

The Balanced IT Scorecard

Quality of Strategy Vs. Strategy Execution

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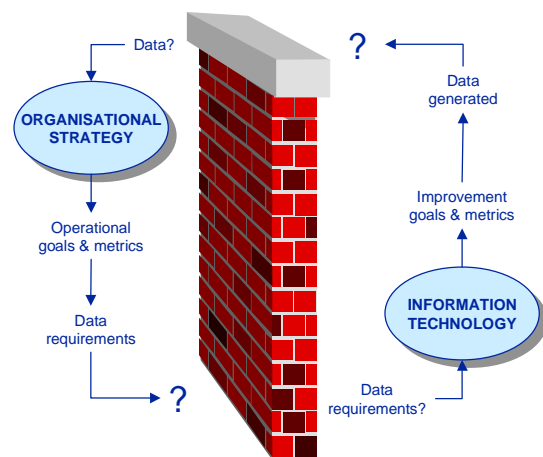
Introduction

It's no secret that to be competitive and to succeed, organisations must understand how their own perceptions of what constitutes quality in their products and services, in other words – their value discipline, meets the customer's expectations for quality products and services – the customer's value proposition – and then develop a good strategy that appropriately realigns all aspects of the organisational system and operations to effectively execute the strategy. However, somewhere in between the ideal of strategic alignment and the reality of strategy execution, many organisations get lost, or at a minimum sidetracked, and fail to achieve their vision.

For one thing, many senior managers get lulled into believing that defining a good quality strategy is synonymous with an effective implementation of the strategy, and that without a high-quality strategy the organisation is doomed to fail. However, according to a 1998 Fortune Magazine article¹ an estimated 70% of senior executive failures are not caused by a poor strategy, but rather by poor execution of the strategy – not getting things done, being indecisive, not delivering on commitments.

This problem is further exasperated in IT organisations where traditional communications barriers caused by the use of very distinct operational languages and idioms often prevents IT from achieving its full potential to add value to the

organisation and identify new business opportunities in order to effectively support the organisation's strategy. Senior executives have traditionally used financial indicators to drive the decision making process yet IT departments tend to focus on more technically oriented metrics. Just put a Chief Financial Officer and an IT Director into the same room and the ensuing conversation will, at best, be humorous. It will more likely be extremely frustrating as the CFO speaks in terms of Cash Flow and Return On Capital Employed while the IT Director is trying to justify a budget increase by emphasising the need to improve System Availability and Defect Removal Effectiveness for new applications development.



What is needed is a business-oriented process to that drives goal-oriented investments in IT and hence creates a common language in the company and provides a framework for consistent evaluation using the same business criteria across the whole organisation.

A Balancing Act

Given that the primary objective of most organisations is to generate positive financial results, most top-level business objectives are easily broken down into target financial results for reaching these goals. Based on these target financial results, organisations set customer related goals for the levels of customer acquisition, retention, satisfaction and loyalty necessary to meet the financial goals. Typically, organisations do not find it difficult to establish this relationship between customer and financial results. However, establishing the links between the people, processes, technology and organisational culture that will enable these results is not a task that has been mastered by many.

The Balanced Scorecard approach developed by Kaplan and Norton² provides a strategic framework for identifying and linking these enablers with their desired results by defining the relationships between performance levels in four distinct perspectives.



Kaplan and Norton describe the Balanced Scorecard as a framework for translating a vision into a strategy by focusing on shareholder, customer, internal and learning requirements which collectively describe the strategy of an organisation and how that strategy can be achieved.

The Balanced Scorecard is based on the premise that organisations can no longer rely on summary financial indicators which provide a “delayed snapshot” of business performance thus making it too late to avoid a problem once detected. This is increasingly true in today’s competitive marketplace where the accelerating rate of change requires increased organisational agility to take decisions and react to the change. Therefore, the “lagging indicators” need to be balanced with other measures that are capable of forecasting economic results through early warnings. These “leading indicators” provide an early manifestation of whether an organisation will achieve its business goals and be able to sustain these achievements in the future.

Likewise, the criteria for evaluating an IT organisation’s performance are changing. The CIO’s value contribution equation has shifted from a nearly exclusive emphasis on efficiency and cost cutting to new criteria such as strategic capabilities and rapid service response to market events and rapidly evolving technologies. The IT investment and management decision-making process is accordingly no longer only about lowering IT unit costs but also about expanding IT service delivery capabilities to satisfy future business needs as well as today’s requirements. For many CIOs, their major challenge is determining how to balance the need to manage and maintain a critical IT legacy against the equally critical need to be an innovative and forward-looking partner with the business.

