THE BALANCED SCORECARD APPROACH TO EFFECTIVENESS

Business organizations have typically focused on financial measures such as profit and return on investment to assess performance. Nonprofit organizations also have to assess budgets, spending, and fund-raising income, and each of these measures is concerned with finances. Traditional approaches based on goal, resource-based, or internal process indicators all have something to offer, but each one, just like sole reliance on financial numbers, tells only part of the story. In recent years, a new approach that balances a concern for various parts of the organization rather than focusing on one aspect has become popular. The balanced scorecard combines several indicators of effectiveness into a single framework, balancing traditional financial measures with operational measures relating to a company's critical success factors.

Exhibit 2.8 illustrates the four effectiveness categories considered by the balanced scorecard. Within each area of effectiveness—financial performance, customer service, internal business processes, and the organization's capacity for learning and growth—managers identify key performance indicators the organization will track. The financial perspective reflects a concern that the organization's activities contribute to improving short- and long-term financial performance. It includes traditional measures such as net income and return on investment. Customer service indicators measure such things as how customers view the organization, as well as customer retention and satisfaction. Business process indicators focus on production and operating statistics, such as speed of order fulfillment and cost per order. The final component looks at the organization's potential for learning and growth, focusing on how well resources and human capital are being managed for the company's future. Measurements include such things as employee satisfaction and retention, amount of training people receive, business process improvements, and the introduction of new products. The components of the scorecard are designed in an integrative manner so that they reinforce one another and link short-term actions with long-term strategic goals, as illustrated in Exhibit 2.8.

The balanced scorecard helps managers assess the organization from many perspectives so they have a better understanding of total effectiveness. Successful managers keep the organization focused on data in all four components rather than relying on just one, such as finances, which tells only part of the story. Companies such as Best Buy, Wells Fargo, and Hilton Corporation, for instance, are striving to understand how they perform on all four components of effectiveness and looking at the relationships among the components. For example, how does internal efficiency relate to customer satisfaction or financial outcomes? How do measures of employee engagement, customer satisfaction, sales performance, and profitability interconnect and contribute to overall effectiveness? Hilton found that a boost in customer retention rates led to an increase in revenues. Best Buy has connected employee engagement to better store performance.

Thus, the balanced scorecard has evolved into a system that helps managers see how organizational effectiveness results from accomplishing outcomes in four consistent and mutually supportive areas. Overall effectiveness is a result of how well these interdependent elements are aligned, so that individuals, teams, departments, and so forth are working in concert to attain specific goals that ultimately help the organization achieve high performance and fulfill its mission.