Measuring Performance

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How is your business doing?

Measuring performance involves studying your business processes and outcomes to see if you are getting the results you intend to achieve. Even if you're making a profit, your business may have room to improve its efficiency. The best way to determine operational effectiveness is by measuring business performance.

There are many methods of measuring performance but the goal is the same — to find out what is working well and what needs to change. Performance measurement can keep you on track towards your vision and help your profits increase. It can also help you to identify undesirable trends, such as:

- Shrinking market share
- Decreasing gross profits
- Decreasing sales
- Increasing costs
- Deteriorating customer satisfaction, and
- Increased staff turnover

Identifying these trends early can help you mitigate them.

This guide identifies some strategies you can use to analyze data from your business to determine how you are performing. Choose the performance measurement method that fits your specific business needs.

1. Methods

The Balanced Scorecard[i]

The Balanced Scorecard is a strategic performance management framework that has been designed to help an organization monitor its performance and successfully implement its strategies. In its simplest form The Balanced Scorecard breaks performance monitoring into four interconnected perspectives:

- **Financial perspective:** How does the business look to owners/investors?
- **Customer perspective:** How do customers see the business?
- **Internal perspective:** How well does the business manage its operational processes?
- **Innovation and learning perspective:** Can the business continue to improve and create value? This perspective also examines how an organization learns and grows.

The Balanced Scorecard system identifies the objectives, measures, targets and initiatives in each of the four key perspectives. In this context the objective is your goal for each perspective. Your target is what you want to achieve in each perspective. Measures are the benchmarks used to evaluate your progress in each perspective and initiatives are the actions you will take.

The following is a brief overview of the four key areas of The Balanced Scorecard with brief examples of objectives, measures, targets and tactics.

- The **financial perspective** covers the financial objectives of an organization and tracks financial success. Earnings are a traditional measure of profitability.

Objective	improve earnings
Measure	percentage growth in earnings year-over-year
Target	achieve a 10% growth in earnings over two years
Tactic	improve manufacturing processes to decrease costs and improve margin

- The **customer perspective** reminds business owners that they need to step back and view their company from their customers' point of view. A company that has strong sales but low customer satisfaction is likely to see its performance decline as unhappy customers eventually find other suppliers. By regularly surveying customers, a business can identify problem areas and respond proactively.

Objective	increase customer satisfaction
Measure	repeat visits from customers
Target	sales per customer increase by 5%
Tactic	service and satisfaction training of sales staff

- The **internal business process perspective** covers internal operational processes and measures the efficiency of the company's operations in specific areas such as manufacturing processes.

Objective	improve manufacturing excellence
Measure	manufacturing cycle times and yields
Target	increase output by 10% in two years
Tactic	review engineering efficiency

- The **learning and growth perspective** covers the drivers of future success such as employee performance, corporate culture, internal communications, skills, training and leadership. Measurements would include reviewing illness and absences, employee turnover and internal promotion rates.

Objective	increase internal promotions
Measure	bigger % of in house promotions
Target	achieve a 10% growth in internal promotions in two years
Tactic	additional classes and training

Inputs-outputs-outcomes

Another way to analyze your business is to use a logic model that is divided into inputs, outputs and outcomes. Are your actual outcomes in line with your strategic goals?

Inputs are everything that goes into creating your product or service. Examples include:

- **Materials and inventory:** The physical supplies that go into producing your product or service, including raw materials for manufacturing a product and office supplies to operate your administration.
- **Labour:** All staffing, including contract employees.
- **Financing:** Capital investment and operating capital required to run your business.

Outputs are your products and services. Outputs also include everything else that your business produces, including waste or by-products that might erode value.

- **Products:** Items you are creating for sale, including both physical merchandise and intellectual products, such as software.
- **Services:** Include any service you sell, such as accounting or engineering, or a personal service like elder care.
- **Waste:** Anything you discard, such as scraps from manufacturing, shredded paper, or dirty water from a car wash.

Outcomes are the results of your business activities. Some of them are desired, such as making a profit. Some are side effects, such as creating employment. And still others might be undesired outcomes. You can measure them in the short, medium or long term.

When you have identified all of your outcomes, compare them to your objectives to see if your business is producing the results you want.

