

Performance measurement

4 aspects of performance measurement system:

- convey information
- They are formal
- Used by managers and can influence decision making
- Influence patterns in organizational activities.

Business strategy is different from business goals

Business strategy: how a company creates value for customers and differentiates itself from competitors in the marketplace.

Business goal = measurable aspirations that managers set for business.

There are many trade-offs

1. Balancing profit, growth and control

Managers of high-performance companies constantly seek profitable growth. To do so, they are continually innovating. Successful innovation finds its way into sustained profitability and growth. However, an excessive emphasis on profit and growth can lead to danger. A wise manager knows that control is the foundation of any healthy business. A profitable business that lacks adequate controls can quickly collapse. Control weakness allows error and risk. Attempting to grow a business that is not profitable can only be described as foolhardy.

2. Balancing short-term results against long-term capabilities and growth opportunities.

Businesses must deliver financial performance. However, producing earnings consistently is difficult. Managers must also manage for the long term. To make money in the future, sometimes it is necessary to reduce profitability in the short term. Performance measurement and control systems play a critical role in managing the tension between short-term profit demands and the necessity for long-term investment in capability and growth opportunities.

3. Balancing performance expectations of different constituencies

Managers strive to achieve a variety of goals. A business entity is comprised of many different constituencies. Different parties may have different stakes in the success of a business and desire different things from the people who manage it. Important stakeholders are:

- Owners and stockholders → dividend payment
- Managers and employees → promotion
- Customers → product quality, service and price
- Suppliers → payment processing
- Lenders such as banks → financial strength and liquidity
- Government agencies → compliance with law and regulation

Each of these constituencies may be interested in different aspects of performance.

Managers must strike a balance between these expectations because they will sometimes collide.

4. Balancing opportunities and attention

Another tension in organizations relates to having too much of one thing and too little of another. There are too many opportunities and too little attention and time. The most critical constraint is management attention. There are so many things to do, and so many issues to focus on, that managers must ration their time and attention wisely. Effective managers have learned how to leverage this scarcest of all resources. Focus on ROM (return on management) = amount of productive organizational energy released/amount of management time and attention invested.

5. Balancing the motives of human behavior

influence the behavior of subordinate managers and other employees of the business. Managers must have a clear sense of what motivates people to work effectively toward the goals of any business.

Employees and managers are viewed as rational, calculating, maximizing individuals who dislike work, attempt to do the minimum that is demanded of them, and can be expected to act in opportunistic ways to enhance their own well-being at the expense of the organization to which they belong.

People in organizations want to contribute to an organization of which they can be proud. People employed by business organizations know the difference between right and wrong and generally choose to do right. People strive to achieve. People like to innovate. People want to do competent work.

Corporate strategy defines the way that a firm attempts to maximize the value of the resources it controls.

Business strategy is concerned with how to compete in defined product market.

A mission, the broad purpose for which an organization exists, guides the formation of business strategy. Business strategy, in turn, determines performance goals and measures, and ultimately, patterns of action. Before they develop specific business strategy, managers must analyze and understand the competitive market dynamics in their industry and their own firm's resource and capabilities. So the first stage is using SWOT analysis to analyze internal strength and weakness of the firm to external opportunities and threats in the marketplace.

To create competitive advantage in specific markets we can use the "five forces" analysis. In any industry, these forces influence competitive dynamics and potentially create opportunities for or constraints to effective competition.

next stage of swot is to analyze the resource and capabilities of the firm to determine what a business does well and what it does not do well. We can look at firm's balance sheet to learn about the resources that are available for competition. In accounting, an asset is defined as a resource, owned or controlled by the entity, that will yield future economic benefits. a resource is more broadly defined as a strength of the business embodied in the tangible or intangible assets that are tied semipermanently to the firm.

For any asset to be recognized on the BS, an asset must have future value to the firm, value must be quantifiable with reasonable precision. Intangible assets are problematic for accounting purpose because their monetary value is difficult to measure so they more rarely appear on firm's balance sheet. (I.g. relationship)

4P of strategy

Now we need to analyze strategy from 4 different angles: strategy as perspective, strategy as position, strategy as plan, and strategy as patterns of action. These are the four Ps of strategy.

Mission/purpose (overall perspective): Mission refers to the broad purpose, or reason, that a business exists. Good missions supply both inspiration and a sense of direction for the future. Missions are often written down in formal documents known as mission statements that are circulated widely throughout a firm. A mission statement communicates the core values of the business.

Position: related to 2 questions: how do we create value for our customers? How do we differentiate our products and services from those of our competitors? Managers of competing firms might answer these questions in very different ways. Some firms may choose to create value by offering their goods and services at low cost, hoping to draw customers who are price sensitive; other firms may compete by differentiating their products and services in a way that adds unique benefits for customers, or by customizing product offerings to respond to the specialized needs of specific customer segments.

Plan: the preparation of plans and goals represents the formal means by which managers (a) communicate a business's strategy to the organization and (b) coordinate the internal resources to ensure that the strategy can be achieved. Goals are the ends or results that management desire to achieve in implementing the business strategy. However, goals become actionable only when time frames and quantitative indicators of success are added. Plans can be used to communicate strategy, set goals, and coordinate resources.

