


Balanced Scorecard implementation in SMEs: reflection in literature and practice

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Abstract

Research indicates that improved business performance is linked positively to the extent of use strategic planning within organisations. To reap these benefits, small and medium-sized businesses (SMEs) must introduce strategic planning processes in a way that is compatible with the constraints of being small – i.e. with limited resources to deploy on such programmes, and without compromising the classic SME benefits of being simply structured and highly responsive.

The Balanced Scorecard is a popular performance management framework strongly associated with managing the implementation of strategic plans. This paper discusses the challenges of, and potential benefits to SMEs from adopting the Balanced Scorecard methodology. It also makes observations about how use and value may differ between SMEs and larger enterprises.

In this paper the author draws upon literature and also information from the project archives of 2GC Active Management, a specialist consulting firm that has completed over 150 Balanced Scorecard design projects over a seven year period, for a wide range of organisation types and sizes.

Introduction

Recent research has shown that clear links between an organisation's approach to strategic planning and its business performance exist in small as well as in large organisations (Lyles et al 1993, Jennings & Beaver 1997, Juul Andersen 2000, Ernst & Young 2000, Davig et al. 2004).

“The root cause of either small business failure or poor performance is almost invariably a lack of management attention to strategic issues”

Peter Jennings, The Business School, Loughborough University, UK and
Graham Beaver, Nottingham Business School Nottingham Trent University England

Improved strategic management processes may also facilitate the development of the more complex management structures that are needed as small firms grow (Miller 1959, Atkins & Lowe 1997).

A popular tool used to support strategic management activity in large firms is the Balanced Scorecard. To date, reported activity to deploy management systems that are based around use of Balanced Scorecards has focused on large, multi-national, multi-divisional firms (e.g. Mobil, Cigna, AT&T, Motorola).

This paper discusses, from a practitioner point of view, the potential merits and feasibility of deploying Balanced Scorecard in SMEs as well as the way in which use and value may differ between its application between large and small enterprises.

Neither comprehensive literature nor empirical research exist on the topic of Balanced Scorecard in SMEs. Therefore, the arguments presented in this paper are based on a combination of general literature research on Balanced Scorecard, SMEs, strategic management and corporate planning combined with the authors' broad practical experience of facilitating Balanced Scorecard design and implementation projects in large and some smaller organisations including using it in our own small company.

About the Balanced Scorecard

The Balanced Scorecard is a performance management framework that has been widely adopted by both public and private sector organisations. Other broadly similar frameworks (for example, the French Tableau de Bord) predate its first appearance about fifteen years ago, but none has matched its popular appeal nor its rapid rate of adoption (Epstein & Manzoni 1997). In its earliest form, the Balanced Scorecard comprised simply a table of regularly reported performance measures, chosen to give managers a broad view of organisational performance - particularly with respect to activities to implement strategic plans (Kaplan & Norton 1992). Subsequently it has evolved into a more sophisticated and adaptable performance management framework used to support both strategic and

operational management activities (Lawrie & Cobbold 2004).

Background

Part of the Balanced Scorecard's success is due to the fortuitous timing of its introduction. Analog Devices, a US electronics firm, had developed a simple but effective management reporting system called 'The Balanced Scorecard' during the 1980s (Stata 1989). The framework organised a small selection of the firm's measures into four 'perspectives': 'Financial', 'Customer', 'Internal Process' and 'Learning & Growth'. Kaplan and Norton popularised the idea in the Harvard Business Review early in 1992 (Kaplan & Norton 1992). The original Kaplan and Norton article outlined a simple, "4 box" approach to performance measurement that was broadly similar to that of the Analog Devices design, but it was more explicit about the need to align the chosen of measures with an organisation's strategy.

Evolution

Although popular, early Balanced Scorecards were poorly received and not widely used by the managers they were intended to help, contributing to a high rate of abandonment for these '**1st Generation**' Balanced Scorecards (Lingle & Scheman 1996, Schneiderman 1999, Radnor & Lovell 2003).

In the mid 1990s the established theories that argued that managers used hypothesised relationships between the 'strategic objectives' identified for their business as a basis for management intervention (Argyris 1977, Mintzberg 1978) were deployed to help in the justification of Balanced Scorecard measure selection (Kaplan & Norton 1996a). Balanced Scorecard designs soon began appearing that recorded these objective-to-objective relationships. Alternatively called Strategy Maps or Strategic Linkage Models (SLM), these graphical illustrations initially attempted to connect the traditional perspectives described in the 1992 Kaplan & Norton paper. By stacking the four perspectives vertically the implied causality was from 'Learning & Growth' objectives to 'Internal Process' objectives, thence to 'Customer' objectives, and finally to 'Financial' objectives (Kaplan & Norton, 1996b). This addition helped with measure selection, and it characterises the '**2nd Generation**' of Balanced Scorecard.

