Bhimani et al
Chapter 22 – SMA and emerging issues

Solutions to some of the end of chapter questions

22.1 Strategy describes how an organisation matches its own capabilities with the opportunities in the marketplace in order to accomplish its overall objectives.

22.2 Two generic strategies are (1) product differentiation, an organisation's ability to offer products or services that are perceived by its customers to be superior and unique relative to those of its competitors and (2) cost leadership, an organisation's ability to achieve lower costs relative to competitors through productivity and efficiency improvements, elimination of waste and tight cost control.

22.3 The four key perspectives in the balanced scorecard are: (1) financial perspective – this perspective evaluates the profitability of the strategy, (2) customer perspective – this perspective identifies the targeted market segments and measures the organisation's success in these segments, (3) internal business process perspective – this perspective focuses on internal operations that further both the customer perspective by creating value for customers and the financial perspective by increasing shareholder wealth, and (4) learning and growth perspective – this perspective identifies the capabilities in which the organisation must excel in order to achieve superior internal processes that create value for customers and shareholders.

22.4 Reengineering is the fundamental rethinking and redesign of business processes to achieve improvements in critical measures of performance such as cost, quality, service, speed and customer satisfaction.

22.5 A good balanced scorecard design has several features:
1 It tells the story of a company's strategy by articulating a sequence of cause-and effect relationships.
2 It helps to communicate the strategy to all members of the organisation by translating the strategy into a coherent and linked set of understandable and measurable operational targets.
3 It places strong emphasis on financial objectives and measures in for-profit companies. Non-financial measures are regarded as part of a programme to achieve future financial performance.
4 It limits the number of measures to only those that are critical to the implementation of the strategy.
5 It highlights suboptimal trade-offs that managers may make when they fail to consider operational and financial measures together.

22.6 Pitfalls to avoid when implementing a balanced scorecard are:
1 Do not assume the cause-and-effect linkages to be precise; they are merely hypotheses. An organisation must gather evidence of these linkages over time.
2 Do not seek improvements across all of the measures all of the time.

3 Do not use only objective measures in the scorecard.
4 Do not fail to consider both costs and benefits of different initiatives before including these initiatives in the scorecard.
5 Do not ignore non-financial measures when evaluating managers and employees.

22.7 Engineered costs result from a cause-and-effect relationship between the cost driver, output and the (direct or indirect) resources used to produce that output. Discretionary costs arise from periodic (usually) annual decisions regarding the maximum amount to be incurred. There is no measurable cause-and-effect relationship between output and resources used.

22.8 SMA is a form of management accounting in which the emphasis is placed on information that relates to factors external to the firm, as well as non-financial information and internally generated information.

22.9 SMA practice is organisation-specific because all the factors that are generated in the analysis are very specific to the company and it is only by being specific to the company that the true strategic objectives and actions can be prescribed.

22.10 SMA's potential is affected by strategic product costing and performance measurement, the firm's product markets and competitive market forces, and the assessment of organisational strengths over a certain length of time.

22.12 Strategy, balanced scorecard.
1 Meredith Ltd follows a product differentiation strategy in 2008. Meredith's D4H machine is distinct from its competitors and generally regarded as superior to competitors' products. To succeed, Meredith must continue to differentiate its product and charge a premium price.
2 Balanced Scorecard measures for 2008 follow:

Financial perspective

(1) Increase in operating income from charging higher margins, (2) price premium earned on products.
These measures indicate whether Meredith has been able to charge premium prices and achieve operating income increases through product differentiation.

Customer perspective

(1) Market share in high-end special-purpose textile machines, (2) customer satisfaction, (3) new customers.
Improvements in these customer measures are leading indicators of superior financial performance.

Internal business process perspective

(1) Manufacturing quality, (2) new product features added, (3) order delivery time.
Improvements in these measures are expected to result in more satisfied customers and, in turn, superior financial performance.

Learning and growth perspective

(1) Development time for designing new machines, (2) improvements in manufacturing processes, (3) employee education and skill levels, (4) employee satisfaction.

Improvements in these measures have a cause-and-effect relationship with improvements in internal business processes, which in turn lead to customer satisfaction and financial performance.

22.15 Balanced scorecard.

1 The market for colour laser printers is competitive. Lee's strategy is to produce and sell high quality laser printers at a low cost. The key to achieving higher quality is reducing defects in its manufacturing operations. The key to managing costs is dealing with the high fixed costs of Lee's automated manufacturing facility. To reduce costs per unit, Lee would have to either produce more units or eliminate excess capacity.

The scorecard correctly measures and evaluates Lee's broad strategy of growth through productivity gains and cost leadership. There are some deficiencies, of course, that subsequent assignment questions will consider.

It appears from the scorecard that Lee was not successful in implementing its strategy in 2008. Although it achieved targeted performance in the learning and growth and internal business process perspectives, it significantly missed its targets in the customer and financial perspectives. Lee has not had the success it targeted in the market and has not been able to reduce fixed costs.

2 Lee's scorecard does not provide any explanation of why the target market share was not met in 2008. Was it due to poor quality? Higher prices? Poor post-sales service? Inadequate supply of products? Poor distribution? Aggressive competitors?

The scorecard is not helpful for understanding the reasons underlying the poor market share.

Lee may want to include some measures that get at these issues. These measures would then serve as leading indicators (based on cause-and-effect relationships) for lower market share. For example, Lee should measure customer satisfaction with its printers on various dimensions of product features, quality, price, service and availability. It should measure how well its printers match up against other colour laser printers on the market. This is critical information for Lee to successfully implement its strategy.

3 Lee should include a measure of employee satisfaction in the learning and growth perspective and new product development in the internal business process perspective. The focus of its current scorecard measures is on processes and not on people and innovation.

Lee considers training and empowering workers as important for implementing its high-quality, low-cost strategy. Therefore, employee training and employee satisfaction should appear in the learning and growth perspective of the scorecard.

Lee can then evaluate if improving employee-related measures results in improved internal business process measures, market share and financial performance.

Adding new product development measures to internal business processes is also important. As Lee reduces defects, Lee's costs will not automatically decrease because many of Lee's costs are fixed. Instead, Lee will have more capacity available to it. The key question is how Lee will obtain value from this capacity.

One important way is to use the capacity to produce and sell new models of its products. Of course, if this strategy is to work, Lee must develop new products at the same time when it is improving quality. Hence, the scorecard should contain some measure to monitor progress in new product development. Improving quality without developing and selling new products (or downsizing) will result in weak financial performance.

4 Improving quality and significantly downsizing to eliminate unused capacity is difficult. Recall that the key to improving quality at Lee SA is training and empowering workers. As quality improvements occur, capacity will be freed up, but because costs are fixed, quality improvements will not automatically lead to lower costs. To reduce costs, Lee's management must take actions such as selling equipment and dismissing employees. But how can management dismiss the very employees whose hard work and skills led to improved quality? If it did dismiss employees now, will the remaining employees ever work hard to improve quality in the future? For these reasons, Lee's management should first focus on using the newly available capacity to sell more products. If it cannot do so and must downsize, management should try to downsize in a way that would not hurt employee morale, such as through retirements and voluntary redundancies.