You can also use the information you gather here to address business process questions as: how will your business manage if any of your key inputs are disrupted?

2. Measures

Quantitative versus qualitative measures

Quantitative data is measurable and objective. Hard numbers like how many employees you have or your net profit last year are important but don't reveal everything about your business. Businesses also rely on less quantifiable factors such as company reputation or team morale.

For example:

Quantitative data can be measured.

A cup of coffee is served at 90 degrees C in a 250 mL cup for a retail price of $1.50.

Qualitative data involves judgment.

Coffee customers also care about the taste of the coffee, how politely it is served, and whether the cafe's location is convenient for them.

Quantitative measures

Most people think of quantitative measures when it comes to performance. Your best source is your financial records, including sales data, inventory and financial statements. Where possible, start with at least three to five years of data, so you can establish trends.

- **Business ratios.** Ratios are a way to evaluate the performance of your business and identify potential problems.
  - Debt to equity ratios indicates what proportion of equity and debt the company is using to finance its assets.
  - Cash and working capital ratios determine the capacity of the business to meet current obligations.
  - Profitability ratios measure a company's ability to generate earnings profits and cash flows relative to sales, assets and equity.
  - Debt service (DSCR) ratio is a measurement used to determine your ability to produce enough cash to cover your debts, including lease payments.
- **Inventory measurements** such as rate of sales, replacements and the number of days it takes to sell the inventory on hand may indicate efficiencies and or possible problems.
- **Asset and infrastructure** maintenance, repairs and replacements are a quantifiable cost and should be part of amortization and depreciation calculations.

You might want to review other business functions to determine how effectively you are managing operations. Some key areas to review include:

- Average age of receivables and payables and the amount of bad debts you are carrying
- Average size of sales to determine the viability of low sales/profit items
- Financing costs such as interest and carrying charges for loans and other credit
- Down time for fleet vehicles or equipment and the impact on productivity

Qualitative measures

Numbers can't tell you everything. Qualitative measures provide the rest of the picture. Some qualitative measurements are outlined below. These can be included in The Balanced Scorecard or inputs-outputs-outcomes methods.

Customers

Customer perspectives are an important measure of success. Referrals, repeat customers and customer comments provide insight into how well you are meeting expectations. Basically, you want to know if customers like your company, product or service. You want to know if your service is timely, friendly and responsive to customer needs and expectations. Social media plays a significant role in influencing customer perceptions. Monitoring your brand name or product appearance on the web can provide valuable information on what you are doing right and what needs improvement.

Your team

Look at the team that you have put together for your business. Consider your employee satisfaction ratings in terms of engagement, management performance, retention and recruitment. Employee surveys, as well as illness and absenteeism records can provide valuable insight into employee satisfaction.

When do you measure performance?

You need to decide how often you will look at your performance. Factors to consider include the nature of your business, the length of the sales cycle, the pressures of competition and the speed of change in your industry.

Companies selling high volumes of rapidly changing products via the internet may measure their performance daily or even hourly. You want to find an optimum balance of analysis and action.

Try making a list of which performance indicators you will measure and then assign a frequency to each. For example, you may want to look at your sales figures weekly and your gross profits monthly. You may decide to do an industry comparison on a quarterly or annual basis.

3. Now what?

Once you have determined what performance measures you will use, and the cycles of measurement, you need to develop an implementation plan. Improving performance means changing processes and procedures. Once you know how well you're doing you can develop a strategic growth plan, identify your goals and objectives and take action on making the changes needed to grow. Then you need to measure how well your growth strategies are working.

Bring your team together to determine the priority areas for change. Identify a champion for leading change in key areas and set a timeline for implementing the initiatives. Be sure you have the capital and commitment needed to implement the changes and the measurement processes.

Planning, measuring and making changes leads to more measuring, more planning and more changes. Business growth is a continual process that moves through cycles. When you set your strategic goals you will determine the length of time required for each phase of your business cycle. Your performance measures are your benchmark for success. They help you set goals and timelines to create future value.

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[i] Kaplan, R. S., & Norton, D. P. (1996). *The Balanced Scorecard: Translating Strategy into Action.* United States of America: Harvard Business Press.