2nd Generation designs made measure selection easier, but problems with the approach were still evident (e.g. Butler et al 1997). In the late 1990s a solution emerged based around the development of a third element of the Balanced Scorecard design – a document known initially as a 'Vision Statement', and later renamed as a 'Destination Statement' to avoid confusion with other uses of the term Vision (Guidoum 2000). The Destination Statement helped both with the design of the Strategy Map element of the Balanced Scorecard, and with target setting for the measures eventually selected.

Related fieldwork showed that the conceptual problems introduced by the Strategic Linkage Model concept – particularly in the public sector (Butler et al 1997, Irwin 2002) – could be addressed through use of a 'Strategy Map' with only two perspectives - one for 'Activities' and one for 'Outcomes' (Cobbold et al 2004). Together these two innovations characterise the '**3rd Generation**' of Balanced Scorecard design, and represent current best practice for this type of activity (Lawrie & Cobbold 2004).

3rd Generation design methods have been in use for about six years, and have continued to evolve and develop. They are particularly well suited for 'cascading' of Balanced Scorecards through an organisation (Lawrie, Cobbold & Marshall 2004).

The Balanced Scorecard in Large Enterprises

Since its introduction in 1992 writing on the Balanced Scorecard focuses on its application in large organisations, drawing on case examples like e.g. Mobil and CIGNA (Kaplan & Norton 1996c, 2000), ABB, Skandia, SKF and Halifax (Olve et al 1999) – all multi-billion dollar companies.

One explanation for this predominantly large company focus may be found in the challenges of communication, coordination, and control in large organisations. The task specialisation and levels of organisational hierarchy that is required to support the scale of the organisation make all forms of change more difficult in large organisations (Miller 1959, Newman & Rowbottom 1968, Sprott 1973, Simon 1976, Moss Kanter 1979, Hatten & Rosenthal 1999).

Application of the Balanced Scorecard in SMEs

Literature on the use of Balanced Scorecard by SMEs is limited, but this should not be taken as an indication that Balanced Scorecard implementation is only appropriate for large organisations. Core to this view is our experience of benefiting from having implemented the Balanced Scorecard in our own organisation and the proposition that many basic strategic management issues are relevant in both small and large organisations. Examples of these include:

- ∞ *The need for a clear sense of direction*: where is the organisation headed?
- ∞ *Managers must have a profound understanding of the business model*: is the organisation doing all the things it needs to be doing?
- ∞ *An ability to focus and prioritise*: how to strike the balance between long-term development and short-term operational pressures?
- ∞ *Agility*: flexibility driven by learning: how to incorporate new knowledge in the strategic and operational planning processes?

Common to each of these issues is the need for the identification, pursuit and achievement of strategic goals. Recently it has become common for these to collectively drive towards fulfilling stakeholder expectations in general, and for publicly quoted firms in particular to deliver Shareholder Value.

“Pick up most well respected finance texts and you will find the maximisation of returns to shareholders being quoted as being the key business objective”

R. Mills, Professor of Accounting and Finance, Henley Management College

Using the Balanced Scorecard as part of a “Strategic Management Framework”

The Balanced Scorecard was originally proposed as an approach to performance measurement that combined traditional financial measures with non-financial measures to provide managers with richer and more relevant information about organisational performance, particularly with regard to key strategic goals (Kaplan & Norton 1992). By encouraging managers to focus on a limited number of measures drawn from four ‘perspectives’, the original Balanced Scorecard aimed to encourage clarity and utility.

Over time Balanced Scorecard has developed to form the centre-piece of a strategic communication and performance measurement framework that helps management teams articulate, communicate and monitor the implementation of strategy using a system inter-linked with the long-term destination of the organisation.

More recent insights suggest that a successful Balanced Scorecard implementation will require adjustments to be made to other management processes used by the enterprise. Only in so doing will the Balanced Scorecard be able to become a central part of a “strategic management framework” (Kaplan & Norton 1996a; Epstein and Manzoni 1997)

“To be successful the Balanced Scorecard must be viewed as the tip of the improvement iceberg.”

A.M. Schneiderman, Consultant on process management

It is, in our experience, this evolution of Balanced Scorecard methodology that has increased its relevancy for small companies. The reason being that in SMEs a greater proportion of the value of Balanced Scorecard comes from its use to formalise the description of strategic destination and associated strategic objectives and priorities in a way that builds consensus; and the impetus it gives to the development and application of more effective strategic and general management processes – both areas that are normally only weakly addressed in SMEs (Jennings and Beaver 1997).

