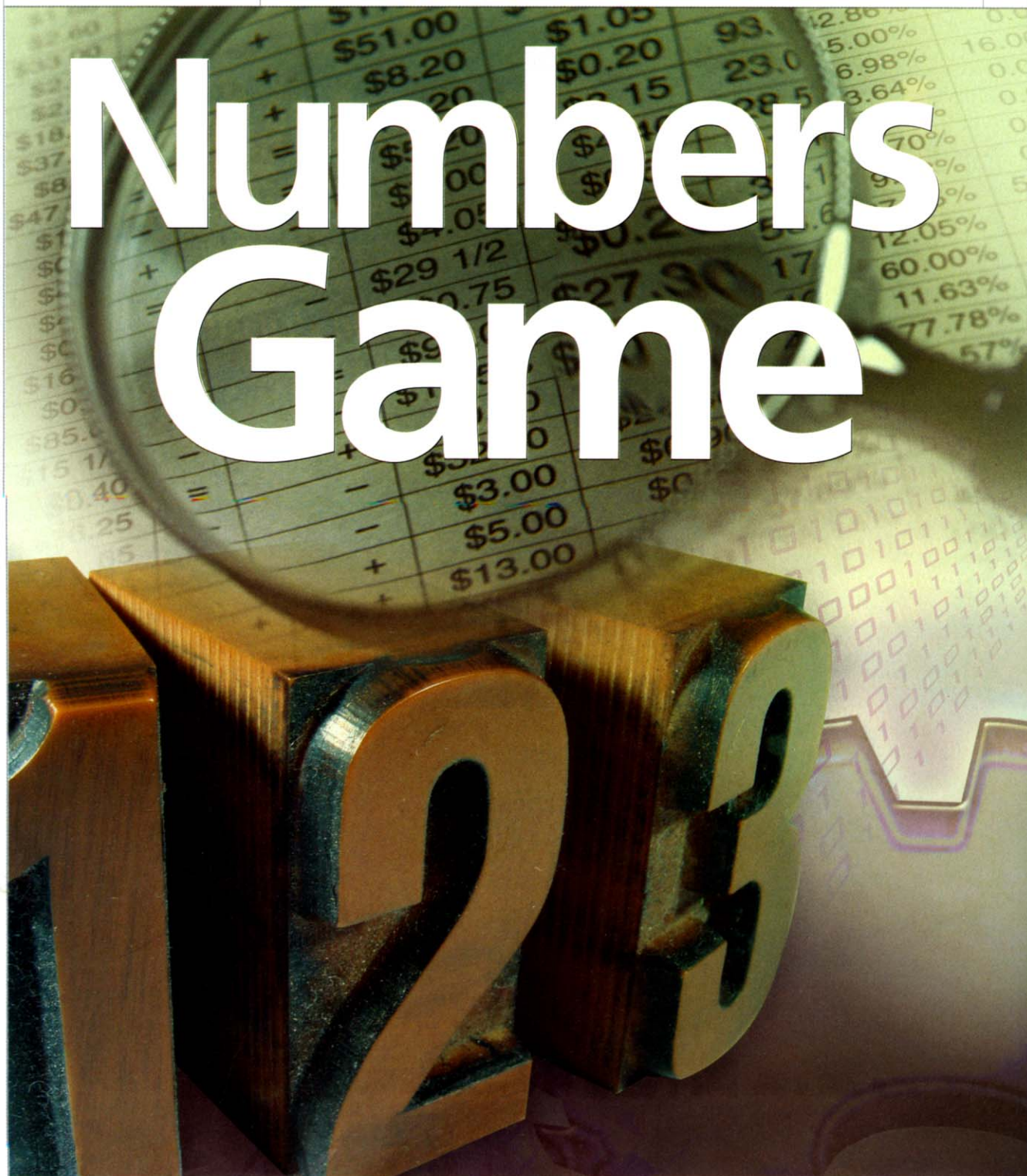


Is your company measuring the things that actually drive your business? If not, immediate changes are in order. Grayson Walker reports.

Numbers Game



Business is a numbers game, pure and simple. Sales figures, profit margins, returns on investment, department headcounts, and innumerable other metrics determine the ultimate success, falter, or failure of a business. For publicly traded companies, Securities and Exchange Commission reporting requirements and Sarbanes-Oxley rules govern what types of numbers companies are required to disclose. But just because a certain number must be disclosed doesn't mean that number is vital to the overall health and performance of the company.

