and tactical controls) was the critical factor.

The BSC framework is consistent with good management. First, it is conceived as a tool for managers, not simply Human Resources. That is, managers must be involved in designing and implementing it because it must specifically relate to strategic goals of the firm or unit. In conjunction with this, the tool seems to promote a clearer connection between accountabilities and strategy. Specifically, the scorecard can help managers define the work more clearly for employees. For example, “I [an employee] know exactly what the corporation expects of me . . . There is no ambiguity in what I do” was one reaction to the scorecard (Ho and McKay, 2002). Secondly, its focus on lead measures allows and encourages more useful feedback related to the work. Furthermore, it does not necessarily call for measurement as a coercive tool.

Because it is a customizable framework rather than a technique, BSC can be implemented in a number of ways. The upside of this customizability is that it forces the company or unit to engage in some form of strategic planning. The down-side is that the BSC can be implemented as a measurement technique, without changing underlying management practices. If managers under a BSC system use it simply as a tool for measuring individual performance, it will be less effective—read McCunn’s commandment to not “use the scorecard to obtain extra top-down control.” Thus, the success of a Balanced Scorecard Program depends on effective management practice and clear strategic goals—the BSC cannot replace these. In fact, the BSC should serve as a framework for augmenting effective management, such as, clearly defining accountabilities down the structure, linking these accountabilities to desired strategic goals (or consequences) of the firm or unit, and providing feedback on pertinent job performance activities.
References