Characteristics of Small and Medium Sized Enterprises

Much work has been done to identify ways in which management practice in small and medium-sized enterprises (SMEs) differ from larger ones. Two linked areas of comparison have been differences in organisational structure, and differences in management processes. SME’s (particularly small ones) have been characterised as being typically “simple structures” or “simple systems” in which the leader (often the entrepreneur or owner-manager) directs the work of a small number of operators with the help of few or no other managers. At around 100 staff, this type of approach begins to become

inefficient, and by the time the enterprise has about 500 employees some sort of hierarchical structure has been introduced – most commonly introducing a layer of managers each tasked with management of a functional area of activity. As the organisation grows, further structure changes occur driven by the increasing problems of communication and co-ordination. It has been observed that the points of transition between organisational forms present or represent particularly risky periods for the enterprise, during which enterprise failure is not uncommon (Mintzberg 1981). Coordination in small organisations mainly happens through direct instruction and supervision, minimising the need for formal management (i.e. planning and control) processes. Many see this as a key strength of the smaller enterprise, since by avoiding extensive standardisation and coordination, and the associated need for support staff and line-management; small firms maintain their flexibility, responsiveness and low cost structure (Miller 1959, Mintzberg 1981).

Balanced Scorecard design process

A wider sense of ownership of a strategy by the organisation is understood to be as important as effective strategy formation. Whether an organisation is large or small, success ultimately depends on persuading employees to align their behaviours with the enterprise's strategic goals, and it has been argued that this is best done through clear communication of the goals, and the enlisting of active support for their achievement from within the organisation.

“One may say that on the whole people do not like being ordered about.... it is not so much being led that people resent, as being controlled by some external power whose intentions are not coincident with theirs”

W J H Sprott, Social Psychologist

In large organisations the complexity of the internal operational environment is high (Miller 1959; Atkins & Lowe 1997), and achieving establishing “insight into value creation” becomes more complicated (Campbell & Alexander 1997): one person can no longer fully capture the activities of the enterprise and determine better strategies for success.

“Most of the insights important for strategy formulation reside in the heads of the operating managers.... excluding them from strategy development means excluding their insights as well.”

Marcus Alexander & Andrew Campbell – Directors
Ashridge Strategic Management Centre

Because of this, best practice Balanced Scorecard design methods for medium and large organisations call for a collective effort, drawing upon the combined operational and strategic insights of the key employees involved with running the business (e.g. Shulver et al, 2000). Failure to use a collective approach may weaken the value of the strategy itself (Simon 1957, Mintzberg 1990) and its implementation due to lack of support from those accountable for executing it (Thomson's “dominant coalition”: Thomson 1967).

We see Balanced Scorecard design as the initial effort to produce physical documentation – a destination statement, some strategic objectives arranged on a strategic linkage model, and some measures and targets for each objective. This documentation forms the reference material for subsequent implementation and use of the Balanced Scorecard by the organisation: something we see as a quite separate activity (i.e. design does not require or imply implementation).

A modern Balanced Scorecard design process for a large organisation typically takes an elapsed time of 12 – 14 weeks. Most of the design work is completed during three or four one-day workshops involving the relevant management team. Including additional design activities outside the workshops, each participant is normally expected to commit between four and five days to the design process across the period – equivalent to less than half a day per week. Subsequent implementation of the device takes between three and six months in most organisations – sometimes longer but rarely shorter.

Key elements of a Balanced Scorecard design

Destination Statement

In order to make rational decisions about organisational activity and not least set targets for those activities, an enterprise should develop a clear idea about what the organisation is trying to achieve (Senge 1990, Kotter 1996). Accordingly, the most effective Balanced Scorecard design processes use the creation of a strategic destination statement describing, ideally in some detail, what the organisation is likely to look like at an agreed future date (Olve et al 1999, Shulver et al 2000, Lawrie & Cobbold 2004). In many cases this exercise builds on existing plans and documents – but it is rare in practice to find a pre-existing document that fully serves this purpose within an enterprise.

A Destination Statement usually is designed to fit onto a single page – but in some less common cases the statement has covered many pages (the most in the 2GC archive being 13 pages). An example of a Destination Statement developed by a small IT firm with support from 2GC is attached as Figure 1. In practical terms this example is little different in style or structure to those produced by very large organisations. The Destination Statement is broken into several sub-sections – these broadly equate to the original ‘perspectives’ of the 1st Generation Balanced Scorecard, and serve a similar purpose – to encourage the authors to think broadly about the aims and requirements of the organisation.

Strategic linkage model / strategic objectives

Once the strategic destination has been established the next step is for the same group to agree on the most important strategic activities and outcomes (strategic objectives) required for the destination to be achieved. Best practice calls for this process step to focus on the actions directly within the scope of the team building the Balanced Scorecard – increasing the likelihood that the objectives agreed will (or can) be pursued once the design process is complete.

By representing the selected objectives on a “strategic linkage model” (see Figure 2 – which is part of the same Balanced Scorecard design as the Destination Statement in Figure 1), the design team is encouraged to apply “systems thinking” (Senge 1990; Senge et al. 1999) to identify cause-and-effect relationships between the selected objectives – this is a useful test to ensure the objectives chosen are mutually supportive. Though it should be noted that formal modelling is not used to develop the objectives – the actual process used is a simple one, but outside of the scope of this paper to describe. But the method used is the same in both small and large organisations in the 2GC project sample.