So, is your company keeping track of the right metrics to move the business forward?

"What has been facilitated by technology is the ability to track and measure a lot of things. The challenge is not to measure too many and to track those that drive the business," said Tony Curtis, principal in the manufacturing services division of The Rehmann Group, a top CPA and consulting firm based in Saginaw, Mich. "In most cases, companies measure too many things—what I call paralysis by analysis—instead of focusing on key drivers."

The key drivers for any business depend on its size, its industry, and its goals, so there isn't a one-size-fits-all solution to share. But the metrics that should be tracked must relate to a company's strategic and business plans, Curtis said.

Measurement goals should start at the top of an organization but should be available to everyone in the organization, said Andre Gien, director of strategic consulting in the accounting, tax, and advisory division of CBIZ, an accounting services and consulting firm based in Cleveland.

"Measurements should be around estimated expectations," Gien said. "A lot of emphasis is placed on top-line measures for the board and C-level executives. However, the tools available to the actual field members are not as effective as those available to the board. The secret is getting the metrics right upfront. It's not an exact science, so there has to be a degree of experimentation, but most organizations don't want to go through that phase."

Avoiding sandbagging

Applix, Inc. is among companies that offer business intelligence and business performance management systems, but the company's Michael Morrison echoes the need for realistic baseline measurements before any goals can be set.

"You can't tie compensation to targets unless you establish a baseline to avoid sandbagging," said Morrison, senior vice president of worldwide field and marketing operations for the Westborough, Mass. company. "You need one round of reporting, at least, to define the metric before you start setting targets. You also need to give the people being measured access to the same information that you're using."

The speed at which metrics can be compiled also cannot be overlooked, Morrison said. In a retail environment, for example, tracking sales of a particular product means nothing if inventory gets depleted during a crucial sales period. A better measure is whether sufficient inventory is available at that crucial time.

"Financial performance is a lagging indicator," said Gien. "Companies need to focus on leading indicators such as target customers, product development, business systems and efficiency



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of delivery—those things I call your intangible assets that, ultimately, affect your ability to compete.”

Removing uncertainty

While financial targets certainly have merit, non-financial ones are equally important to the overall health of an organization, said Morrison, indicating the balanced scorecard approach to a management system. The balanced scorecard measures a company's vision and strategy among four interrelated processes: financial goals related to shareholders, customer-focused goals, an organization's internal business processes, and its ability to learn and grow.

“Markets don't like uncertainty. The more you can remove the uncertainty, the better off you are,” Morrison said. “Organizations that understand the various elements of their operation can communicate that more effectively to the investment community. Non-financial metrics such as higher customer satisfaction can be measured and correlated to financial data to show cause and effect.”

Gien agrees that non-financial measures are just as important as financial ones in gauging the overall health of a company. If one of a company's key measures is customer service, for example, factors that come into play include employee satisfaction, product quality, time of delivery, employees, and others, Gien said. “There's a mapping process that needs to be done with a cause-and-effect linkage, and then a determination can be made about how to measure it.”

Getting to the heart of the matter, Gien believes that the most successful companies create a

culture of learning where metrics are embraced to gauge a company's performance. But that's not easy, either. “Seldom does a CEO ask what he can do to create a learning organization,” Gien said. “Being a learning organization is different for every organization and depends on culture.” What works well at one company won't necessarily work at another, so the solution will be unique to each organization.

Curtis uses a Z-score with his clients to gauge the overall health of a company. Developed by Edward Altman in the 1960s, the score combines the ratios of working capital/total assets/retained earnings, EBIT/total assets, and net worth/total liabilities. A composite score above 2.6 indicates a healthy company, while a score below 1.1 indicates a bankruptcy risk. Using this measure periodically over a period of time will give management a sense of the company's overall direction.

“If you are measuring simply because you like to measure, chances are you aren't getting to the core of what you're trying to achieve,” Curtis said. He advises top management to articulate big picture issues in the operating plan, give managers clear direction and support on how to achieve success, and then look for the proper metrics to gauge performance.

Gien said that managers are extremely good at problem solving. What they aren't good at, however, is defining the problem in the first place. “That dissemination should be the function of a performance management system,” Gien said. “That's when it becomes truly powerful to change an organization's ability to compete.”

But he's quick to link any performance management system to the overall goal of creating a learning organization. “A performance management system isn't something to be ticked off a list,” Gien said.

“The real test should be whether it helps me make better decisions and whether it helps me make them through the whole organization. The trick is better decisions at every level of the organization.” ■

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