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The New Thinking on KPIs - Revisited

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The following article is an extract from [Key Performance Indicators: Developing, Implementing, and Using Winning KPIs](#).

"Show me a company who thinks they have KPIs, which are measured monthly and quarterly, and I will show you measures that do not create change, alignment and growth and have never been KPIs" - David Parmenter

From my research shows that very few organizations really monitor their true key performance indicators (KPIs). The reason is very few organizations, business leaders, writers, corporate accountants and consultants have explored what a KPI actually is. This brief paper will hopefully help you unearth what a KPI is and point where to look for them in your organization.

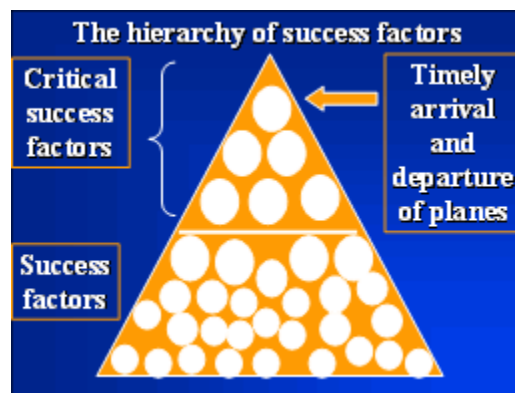
Let me explain what a KPI is through two KPI stories.

An airline

My favourite KPI story is about Lord King, who set about turning British Airways (BA) around in the 1980s by reportedly concentrating on one KPI.

Lord King appointed some consultants to investigate and report on the key measures he should concentrate on to turn around the ailing airline. They came back and told Lord King that he needed to focus on one critical success factor (CSF): the timely arrival and departure of airplanes. (See Exhibit 1) Lord King was not impressed as everybody in the industry knows the importance of timely planes. They pointed out to Lord King that British Airways knew it was a success factor, along with 30 to 40 other success factors. The difference was that they were informing BA that it was the most important success factor. The consultants then pointed out that this is where the KPIs lay and they proposed that Lord King focus on late plane measures.

Exhibit 1: The importance of knowing your critical success factors



He was notified, wherever he was in the world, if a BA plane was delayed over a certain time, say two hours. The BA airport manager at the relevant airport knew that if a plane was delayed beyond a certain "threshold", they would receive a personal call from Lord King. It was not long before BA planes had a reputation for leaving on time.

The late planes KPI was linked to most of the critical success factors for the airline. It linked to the "delivery in full and on time" CSF namely the "timely arrival and departure of aeroplanes", and it linked to the "increase repeat business" CSF etc. The importance the CSF "timely arrival and departure of aeroplanes" can be seen by its impact on all the six perspectives of a modified balanced scorecard. (See Exhibit 2)

I have added 'employee satisfaction' and 'environment & community' to the traditional four perspectives. These two perspectives were underestimated in the original work of Robert Kaplan and David Norton. Having a separate employee satisfaction perspective emphasizes the importance of measuring the key drivers of employee satisfaction such as the amount and regularity of recognition (e.g., how many recognition events are planned for the next week/fortnight, how much recognition has been made this week, the past two weeks, and this month). It will also support the need for more regular staff satisfaction surveys performed on a rolling sample basis.

The environment/community perspective will help create a major asset for the HR team, assisting the organization in becoming an employer of choice. Long-term successful linkages with the community, both local and national, are extremely valuable. Also, initiatives in this area feed into positive customer perceptions.

Exhibit 2: A balanced scorecard with six perspectives

FINANCIAL	CUSTOMER	ENVIRONMENT/COMMUNITY
Utilization of assets	Seamless service	Supporting local business
Optimization of working capital	Increased customer	Green Globe 21
Focus on top 10% of customers, inc.	Satisfaction, etc.	Community leadership
INTERNAL PROCESS	EMPLOYEE SATISFACTION	LEARNING AND GROWTH
Delivery in full on time	Positive company culture	Empowerment
Effective relationship with key stakeholders	Retention of key staff	Increasing expertise
Optimizing technology	Increase recognition	Adaptability, etc.

Timely arrival and departure of planes affected all six balanced scorecard perspectives. Late planes:

- Increased costs in many ways, including additional airport surcharges and the cost of accommodating passengers overnight as a result of late planes being “curfewed” due to noise restrictions late at night (financial perspective).
- Meant unhappy customers and alienated those people affected by the late arrival of the passengers – possible future customers (customer perspective).
- Created a negative impact in the wider community and thus reduced the potential pool of future employees (community perspective).
- Incurred created wastage of food - hot food has a short serving window and wastage of fuel as planes endeavoured to make up for lost time and operated outside their most economical flight speed (environmental perspective)
- Had a negative impact on staff development as staff would repeat the bad habits that had created late planes (learning and growth perspective).
- Adversely affected supplier relationships and servicing schedules, resulting in poor service quality (internal process perspective).
- Led to employee dissatisfaction as employees had to deal both with frustrated customers and the extra

stress each late plane created (employee satisfaction perspective).

A distribution company

A CEO, of a distribution company, realised that a critical success factor for their business was trucks leaving as close as to capacity as possible. Large truck and trailer units capable of carrying more than 40 tonnes were being sent out with small loads as despatch managers were focusing solely on "deliver in full on time" to customers.

Each day by 9am, the CEO received a report of those trailers that had been sent out under weight. The CEO rang the despatch manager and asked whether any action had taken place to see if the customer could have accepted that delivery on a different date that enable better utilisation of the trucks. In most cases the customer could have received it a day or two earlier or later, fitting in with a past or future truck going in that direction. The impact on profitability was significant.