The importance of clearly articulated objectives is highlighted by. Lingle & Schiemann (1996), who warns against what they call “fuzzy objectives” as a frequent cause for lack of implementation and expected results.

In Figure 2 the chosen strategic objectives are spread across just two zones or ‘perspectives’. This is a simplification of the type of layout seen in early documents describing 2nd Generation Balanced Scorecards – which are usually shown having the classic four Balanced Scorecard perspectives arranged vertically on the page (with Financial at the top).

In Figure 2, the lower perspective contains ‘Activity’ objectives – i.e. objectives describing things the management team is planning to do in the short / medium term. These broadly overlap with the type of objectives found in the lower two perspectives of a typical 2nd Generation Balanced Scorecard (Internal Processes, Learning & Growth).

The top perspective on Figure 2 contains ‘Outcome’ objectives – i.e. objectives relating to the anticipated consequences of the Activity objectives on the same diagram. These objectives are similar to the ones typically found in the top two perspectives of a typical 2nd Generation Balanced Scorecard (External Relations / Customer, Financial).

Developing a ‘strategic linkage model’ as described above can help a management team to:

- ∞ test the validity of a business model by developing a thorough understanding of the model and its strategic/operational requirements
- ∞ identify the most important strategic objectives in the form of a coherent strategy spanning the whole spectre of the business and that way create the necessary focus for things to get done



Figure 1 – Sample Destination Statement

This destination statement was created by a client of 2GC Active Management during 2004. The client firm is a small IT services company in the UK. The five-year horizon, and the relatively concise description of how the management team envisage their organisation to look at that time is quite consistent with Destination Statements designed by other organisations, regardless of size.

Smallco Destination Statement MAY 2009

Financial and Buyer Expectations

- F/BE1 - We have a turnover of EXXm+ from: circa EXXm+ Consulting, circa EXXm Licence sales EXXm SLAM/optimisation
- F/BE2 - We have a net profit of EXXm+ (8%)
- F/BE3 - Smallco is owned by the founders 60%, staff 20% and external/venture capitalists 20%
- F/BE4 - Our sales revenue is split 75% private sector and 25% public sector
- F/BE5 - Our sales revenue is split 70% large 20% medium and 10% small organisations
- F/BE6 - We make 85% of our sales revenue in the UK, 10% in Europe and 5% in the rest of the world
- F/BE7 - We have successfully acquired (and possibly integrated) two consulting businesses: one of 100 or so people and one smaller specialist of 20 people and have established offshore resourcing capability
- F/BE8 - We have a focus on growing our "annuity" services covering recurring contracts ("annuity" revenue) and regular repeat purchasing from long-term clients ("annuity" relationships)
- F/BE9 - We have established a "franchise" model for growth outside the UK
- F/BE10 - We have an established process for evaluation of options to expand our services outside of the ERPSOFT world (JDE, Retec, Siebel, Peoplesoft capability)
- F/BE11 - We have a business that is attractive to potential buyers, having:
 - A strong brand
 - Sustainable revenue and profit growth
 - Long-term customers
 - Scalable processes
 - Market leadership
 - Strong management

External Relationships

- ER1 - We are the UK's leading independent consultancy providing expert advice and solutions to the ERPSOFT community and our clients see us as their "trusted advisor" in all matters relating to ERPSOFT - the company, their product and services, and their strategies
- ER2 - Our clients benefit from our ability to understand of their business drivers and trends within their vertical industry sector
- ER3 - We optimise clients' use of ERPSOFT technology and services to maximise their ROI
- ER4 - ERPSOFT Corporation management see Smallco as an enabler of growth at low cost, through innovative routes to market
- ER5 - ERPSOFT sales see Smallco as a trusted safe pair of hands
- ER6 - Smallco's employees see being with the company as the best career move they ever made
- ER7 - Smallco are consistently quoted by the UK IT press on ERPSOFT matters
- ER8 - Smallco's key supplier/partner relationships are with:
 - ERPSOFT
 - Management consultants
 - ERPSOFT tech/apps specialists
 - The associate/contract agency market
 - Market intelligence specialists
- ER9 - Our suppliers see Smallco as one of their most valued clients

