Measuring Success

By Mano Mahadeva, CPA, MBA | Column Editor

Investors periodically look at key measures to assess a company's sustainability and value. In other words, they look for a yearly increase in top-line growth and greater efficiency as the company grows. Top-line growth has two components – same store or organic growth (i.e., the core business showing steady growth) and inorganic growth, which is a robust pipeline of new products, services or acquisitions. Greater efficiency has two components – capital efficiency and operational efficiency – i.e., improving leverage as we spend money on capital items and hire capable people. To keep investors engaged and enthused, we need a level of discipline and skill necessary to continuously gather and measure relevant business data to share our success.

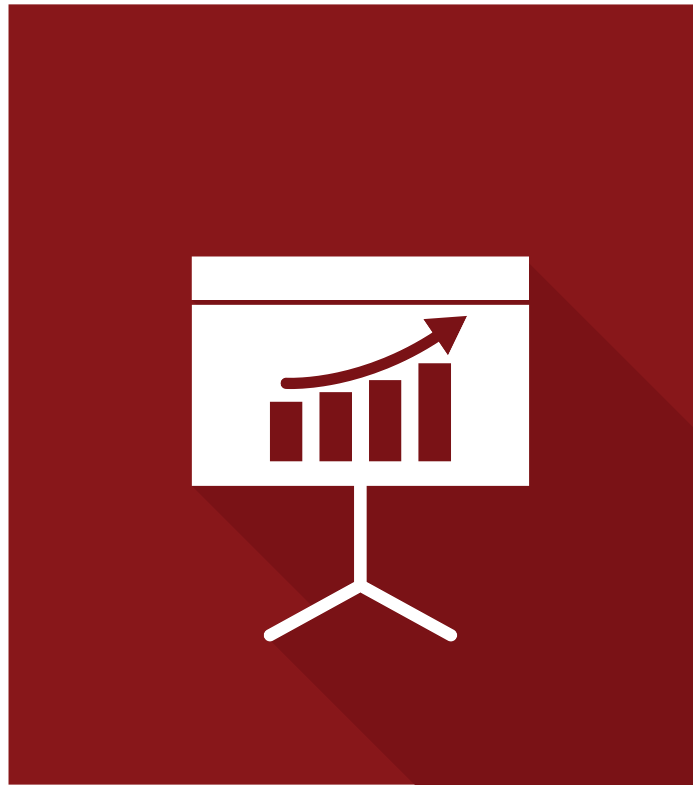
Measurement of relevant data plays a vital role in setting strategy, organizational objectives and manager compensation. But we won't know if we are succeeding unless we define what these data measures are and track them. So many questions abound. What needs to be measured? When should they be measured? How should they be measured? Ambiguous answers to these types of questions or ignorance typically result in mismanagement by business leaders.

Example 1 – A company had a dashboard of measures, about a page long, begun and agreed to by a group of leaders many years ago. Over the years, some of them left the organization and new leaders added more measures to the already existing list. The font sizes became smaller as more measures were crammed onto the same page. As new products and services were added to the company, more measures were added to the existing list, so now the one page that had small fonts became two pages with small fonts. Soon, the organization lost focus across all areas as division heads were overwhelmed with tracking and analyzing too many measures.

Example 2 – The head pharmacist of each pharmacy across a network was incented to keep inventory low at the last day of each month. So the pharmacists bought an estimated amount of inventory on the first day of each month and ran it low to near zero at month end. This resulted in some lost sales due to no availability of product. The sellers of products wanted to see periodic sales across the month versus a one-time sale each month. So the company shifted to an economic order quantity model with appropriate incentives for the buyers, across each month, which satisfied all constituencies.

From these examples, it is important to understand why everyone within the organization needs to understand the adopted measures (definitions and relevance) and the behaviors they create. In the first scenario, it was clear that there were too many measures and that there was no regular review of how they were relevant to present performance. As a result of chasing all measures, the organization lost its focus on the overall mission.

In the second scenario, the department heads understood the measure, but their focus was not aligned with that of the company. Also, the definition of the measure was not well thought out and improperly aligned incentive compensation of the department heads and that of the company's goal of low inventory.



Measures are important in that they highlight what is important for success. They provide a medium to communicate objectives, activities and performance within the company. They provide a way to monitor and reward performance by aligning strategic objectives with that of personnel incentives. They also create constructive feedback in a timely manner.

Measures need to be simple and easy to understand. Everyone needs to understand how these fit within the big picture. We need to have a few of them, versus too many, so that we remain focused. The definitions of each must be unambiguous, consistent and operationally grounded. We need to confirm that the data used in calculations are not mislabeled in any way. Results need to be timely and accessible by those who use them. And the assumptions underlying actions need to be constantly questioned to make certain that the measurements used are still valid.

Do not measure for measurement's sake. And don't do so without looking for evidence that they are relevant and that they work. Better information and better decision making can help uncover new opportunities and create a competitive advantage. It is important that the entire company has bought in, as it helps to create a culture of celebration and success.

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