Consequently, IT managers are seeking new performance management systems that include the measurements to support their need to record/report and a framework that supports their need to direct/transform. IT managers are seeking measurement systems that can be used to demonstrate and communicate the ability of IT to deliver value by linking IT performance drivers to business

performance drivers and metrics. One of the most significant drivers of strategic change in the world is technological innovation. In particular, the application of innovative IT is radically altering the basis of business competition. Today, the benefit of exploiting IT not only relates to making business processes and tasks more efficient. Instead, IT also enables the creation of IT-enabled products, services, distribution channels and IT-enabled links with customers, suppliers and other stakeholders. IT is virtually interwoven with almost every aspect of modern organisations, their business network and their environment as a whole.

Over the last couple of years we have been applying the principles of the original Balanced Scorecard framework to IT organisations in an attempt to address many of the issues described on the previous page. One of the most notable deviations in our adaptation of this framework has been the addition of a fifth perspective, the People Perspective, to address the special requirements of IT and software development³.



Balanced IT Scorecard Framework

In a world where nothing is built to last – where today’s innovative product will be replaced with tomorrow’s newer and better version – the variable that remains most constant is the organisation’s people. Paying close attention to increasing both the satisfaction and competence of an

organisation’s employees can reap extraordinary dividends in the long-term through increased commitment and productivity.

For many years the manufacturing industry has placed a high level of emphasis on supply chain management as a key driver for increasing profits. While there are many variables that must be considered as a part of effective supply chain management, undoubtedly managing the quality of the raw material provided by one’s suppliers and the quality of the internal processes that will convert the raw material into products are key to creating and sustaining a profitable enterprise. Part of this practice should be transferred to the software industry and integrated into the practices of Software Process Improvement (SPI). We strive to continuously improve our software development and management processes, yet we often forget about the importance of the raw material that these processes must convert to produce better, faster and cheaper software.

Software development is probably one of the most knowledge intensive industries, so how does a software development organisation manage the quality of its raw material when the raw material itself is embedded in the knowledge of its staff? Research, experience and even common sense all tell us that there is a direct relationship between the quality of our products, the processes that produce them and the people that perform those processes. In spite of this, why is common sense so uncommon when managing people during the course of a SPI programme (or any improvement initiative for that matter)?

In their book “*Peopeware*”⁴, software industry gurus Tom DeMarco and Tim Lister comment “*The final outcome of any effort is more a function of who does the work than of how the work is done*”. Any nontrivial process performed without skill

and motivation may very well have the opposite effect of what it was designed to do – increase organisational performance. By taking care of the personal and professional needs of your employees, the source of the precious raw material that will develop your products and services, you will be provided with readily available opportunities to avoid organisational entropy and boost your organisation's financial performance.

While we find the Balanced IT Scorecard (BITS) to be a useful framework for identifying how the organisation must perform and improve in order to enhance the chances of long-term profitability, it is the actual process of defining and implementing the BITS that addresses some of the real challenges facing IT organisations, or any knowledge intensive company for that matter.

There's more value than what is on the books.

According to an Ernst & Young LLP report⁵, when analysing the value of an organisation, 35% of the valuation decision is based on non-financial data. The report goes on to identify the non-financial factors that most highly influence shareholder valuation:

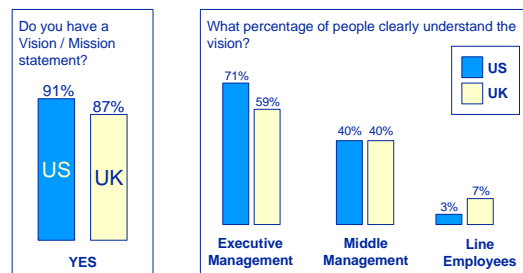
1. Strategy Execution
2. Management Credibility
3. Quality of Strategy
4. Innovation
5. Attract & Keep Talented People
6. Market Share

In an age where shareholder valuations far exceed the capital holdings of a company, the ability of an organisation to execute its strategy is becoming increasingly crucial.

Strategies, in and of themselves, are nothing more than a series of hypothesis that imply a certain cause-and-effect

relationship between the actions that we take and the results (hopefully the desired results) that will occur from those actions. Understanding the cause-and-effect relationships between the five perspectives of the Balanced IT Scorecard thus becomes an essential factor in refining not only the quality of the strategy, but also the ability to communicate and execute it and come closer to reaching the organisation's vision.

Defining the link to the vision is a crucial point that many organisations overlook or bypass when defining their strategy. This is not surprising since so many visions are so poorly or vaguely stated that people in the organisation find it difficult, if not impossible to understand and relate to. A Renaissance/CFO Magazine survey highlights the failure of many organisations to effectively communicate their vision in an understandable manner.



Source: Renaissance / CFO Magazine Survey

As we can see in the chart above, while a relatively high number of the survey participants in the United States and the United Kingdom recognise that their organisation has a vision statement, as you move down in the organisational ranks, the number of people who actually understand the vision falls below 10% in both cases. This is not very encouraging when you consider that executing strategy is the job of everybody in the organisation – and how can you execute a strategy when it's linked to something you can't understand?