Organisation & Culture

- O&C1 - We have a "can do-will do" culture
- O&C2 - We have strong Intellectual Property in our people, our ERPSOFT knowledge, SLAM and our customer database
- O&C3 - We have a communication programme that successfully allows our management and employees to be fully up to speed with all relevant information
- O&C4 - We have established a performance management framework that enables alignment of individuals' performance to the company's business objectives
- O&C5 - We have successfully recruited the right people with the right cultural fit for all job functions
- O&C6 - We have maintained our strategy to outsource non-core business functions
- O&C7 - Our success as a "trusted advisor" comes from our continued focus on putting our clients first
- O&C8 - We celebrate our successes and share and learn from our failures
- O&C9 - We have, wherever possible, maintained a predominantly virtual office approach
- O&C10 - We have approximately 150 full-time employees
- O&C11 - We have a less than 10% attrition rate
- O&C12 - We have an established personal and career development programme to enable our employees to reach their full potential
- O&C13 - We have a Finance and an HR Director with specific fast growth company experience
- O&C14 - We have developed a strong operational board through developing our own management talent
- O&C15 - We have appointed non-executive directors and board advisors with specific experience in taking companies to trade sale or flotation
- O&C16 - We maintain an active pool of associates and contractors

Processes & Capabilities

- PC1 - Our use of on-line electronic collaboration allows us to share standard templates so that our business process and support systems are repeatable and efficient
- PC2 - Our best practice sales methodology comprises: planning (accounts, territories, compensation) and management (lead, opportunities, budgets, forecasts) supported by our centralised customer and prospect database
- PC3 - We use clear and well understood processes with defined responsibilities for the qualification and winning of bids, the delivery of projects and post-sale customer management
- PC4 - Our business is supported by an infrastructure comprising HR, training & development, finance and IT
- PC5 - Our learning and sharing culture is underpinned by our Knowledge Management system
- PC6 - Our commitment to people is demonstrated by our Investors in People accreditation
- PC7 - We have evolved a strong quality and risk management culture supported by effective and proven management processes
- PC8 - We have integrated marketing processes that enable campaign planning, ROI analysis, integration into the sales process and multi-channel capabilities, whilst continually promoting and strengthening the Smallco brand