Pattern/action: action in order to achieve the goals. But Not all successful strategies are planned. Many arise spontaneously. Many successful strategies arise from local experimentation and replication. So sometimes we need a bottom-up strategy. Action → learning → strategy. Strategy can be planned but it can also emerge in unexpected and unanticipated ways.

Building a balanced scorecard

The balanced scorecard communicates the multiple, linked objectives that companies must achieve to compete based on their intangible capabilities and innovation. The scorecard translates mission and strategy into goals and measures; capture intangible dimensions of daily operations. It is organized into four different perspectives: financial, customer, internal business process, and learning and growth.

Financial= financial measures are essential in summarizing the economic consequences of strategy implementation. Financial performance measures indicate whether the implementation of plans and initiatives is contributing to profit improvement.

Customer= managers identify the customer and market segments in which the business desires to compete. managers develop measures to track the business unit's ability to create satisfied and loyal customers in these targeted segments. Studies have shown that businesses with satisfied, loyal customers become significantly more profitable over time. customer satisfaction, customer retention, customer loyalty, and market share should be measured only for those customer or market segments for which the organization desires to be a dominant provider of goods and/or services.

Internal process= managers identify the critical internal processes for which the organization must excel in implementing its strategy. The internal business processes dimension represents the critical processes that enable the business unit to deliver the value propositions that will attract and retain customers in targeted market segments, and satisfy shareholder expectations regarding financial returns. The generic value chain model encompasses three principal business processes: 1. Innovation process; 2. Operation process; 3. Post-sale service process.

Learning and growth= identifies the infrastructure that the organization must build to create long-term growth and improvement. Intense global competition requires companies to continually improve their capabilities for delivering value to customers and shareholders. Organizational learning and growth come from three principal sources: people, systems, and organizational procedures.

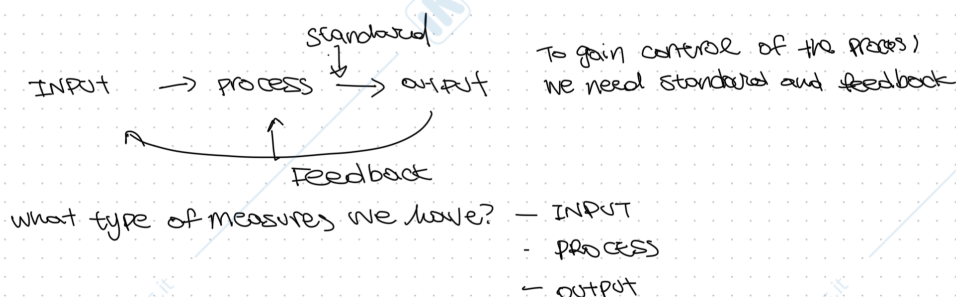
Financial measures alone, however, are insufficient for guiding and evaluating how companies create future value through investment in customers, employees, processes, and innovation. Financial measures tell the story of tangible assets; the balanced scorecard provides a window into the value created by intangible assets.

Well-designed scorecards enable both financial and nonfinancial measures to be part of the information system for employees at all levels of the organization.

The four perspectives of the scorecard permit a balance (1) between short- and long-term objectives, (2) between external measures—for shareholders and customers—and internal measures of critical business processes, innovation, and learning and growth, (3) between desired outcomes and the performance drivers of those outcomes, and (4) between hard objective measures and softer, more subjective measures.

EU law requires large companies to disclose certain information on the way they operate and manage social and environment challenges. Companies are required to include non-financial statements inter annual reports from 2018. This law only apply to large public interest companies with more than 500 employees. They need to publish reports on the policies they implemented in relation to social responsibility; environment protection; respect for human right; anti-corruption; diversity in board. Companies with high rating on ESG factors have a lower cost of capital. Sustainable investing means positive impact on the society, accepting higher risk or a lower return from the investment.

Using information



Information about INPUT is necessary but not sufficient

Next focus on also process and output

- 4 criteria for make the choice:
1. feasibility of monitoring and measurement
 2. understanding cause and effect
 3. costs
 4. desired level of innovation

① if it is possible to monitor the process or measure the outcome

↑
only if the manager
can observe the
process in action

↑
only if it is possible
to measure it accurately

② if the manager can't observe the cause-effect relationship means that there is no way to monitor the process

③ 2 types { cost of generating and processing information
lost opportunity or damages resulting from not generating the info

④ limit innovation → control process → ↑ efficiency

ES control input when:

- is not possible to monitor process or output
- cost of input is high
- quality / safety is important → limit innovation

control process when:

- process can be observed and measured
- cost of measuring process is low
- standardization for quality / safety
- cause-effect relationship are understood
- proprietary process can result in strategic advantage

control output when:

- output can be measured
- cost of measuring is low
- high innovation
- cause-effect relationship is not well understood

Culture is the tacit social order of an organization. When properly aligned with personal values, drivers, and needs, culture can unleash tremendous ampoules of energy towards shared purpose and foster an organization's capacity to thrive. The 4 attributes of corporate culture are:

- shared: culture is a group phenomenon
 - pervasive: culture permeate multiple level and applies very broadly in a organization.
 - Enduring: culture can direct the thoughts and action of group members over long term
 - Implicit: people are effectively hardwired to recognize and respond to culture instinctively.
- Culture will influence outcomes.

