ASSESSING ORGANIZATIONAL EFFECTIVENESS

Understanding organizational goals and strategies, as well as the concept of fitting design to various contingencies, is a first step toward understanding organizational effectiveness. Organizational goals represent the reason for an organization's existence and the outcomes it seeks to achieve. The next few sections of the chapter explore the topic of effectiveness and how effectiveness is measured in organizations.

Recall from Chapter 1 that organizational effectiveness is the degree to which an organization realizes its goals. Effectiveness is a broad concept. It implicitly takes into consideration a range of variables at both the organizational and departmental levels. Effectiveness evaluates the extent to which multiple goals—whether official or operative—are attained.

Efficiency is a more limited concept that pertains to the internal workings of the organization. Organizational efficiency is the amount of resources used to produce a unit of output. It can be measured as the ratio of inputs to outputs. If one organization can achieve a given production level with fewer resources than another organization, it would be described as more efficient.

Sometimes efficiency leads to effectiveness, but in other organizations, efficiency and effectiveness are not related. An organization may be highly efficient but fail to achieve its goals because it makes a product for which there is no demand. Likewise, an organization may achieve its profit goals but be inefficient. Efforts to increase efficiency, particularly through severe cost cutting, can also sometimes make the organization less effective. One regional fast food chain wanting to cut costs decided to reduce food waste by not cooking any food until it was ordered. The move reduced the chain's costs, but it also led to delayed service, irritated customers, and lower sales.

Overall effectiveness is difficult to measure in organizations. Organizations are large, diverse, and fragmented. They perform many activities simultaneously, pursue multiple goals, and generate many outcomes, some intended and some unintended. Managers determine what indicators to measure in order to gauge the effectiveness of their organizations. Studies and surveys have found that many managers have a difficult time with the concept of evaluating effectiveness based on characteristics that are not subject to hard, quantitative measurement. However, top executives at some of today's leading companies are finding new ways to measure effectiveness, including the use of such "soft" indications as customer loyalty and employee engagement.

First, we will discuss several traditional approaches to measuring effectiveness that focus on which indicators managers consider most important to track. Later, we will examine an approach that integrates concern for various parts of the organization.

TRADITIONAL EFFECTIVENESS APPROACHES

Organizations bring resources in from the environment, and those resources are transformed into outputs delivered back into the environment, as shown in Exhibit 2.7 Traditional approaches to measuring effectiveness look at different parts of the organization and measure indicators connected with outputs, inputs, or internal activities.

Goal Indicator

The goal approach to effectiveness consists of identifying an organization's output goals and assessing how well the organization has attained those goals. This is a logical approach because organizations do try to attain certain levels of output, profit, or client satisfaction. The goal approach measures progress toward attainment of those goals. For example, an important measure for the Women's National Basketball Association is number of tickets sold per game. During the league's first season, President Val Ackerman set a goal of 4,000 to 5,000 tickets per game. The organization actually averaged nearly 9,700 tickets per game, indicating that the WNBA was highly effective in meeting its goal for attendance.

The important goals to consider are operative goals, because official goals (mission) tend to be abstract and difficult to measure. Indicators tracked with the goal approach include:

- Profitability—the positive gain from business operations or investments after expenses are subtracted
- Market share—the proportion of the market the firm is able to capture relative to competitors
- Growth—the ability of the organization to increase its sales, profits, or client base over time
- Social responsibility—how well the organization serves the interests of society as well as itself
- Product quality—the ability of the organization to achieve high quality in its products or services

Resource-based Indicators

The resource-based approach looks at the input side of the transformation process shown in Exhibit 2.7. It assumes organizations must be successful in obtaining and managing valued resources in order to be effective. From a resource-based perspective, organizational effectiveness is defined as the ability of the organization, in either absolute or relative terms, to obtain scarce and valued resources and successfully integrate and manage them. The resource-based approach is valuable when other indicators of performance are difficult to obtain. In many nonprofit and social welfare organizations, for example, it is hard to measure output goals or internal efficiency.

In a broad sense, resource indicators of effectiveness encompass the following dimensions:

- Bargaining position—the ability of the organization to obtain from its environment scarce and valued resources, including financial resources, raw materials, human resources, knowledge, and technology
- The abilities of the organization's decision makers to perceive and correctly interpret the real properties of the external environment

- The abilities of managers to use tangible (e.g., supplies, people) and intangible (e.g., knowledge, corporate culture) resources in day-to-day organizational activities to achieve superior performance
- The ability of the organization to respond to changes in the environment

Internal Process Indicators

In the internal process approach, effectiveness is measured as internal organizational health and efficiency. An effective organization has a smooth, well-oiled internal process. Employees are happy and satisfied. Department activities mesh with one another to ensure high productivity. This approach does not consider the external environment. The important element in effectiveness is what the organization does with the resources it has, as reflected in internal health and efficiency. The best-known proponents of an internal process model are from the human relations approach to organizations. Such writers as Chris Argyris, Warren G. Bennis, Rensis Likert, and Richard Beckhard have all worked extensively with human resources in organizations and emphasize the connection between human resources and effectiveness. Results from a study of nearly 200 secondary schools showed that both human resources and employee-oriented processes were important in explaining and promoting effectiveness in those organizations.

Internal process indicators include:

- A strong, adaptive corporate culture and positive work climate
- Operational efficiency, such as using minimal resources to achieve outcomes
- Undistorted horizontal and vertical communication
- Growth and development of employees

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.

DESIGN ESSENTIALS

- Organizations exist for a purpose. Top managers decide the organization's strategic intent, including a specific mission to be accomplished. The mission statement, or official goals, makes explicit the purpose and direction of an organization. Operative goals designate specific ends sought through actual operating procedures. Official and operative goals are a key element in organizations because they meet these needs—establishing legitimacy with external groups, providing employees with a sense of direction and motivation, and setting standards of performance.
- Two other aspects related to strategic intent are competitive advantage and core competence. Competitive advantage refers to what sets the organization apart from others and provides it

with a distinctive edge. A core competence is something the organization does extremely well compared to competitors. Managers look for competitive openings and develop strategies based on their core competencies.

- Strategies may include any number of techniques to achieve the stated goals. Two models for formulating strategies are Porter’s competitive forces and strategies and the Miles and Snow strategy typology. Organization design needs to fit the firm’s competitive approach to contribute to organizational effectiveness.
- Assessing organizational effectiveness reflects the complexity of organizations as a topic of study. No easy, simple, guaranteed measure will provide an unequivocal assessment of performance. Organizations must perform diverse activities well—from obtaining resource inputs to delivering outputs—to be successful. Traditional approaches use output goals, resource acquisition, or internal health and efficiency as the indicators of effectiveness.
- No approach is suitable for every organization, but each offers some advantages that the others may lack. In addition, a more recent approach to measuring effectiveness is the balanced scorecard approach, which takes into consideration financial performance, customer service, internal business processes, and the organization’s capacity for learning and growth. Managers track and analyze key metrics in these four areas to see how they are interconnected and contribute to overall effectiveness.