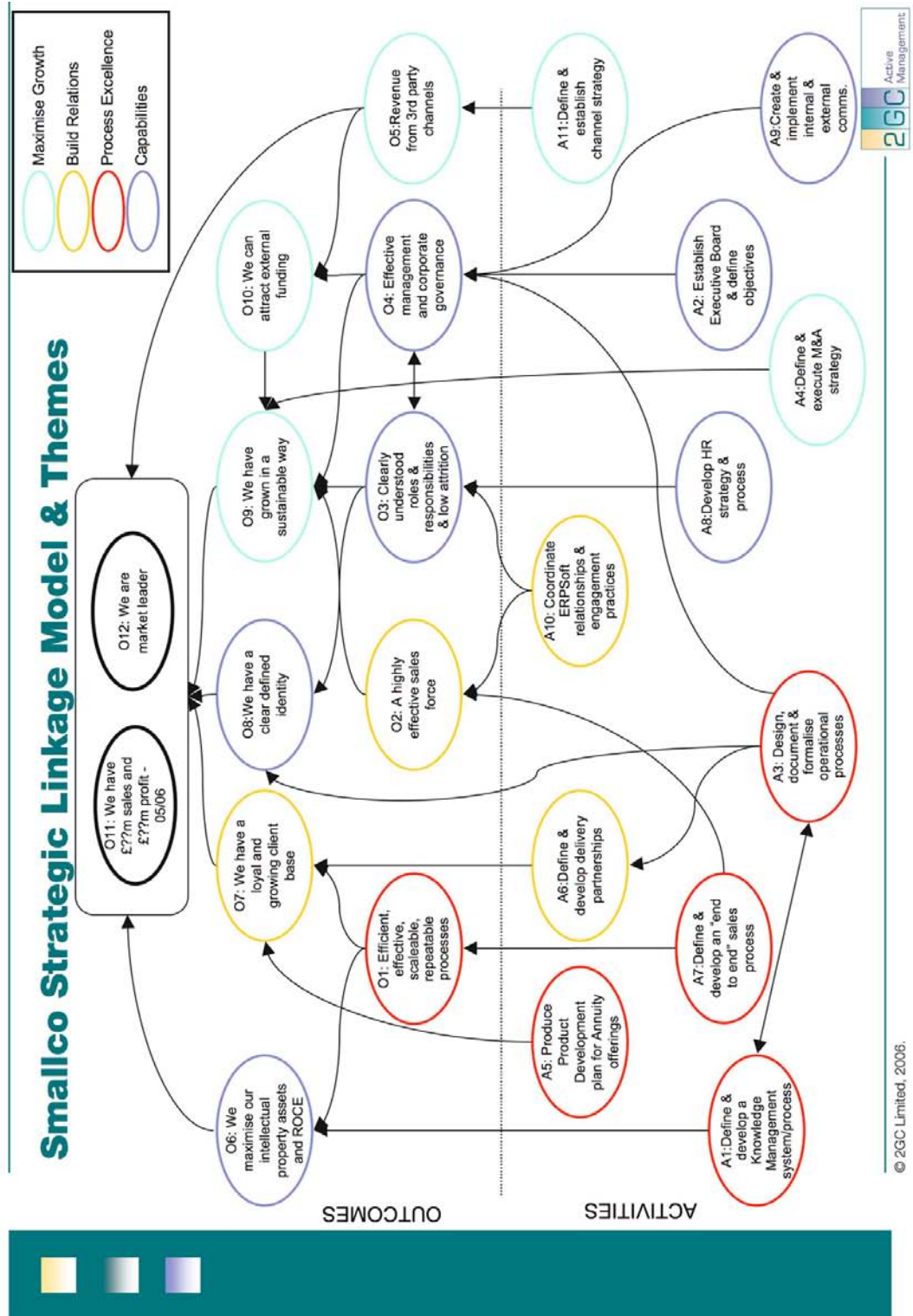


Figure 2 – Sample Strategic Linkage Model

This is the Strategic Linkage model developed by Smallco, and is part of the same Balanced Scorecard as the Destination Statement shown in Figure 1. The complexity of the diagram, both in terms of number of objectives and the number of links between objectives is consistent with those developed by other organisations regardless of size.

Measures

Balanced Scorecard designs in large enterprises normally include an elaborate process for identifying and describing measures selected to inform management about the organisation's progress towards achievement of its goals (Olve et al. 1999). In SMEs (particularly small enterprises) the utility of formal measure definition is lower. The limited size and complexity of the organisation means that managers are often well aware (at least collectively) of all performance related issues due to the limited size and complexity of the organisation (Miller 1959; Mintzberg 1981). But identification of measures, at least to the extent where targets can be set and followed up, does help to test the validity of the assumptions about cause and effect on which the design team has based its strategy. Without a deliberate approach to testing assumptions aimed at informing the choice of corrective action, the idea of planning risk losing part of its value – an aspect further highlighted below. Because of this, some SMEs, though not all, will find measure definition activities of value.

Balanced Scorecard design in SMEs

Balanced Scorecard design in an SME needs to generate similar documentary outputs to those produced in larger organisations, and so will require similar process steps to those used in large organisations. A key difference is the duration of the process. In general design happens more quickly in small organisations – typically requiring 6 – 10 weeks – largely due to less diary conflicts for the team coming together to build the Balanced Scorecard mean the design meetings can happen more frequently.

Insofar as the Balanced Scorecard design process can be said to provide a structured or formalised representation of strategic plans, it can be argued that developing best practice Balanced Scorecards encourages SMEs to engage in (simple) strategic planning – the importance of which to SMEs was considered earlier.

As noted above, in many cases, SMEs developing Balanced Scorecards do not go on to formally collect or report the measures defined during the design phase. Feedback from 2GC client organisations suggests this is due to a mixture of resource constraint and a perception that the measurement information required is already known to the management team and so does not require reporting formally. Such failure to collect and report the measurement data is less common in larger organisations, where it harder for the senior managers to 'keep tabs' on all the activities within the organisation – and so it is more likely that the Balanced Scorecard measures are able to provide managers with 'new' information.

Deployment

It is a truism, but a Balanced Scorecard needs to be used to realise its full value. Balanced Scorecards fail when, having developed strategic goals and identified relevant performance measures an enterprise doesn't use the information provided to drive changes in the way the organisation works (Schneiderman 1999).

For example, if an organisation is strongly budget orientated in its planning approach, the budgeting cycle will have to change and take its starting point at the Balanced Scorecard. If not, the long-term strategic requirements highlighted during the Scorecard design process are not likely to be integrated in the short-term financial planning of the budget. As noted by Jennings & Graham (1997), the balancing of long-term development with short-term requirements for survival is a particularly important issue for small companies and start-ups – failing to get the budget process aligned with the strategic goals of the enterprise can make achieving this balance harder.

Often, implementing changes to management processes requires a management team or manager to "take a leap of faith" in support of their new management system (Schneiderman 1999) and will then require long-term top management commitment to sustain the changes. Herbert Simon, Robert Schrank and Rosabeth Moss Kanter suggests that, breaking these old habits and instilling new behaviours should start with managers changing their own ways.

"If we are to change our institutional arrangements from hierarchy to participation, particularly in our work places, we will need to look to transformation of ourselves as well"

Robert Schrank, Sociologist

Instilling a sense of direction combined with focus and prioritisation

The use of the Balanced Scorecard as the centrepiece of a strategic management system, as described in this paper, naturally promotes goal and task delegation. By jointly constructing and communicating a well-articulated and logical plan, supported by an efficient approach for monitoring its implementation, management and the rest of the organisation is encouraged to focus on critical strategic outcomes in preference to narrow functional or tactical factors. By enabling component parts of an SME organisation to coordinate activities with reference to a clearly articulated corporate strategy, as described above, senior managers can reduce the time spent on detailed operational management control, freeing up management resources that can more valuably be applied to coordinate further developments of the organisation. Introducing a strategic management system based on the Balanced Scorecard may therefore defer the need for the organisation to move to more complex organisational structures (Miller 1959) with potential positive consequences for cost base as well as potentially retaining more innovative flexibility (Mintzberg 1981).