Organizing for performance

After business strategy has been set, managers must decide how to organize people and resource to achieve that strategy.

A work unit represents a grouping of individuals who utilize the firm's resources and are accountable for performance.

Accountability defines (1) the outputs that a work unit is expected to produce and (2) the performance standards that managers and employees of that unit are expected to meet. There are two basic types of work units: (1) groups of people and resources engaged in a similar work-process, and (2) groups of people and resources focused on a specific market. The former is often called a function; the latter is often called a division or business unit.

A function is the most basic organizational component, comprising a group of managers and employees who specialize in a specific work process.

Market-focus work units are normally found in one of the three basic configurations.

- by product: product division, these are created in order to exploit economies of scale and scope related to product specialization.
- By customer: these are found when the market needs of each customer segment are unique so that specialized expertise and knowledge about customers are essential to compete.
- By geography: they are often referred to as regional business. Specialization is required to understand and respond to local specificities.

Any firm when taken as a whole is a market-focus entity. For an intermediate level, a manager can choose market focus, general knowledge; or work process, efficiency but difficult to coordinate.

At the lowest organizational level, all activities are grouped by function to allow specialization.

Span of control indicates how many (and which) subordinates and functions report to each manager in the organization. It describes the resources—in terms of people and work units—directly under a manager's control. But span of control does not tell us what they are accountable for. For this, we need also span of accountability, which describes the range of performance measures used to evaluate a manager's achievements. Some managers may be held accountable for revenues only, for cost only, for net profit before interest and taxes, for return on asset. We have:

- cost center: only cost, no profit, no loss
- Profit center: associate to any single business unit
- Investment center: similar to profit center, we have responsibility of the investment

Span of attention refers to the domain of activities that are within a manager's field of view. In simple terms, it is what people care about and pay attention to. Managers must be able to influence span of attention at all levels of an organization if they are to have any success in achieving their profit goals and strategies. It is the core concept to centralization, narrow span of attention and no autonomy to manager, and decentralization, wide span of attention and it is essential when demands quick and agile responses.

Building a profit plan

Profit plans are the principal tools that managers use to price their business and operating plans. A budget refers to the resource plans of any organizational unit that either generates or consumes resources. The term profit plan is reserved for units that generate profits—stand-alone business units that generate and are held accountable for both revenues and expenses. The objectives of this planning process are:

- to translate the strategy of the business into detailed plan to create value.
- To evaluate whether sufficient resources are available to implement intended strategy
- To create a link between economic goals and leading indicators of strategy implementation.

The design of the business plan helps strategic management in encouraging a deep reflection about the future.

3 wheels of profit planning



The profit plan provides information on the economic resources available to the company and helps managers evaluate the trade-offs facing them.

Business plan is different from budget

Business plan is dimensioning of resource to achieve strategic goals. Once finished the business plan we moved to budget which is resource allocation of any organizational unit that generate revenue and/or cost.

	BP	Budget
Objective	Optimization	Rationalization
Approach	Comparative	Incremental
Perspective	Medium-term	Short-term
Reference	Business unit	Organizational unit
Criteria	Competitiveness	Controllability
View point	Global ↓ effectiveness in resource dimensioning	Functional ↓ efficiency in resource allocation

Aligning performance goals and incentives

Overall performance = performance goals + behavior

Performance goals can be measure in 3 levels:

- corporate level
- Business level
- Individual level

strategy focuses on the choices that must be made to create value for customers and differentiate products and services. However, successful strategy implementation requires communicating these strategic choices to hundreds or thousands of employees.

For the design of incentive systems, we must focus on:

- the definition of goals and objectives
- The design of performance measures and targets
- The role of incentives for motivation

The term performance goal is used to denote a desired level of accomplishment against actual results can be measured. They are important because:

- they indicate a set of strategic priorities.
- They provide managers with motivational tools
- Can be shared with stakeholders to communicate the prospects of the business

Critical performance variables indicate factors to be achieved for the intended strategy of the business to succeed.

In any goal setting process managers are required to choose the target or desired level of achievement. There are daily 2 steps toward this:

- benchmark comparison
- Motivation effort, level of difficult and challengeable task motivate more.

There are 2 ways to motivate people:

- intrinsic motivation: managers can emphasize the positive ideals and beliefs of the business so that employees want to contribute to its overall mission.
- Extrinsic motivation: a reward or payment that is expected to motivate performance

The term “incentive” implies that individuals are paid more when performance exceeds some base or threshold. This means that higher performance generates higher pay, lower performance, lower pay.

The final design of incentives concerns what types of incentives to provide to employees to recognize their achievements. There is a wide range of options concerning the types of financial incentives that can be provided: awards of company stock, grants of options for the future purchase of company stock, gifts and prizes, deferred cash payments.