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THE BALANCED SCORECARD
is it up to par?

Robert Kaplan and David Norton intended their 'balanced scorecard' to link company strategy and front-line performance, chiefly by increasing the range of what managers could measure1. No one can argue that managers now understand their businesses better. But do they make better decisions too? Not, it turns out, if they use the scorecard to set numerical performance targets and demand immediate returns. Unfortunately the temptation to do just this is enormous.

The move from a capital-intensive economy to a knowledge economy in the 1970's made life instantly difficult for traditional business managers, who were used to evaluating firms' performance and overall worth in strictly financial terms. A firm's value was no longer a matter of buildings and machinery; now it had to do with customer transactions, the quality of the goods it sold, and the abundance and calibre of its employees' ideas2. By 1990, the Nolan Norton Institute, part of the accountancy giant KPMG, thought they had just the assessment and tracking system to match the new style of business concern in their 'balanced scorecard'. Support for this scorecard was widespread, and it included influential entities like the Harvard Business Review. Developers refined the model enthusiastically. By 2002, more than half of the world's leading companies were using it 2 for strategic management.

Were they wise to do this? Research suggests so. Kaplan and Norton, famously, call the card a translation device, that makes clear to every last employee exactly how best to behave in the interest of his company1. The scorecard does this by keeping track of four things: the usual financial features of the firm, customer acquisition and retention, internal processes that deliver value, and what the scorecard's creators call 'learning and growth', or adaptability to economic changes. Judicious use of these four kinds of information ought to improve company strategy, communication, and performance. It should also help address the cause of performance problems. Talented managers can learn by double-loop when they spot variances from targets—i.e. they can question their most fundamental assumptions about what must have gone wrong 3. And this learning need not be limited to the management community: Niven imagines a company, 'sharing scorecard results throughout the organisation, providing managers and employees the opportunity to discuss the assumptions underlying the strategy, [to] learn from any unexpected results and make changes as necessary 2, thus making the scorecard of use not just in strategy formulation but also deployment.

The scorecard's biggest promise, built into the name, is to bring balance to organisational strategy. Rather then being stuck with uni-dimensional financial indicators the scorecard links leading and lagging measures1. Leading measures are those that are really connected to customers, such as how satisfied they are, and lagging measures are actual outcomes of the organisation's performance.

The scorecard is easy to use wrong. Many businesses, particularly in the West, are inappropriately preoccupied with short-term earnings, for example. Some managers demand results that do not give the scorecard a chance to work. Other managers simply make starting assumptions about business that are false, and incompatible with the way the scorecard works. One of these is that numerical targets motivate people. A second is that achieving targets is always within the capability of the individual. A third is that managers can always understand the true causes of organisational failure. And ironically there are those who claim the scorecard is not really balanced at all: one critic says this is because the device ignores stakeholders, regulators and environmental factors4.

Some research backs this up. Often employees do not trust the scorecard to work, or to be connected at all to company strategy, or to be anything but a tool to control them5. This may be justified in many cases, where managers do not really understand department workings or deep business logic6. It is quite common for senior managers to say they still prefer to rely on traditional financial measurements5.

Is it really untrue that people need the motivation of targets 2? Sceptics say so for three reasons. Frederick Hertzberg declares flatly that target-setting does not change the conditions for motivation at all7. Alfie Kohn, critic of all targets, incentives and competitions, adds that targets actually de-motivate employees, especially when they are linked to incentives, because employees tend to find this manipulative8. And John Seddon says, finally, that targets even encourage some people to cheat, usually by falsifying their apparent work results6.

These objections do seem well founded in practical work life, where sometimes the problem is in deployment, not the scorecard itself. Senior managers in a large pension management division in London tried recently to move their organisation into profit. Their strategy was to improve customer service, which would optimise existing customer relationships and generate new ones. They developed their strategy, and set two-year targets. The plan, being a textbook example of scorecard strategy, linked staff performance to organisational goals. There was a critical flaw, however. Results should have provided a simple opportunity for long-term learning. Instead, partly because of leaked information about the company's share price, short-term performance targets suddenly seemed critically important. This was disastrous. Managers, forced to hit targets that sustained particular share prices, and working largely ignorant of the subtleties of their own divisions, operated without regard to real demand and real capability.

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A worker remembers.

'In the morning a manager handed me my quota for the day. The only way I could get through my work was to do all the easy stuff; the other work got left, and some people even hid theirs in the filing cabinet. That way we met our targets and didn't get into trouble. Managers in this place were not interested in why we didn't get through our work–only who should be blamed when something didn't get done. We used to care about helping customers. Not any more. Now we just wanted to hit the target and keep the managers off our backs.'

Kohn and Seddon predicted this. Staff were no longer focussed on doing the right thing for customers. They were interested only in hitting their targets, by whatever means possible. Investigation within this particular company turned up some 4,000 pieces of work actually hidden from managers. Some employees had even learnt how to hack into their managers' computer work logs and change what was there. Customers, of course, were outraged. Pension scheme managers began to move their schemes to other administrators.

Perversely, after two years all the leading targets were being hit. The internal efficiency quadrant looked good, and volume measures appeared satisfactory, but this was because it was the easy work that was being done. In the customer satisfaction quadrant response time looked fast, though this was because staff were careful to count only the time they actually worked on particular cases. And in the staff satisfaction quadrant, 'staff motivation' appeared healthy, but only was because one manager turned out to have been employed to stuff ideas into the company suggestion box—and then report how many had been stuffed in. And though training sessions seemed well attended, 'attendance' was really only a seat-count. The financial measures were accurate, too, though dismal. Unfortunately, the cause-and-effect logic promised by the scorecard provided no insight. The company began to fail, and senior managers were as mystified as they were alarmed.

It was all a matter of outdated assumptions. Managers were sure, for example, that staff necessarily had control over their output. Not so, observed no less an authority than W. Edwards Deming, the architect of Japan's economic revival. Deming showed many years ago that organisation design, not the willingness of an individual, determines output. Managers in our study organisation spent nearly all their time trying to cajole workers to try harder, when they should have been optimising the system 9. Next, strategy. Any fan of the scorecard system should concede that strategists must acknowledge market needs and organisational capability10;11. Their targets should contain no numbers, furthermore. And their measures should reflect output capability and the exact mechanism currently at work12. Managers as well need to be closer to the work than scorecard advocates usually recommend, and at the same time they need to have the courage to think long-term.

Results like this may have hurt the scorecard's popularity. Olve reports that today only 36% of the world's top organisations use it, and these use it more for measurement and feedback than for its original strategic function5. Managers may no longer trust the tool. Or they may only trust it in more experienced hands than theirs.

Conclusion

Kaplan and Norton intended that their scorecard would broaden what managers knew of their companies beyond financial measures, and bridge the gap between strategy and front-line performance. It certainly did these things. But the scorecard is easy to misuse. Managers must not use it to set arbitrary targets or incentives and should give the tool a chance to work, mistakes that so nearly cost one big London concern its life.

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