Finally, where an organisation has a clearly defined strategic destination and an equally well-defined strategy for getting there, the risk of 'scope creep' is reduced. It is well documented that organisations underestimate the risks of following novel opportunities for potential growth in new and related business areas. For the innovative entrepreneurial organisation in particular taking them on may seem like an easy way to achieve added growth – "We just work a bit harder". But pursuing new opportunities carries both additional business risk, and the risk of neglecting established long-term goals (Bhide 1996, Jennings and Beaver 1997). A number of times, we have benefited from using our destination statement and strategic objectives as basis for evaluating the added value and strategic fit of new opportunities.

Understanding the business model

Although the discussion so far has focused on introducing Balanced Scorecard thinking to an established SME, this is not a pre-requisite. Adopting the Balanced Scorecard approach during the planning stages of a business venture has its distinct advantages in terms of its ability to help a management team clearly articulate the goals of the venture, and the activities that will realise the goals. It also will highlight areas with the greatest need for change, and may prove useful in securing the necessary external backing for the business.

Just as the Balanced Scorecard design process helps demonstrate and prove/disprove a business model to the entrepreneur and/or management team themselves, so the ability to communicate a well articulated and logically constructed plan supported by an efficient approach for monitoring its implementation will help any organisation trying to gain or sustain the support of external stakeholders (Bhide 1996) – another area where we feel our Balanced Scorecard has been useful. The importance of demonstrating a sound approach to management, not only while seeking initial funding but also for later investor evaluation of the organisation is emphasised by recent research showing that 35% of investor decisions are influenced by non-financial issues with strategy and quality of corporate strategy being the most important (Ernst & Young 2000).

"The actual root cause of failure [of SMEs] may be seen to lie with the apparently non-rational behaviour and decision-making of the entrepreneur and/or owner-manager who does not obey the 'rules' of classical management theory"

Peter Jennings, The Business School, Loughborough University, UK and
Graham Beaver, Nottingham Business School Nottingham Trent University England

Increasing flexibility and learning

The concept of using the Balanced Scorecard as a central part of a strategic management system (Kaplan & Norton 1996a, 2000) is based on a "double-loop learning cycle" (Argyris, 1977; 1991), which calls for regular appraisal of strategic performance by asking three questions:

- ∞ Have we done what we set out to do?
- ∞ Have we achieved the results we thought we would?
- ∞ What do we need to do differently in future?

The answers to these questions and information about changes in the external environment form the basis for wider analysis and discussion leading to decisions about continuing validity of the strategic choices originally described in the Balanced Scorecard. The information provided by the Balanced Scorecard can therefore drive changes in both the objectives and measures used to track them. Such

changes are likely to reflect a combination of changing market and organisational conditions as well as increased learning about cause and effect assumptions. Mintzberg 1990 and Simons 1995 each suggest that enterprises that include this type of “interactive component” (which can allow for ongoing adaptation of plans to include “emergent strategies”) in their planning and review processes, are more flexible and adaptable in their responses to external changes than those that do not.

How formal the Balanced Scorecard review process will need to be will vary greatly depending on enterprise complexity and culture. Similarly the effort applied to the collection of Balanced Scorecard measures varies widely. Setting up formal processes to collect measure data may be seen by small organisations as an unjustifiable administrative burden. But experience from our own company shows that highly informal measurement collection processes work well in small organisations: The greater transparency in these companies tends to make formal and potentially time-consuming information collection exercises redundant. Instead, the output of the design process serves mainly to provide a framework for organising a verbal or even mental thought process “of asking questions and listening to answers...and [resolving questions on] the relevance of basic assumptions about its objectives, strategy, and operations, and their interactions.” (Hatten & Rosenthal 1999) – an often-neglected process in small companies according to e.g. Jennings & Beaver (1997).

The experience at Smallco

The illustrations of Balanced Scorecard elements in this paper come from a 2004 project for UK small firm Smallco (name changed) – a small IT services firm. For Smallco the design process took a total of sixteen weeks to complete (see figure 3). The design process was considered successful by the management team, but the emphasis was firmly placed on the value of the design activity itself – the articulation of shared strategic goals and their subsequent communication to the organisation – rather than on the measuring and monitoring it enabled. Here are some of the comments provided by the management team in the follow-up review meeting after the project had finished:

- “2GC’s process is a good one. All of the team enjoyed the process... and the facilitation”
- “The project harmonised the management team’s views of the organisation’s destination”
- “The process engendered a strong management consensus on key issues, smoothing over potential political issues
- “We now have a common feel and understanding of where we are going”
- “We now have a spirit of being on the same trip, lined up in the same direction”
- “The project helped to deliver greater management teamwork and motivation”
- “We have a common language and a common vision of what we need to do”