Kotter suggests that an effective vision has six essential characteristics⁶. A vision must be:

Imaginable – it conveys a picture of what the future will look like.

Desirable – it appeals to the long-term interests of ALL stakeholders.

Feasible – it sets ambitious yet realistic and attainable goals.

Focused – it is clear enough to provide guidance in decision making.

Flexible – It is general enough to allow individual initiative and alternative responses in light of changing conditions.

Communicable – it is easy to communicate and can be explained in five minutes.

Our experience shows that once the link between vision and strategic objectives is established, defining the strategy to achieve those objectives becomes a powerful and empowering process. To translate the vision into strategic intent, for each of the five perspectives of the Balanced IT Scorecard we ask the organisation to concisely complete the following sentences in a plain language format:

Success Means...
 ↳ We will measure success by...
 ↳ To achieve success, we must excel at...

An example for the Customer Perspective is:

Success means we will provide the best value in offerings matched to customers' needs in the markets that we choose to serve.
 ↳ We will measure success by determining our customers' assessment of the overall value of our products and services.
 ↳ To achieve success we must excel at improving the customers' perception of value so that the number of customers who do not rate us as "Very Good" will have declined by 40% in three years.

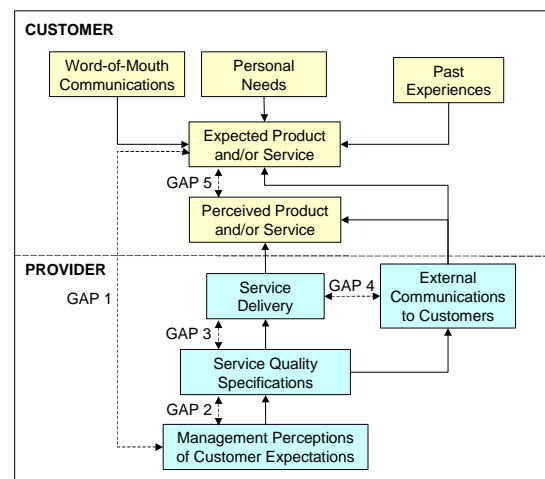
By doing this for each of the perspectives, all of an organisation's stakeholders are provided with a clear statement of what the future will look like, how it will be measured and what the long-term performance targets are.

A disciplined proposition

For the statement of strategic intent, I have purposely chosen to provide an example for the Customer Perspective. In a recent article by Kaplan and Norton⁷, they state that "...although a clear definition of the value proposition is the single most important step in developing a strategy, approximately three-quarters of executive teams do not have consensus about this basic information."

There is little doubt that how well an organisation performs with respect to meeting the customer's value proposition will have an impact on their ability to attain and maintain a profitable customer base. However, the definition of quality products and services from the point-of-view of a provider's senior leadership team – the organisation's value discipline – is not always aligned with the expectations for quality and value that a customer has for those same products and services.

There are different methods for detecting these gaps and one of the most widely used in the 90's was the SERVQUAL⁸ method.



The SERVQUAL model is illustrated above and highlights the product/service provider shortfalls (Gaps 1-4) that result in product/service quality discrepancies from the customers' viewpoint (Gap 5).

Gap 1 – Discrepancy between customers' expectations (the value proposition) and

managers' perceptions of those expectations.

Gap 2 – Discrepancy between managers' perceptions of customers' expectations and product/service quality specifications (the value discipline).

Gap 3 – Discrepancy between and product/service quality specifications and the product/service delivered.

Gap 4 – Discrepancy between the product/service delivered and product/service promised.

Gap 5 – Discrepancy between the customers' expectations and their perceptions of the product/service received.

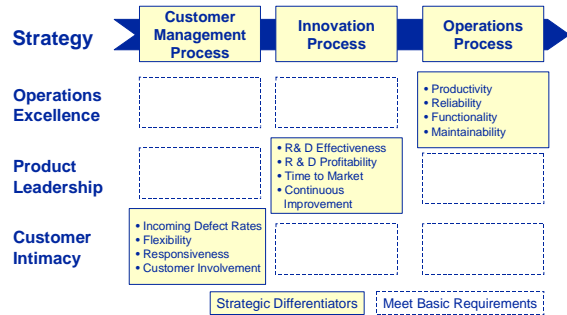
From the eyes of the customers', *Gap 5* is the one that matters and will influence the customers' decision to purchase new products and/or services from the provider in the future. Therefore, *Gap 1* must be bridged so that the organisation has a clear understanding of the customer's expectations and, as such, define the appropriate value discipline for meeting the customer value proposition.

Treacy and Wiersma describe three organisational value disciplines⁹ for choosing market segments and succeeding in meeting the value proposition(s) of the customers in those segments.

Operational Excellence - "Companies that deliver a combination of quality, price and ease of purchase that no one else can match them." Companies that successfully compete based on this discipline are recognised for providing the *Best Total Cost* to their customers.

Product Leadership - "Companies that push their products into the realm of the unknown, the untried, or the highly desirable." Companies that successfully compete based on this discipline are recognised for providing the *Best Product* to their customers.

Customer Intimacy - "Companies that build bonds with their customers; they know the people they sell to and the products and services they need." Companies that successfully compete based on this discipline are recognised for providing the *Best Total Solution* to their customers.



As highlighted in the figure above, for an IT organisation to compete based on *Product Leadership* its Customer Management and Operations processes must meet the minimum requirements that any organisation competing in its chosen segment(s) must meet. However, for it to succeed, the organisation must differentiate itself from current and potential competitors by excelling at the Innovation process. Such a situation may compel the organisation to track indicators related to Research & Development, new product cycle times and continuous process improvement.

By understanding and closing the gaps between the customers' value proposition and the organisation's value discipline, determining where to focus internal actions in the People, Process and Infrastructure & Innovation perspectives of the Balanced IT Scorecard and what to measure become clearer.

From strategy to action – say what we do and do what we say

Once a script is written, any good film director employs a set of tools and techniques that will guide them through the filming process in order to enhance the of producing a theatre blockbuster. In the

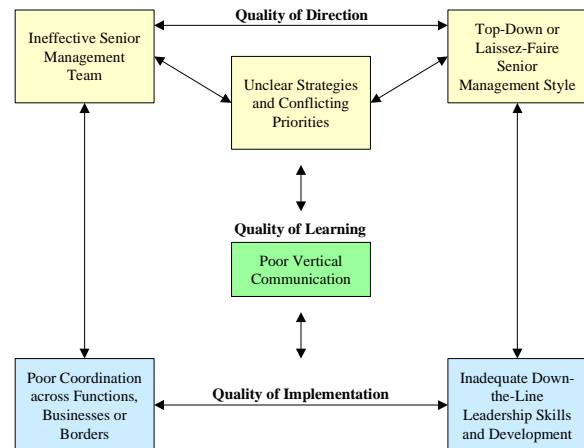
same manner, once a company has reached a consensus on a clearly mapped-out strategy and understands the cause-and-effect relationships between the organisation's drivers of success (the script), it's time to set the stage for strategic action. By defining and balancing the leading and lagging indicators across the five perspectives of the Balanced IT Scorecard, and setting performance targets for each of the indicators, senior leadership sends a clear signal to the entire organisation that a disciplined approach will be taken to controlling organisational operations – strategy will not just be left up to chance.

Werewolves don't exist, and neither do silver-bullet solutions

Although many organisations are reporting a wide range of benefits that they attribute to the Balanced (IT) Scorecard, these benefits would not have been achieved if the organisation did not already have a strong leadership team that was dedicated to the process. The scorecard requires good leadership, it is not a substitute for good leadership and, as such, senior leadership should not be lulled into a false sense of security believing that the scorecard will solve all of the organisation's ills. Over the last decade Beer & Eisenstat have been using their Organisational Profiling Technique to understand the root causes of problems encountered when responding to shifts in competitive strategy. They suggest that in the majority of cases that they studied, six barriers that block strategy implementation are commonly found¹⁰.

As highlighted in the illustration on this page, Beer & Eisenstat's six "Silent Killers" are, when looked at on their own, worrisome. However, when looked at in the context of their interrelationships, we can see that escaping from this vicious circle is a monumental task.

While we suggest that a Balanced IT Scorecard approach to developing and



implementing strategy can effectively act as a bulldozer that breaks through these six barriers, without a good leadership team in the driver's seat, the bulldozer will more likely cause destructive harm instead of clearing the path for constructive good.

Conclusions

Although the development of a good quality strategy remains, to a certain degree, an art form, the description and communication of the strategy should not be left up to chance. Just as well, by taking a methodological approach to describing a strategy, an organisation is provided with a mechanism for better understanding and making explicit the cause-and-effect relationships between strategic actions and business outcomes. Few will disagree with the statement "The quickest way to fail is to consistently do the wrong things in an effective and efficient manner." The framework and process for developing a Balanced IT Scorecard is a powerful tool for expressing the organisation's vision and strategy in tangible terms, gather support for them at all levels of the company and, as such, increase the organisation's capability to execute a good quality strategy. The scorecard provides a clear map of where we are and where we want to go while at the same time highlighting the route that we choose to take and helps us to avoid what Paul Nitze described as "one of the most dangerous forms of human error – forgetting what one is trying to achieve".

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