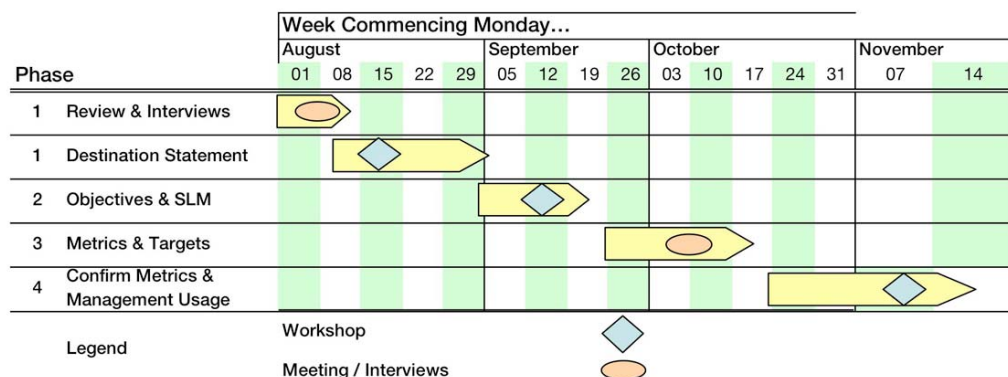


Figure 3 – Smallco Balanced Scorecard design project plan

Conclusion

Despite the lack of comprehensive literature focused on Balanced Scorecard implementation in SMEs we believe Balanced Scorecard and its associated management processes can prove equally beneficial to SMEs as to large organisations.

However, the potential benefits are likely to differ between the two. In large / complex organisations much of the utility of Balanced Scorecard comes from the communications elements: the two-way provision of concise and relevant summary information about 'what is going on' in the organisation. In smaller firms such as our own, a greater proportion of the value of Balanced Scorecard comes from two other elements: the description of strategic destination and associated strategic objectives and priorities in a way that builds consensus; and impetus given to the development and application of more effective strategic management processes.

However, the Balanced Scorecard used at the centre of a strategic management system addresses effectively a number of the fundamental issues relevant to large as well as small businesses:

- ∞ *A clear sense of direction*
The Balanced Scorecard framework is an efficient tool for clearly articulating long-term strategic goals in the form of a destination statement that can be translated into short-term activities
- ∞ *A profound understanding of the business model*
Identifying strategic objectives within the four business perspectives of the Scorecard and linking them in an expression of cause-and-effect relationships forces managers to apply "systems thinking" and develop a holistic strategy covering all aspects of their business – an equally important exercise for mature organisations as well for start-ups.
- ∞ *An ability to focus and prioritise*
Focusing on a clearly defined destination for the future and a clear strategy for how to realise it will help any company reduce the risk of losing sight of what they are trying to achieve
- ∞ *Organisational agility*
Using the Balanced Scorecard to regularly check whether the organisation is doing what it set out to do and is achieving the results it expected, creates learning about the validity of the cause-and-effect relationships. It also forms a useful foundation for deciding what needs to get done in the future based on the above learning and any changes in the external environment

In SMEs these Balanced Scorecard benefits can be achieved without the need for developing a complicated and administratively demanding measurement regime by simply using the Balanced Scorecard and its measures as a mental or verbal frame of reference for addressing general strategic and operational change issues resulting from the pursuit of long-term goals. These are real benefits experienced in our own company.

But successful Balanced Scorecard implementation in any organisation requires sustained management commitment to using it making sure it drives the necessary behavioural changes within the organisation, starting with the managers themselves.

Observing these success criteria, Balanced Scorecard can prove an effective tool for SMEs in meeting the challenge posed by the need to introduce more efficient strategic planning processes while retaining the competitive advantage of having relatively simple structures.

Finally, it should be noted that although this paper has highlighted the existence of important potential and real benefits to SMEs from applying the Balanced Scorecard as a strategic management tool, there is an obvious need for further substantiating these conclusions through empirical research.

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Useful Web Resources

2GC maintains an extensive collection of free-to-download documents relating to performance management and Balanced Scorecard design. The resources include copies of working research papers, presentations, case studies, and answers to FAQs. The site also contains two databases – one of internet sites with performance management related content, and one with details of software firms offering performance management reporting software packages.

All the information on the site is free to download – find it at <http://www.2gc.co.uk/resources.asp>

About 2GC

2GC is a research led consultancy expert in addressing the strategic control and performance management issues faced by organisations in today's era of rapid change and intense competition. Central to much of 2GC's work is the application of the widely acknowledged 3rd Generation Balanced Scorecard approach to strategic implementation, strategy management and performance measurement.

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