Just with the airline example, staff some did their utmost to avoid a career-limiting phone call with their CEO.

The characteristics of KPIs

KPIs represent a set of measures focusing on those aspects of organisational performance that are the most critical for the current and future success of an organisation. There are only a few KPIs in an organisation (no more than 10) and they have certain characteristics.

KPI characteristics include:

- Non financial measurement (not expressed in monetary figures)
- Measured frequently e.g. daily or 24/7 (KPIs are not measured monthly)
- Acted upon by the CEO and the senior management team on a daily or 24/7 basis.
- All staff understand the measure and what corrective action is required
- Responsibility that can be tied down to a team
- The KPI has a significant impact on the organisation e.g. it impacts on most of the critical success factors and balanced scorecard perspectives
- Positive movement that affects all other performance measures in a positive way

When you put a Pound or Dollar sign to a measure you have not dug deep enough. Sales made yesterday will be a result of sales calls made previously to existing and prospective customers, advertising, amount of contact with the key customers, product reliability etc. I label any indicator expressed in monetary terms as result indicator, see below for more explanation.

KPIs should be monitored and reported 24/7, daily and a few perhaps weekly. How can a KPI be measured monthly? This surely is "shutting the barn door well after the horse has truly bolted". KPIs are "current" or "future" measures as opposed to "past" measures. When you look at most organisational measures, they are very much past indicators measuring events of the last month or quarter. These indicators cannot be and never were a KPI. That is why a satisfaction percentage (e.g. 65%) from a customer satisfaction survey performed every six months can never be a KPI.

All good KPIs that I have come across, that have made a difference, had the CEO's constant attention, with daily calls to the relevant staff. Having a potentially "career limiting" discussion with the CEO is not something staff want to repeat, and in the airlines case, innovative and productive processes were put in place to prevent a reoccurrence.

A KPI should tell you about what action needs to take place. The British Airways "late plane" KPI communicated immediately to everybody that there needed to be a focus on recovering the lost time. Cleaners, caterers, ground crew, flight attendants, and liaison officers with traffic controllers would all work some magic to save "a minute here and a minute there" whilst maintaining or improving service standards.

A KPI can be tied down to a team. In other words, the CEO can ring the manager and ask "why". Return on capital employed has never been a KPI as it cannot be tied down to a manager, it is a result of many activities under different managers. Can you imagine the reaction if a GM was told one morning by the CEO "Pat, I want you to increase the return on capital employed today".

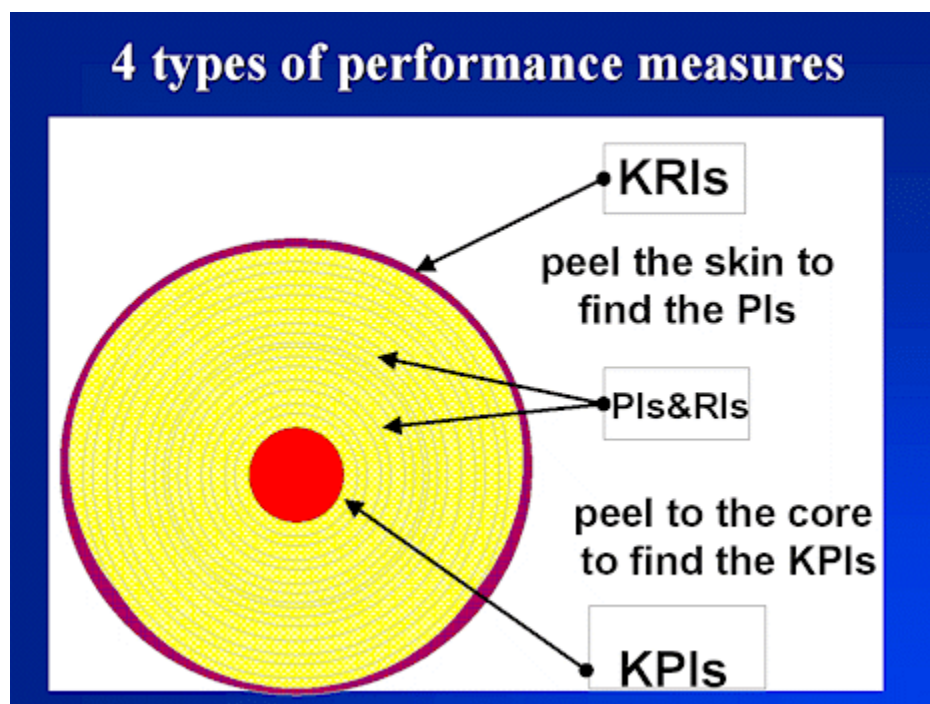
A KPI will affect more than one critical success factor and most of the balanced scorecard perspectives. In other words, when the CEO focuses on the KPI, and the staff follows, the organisation scores goals in all directions.

A KPI has a flow on effect on other performance measures. Reducing late planes would improve performance measures around improved service by ground staff as there is less "fire fighting" to distract them from a quality and caring customer contact.

The four types of performance measures

From the research I have performed, from workshop feedback across diverse industries and as a byproduct of writing my book *Key Performance Indicators: Developing, Implementing and Using Winning KPIs* (Wiley, 2007), I have come to the conclusion that there are four types of performance measures:

Exhibit 3: A Scorecard with 6 perspectives



- **Key result indicators (KRIs)** give an overview on past performance and are ideal for the board as they communicate how management has done in a critical success factor or from a balanced scorecard perspective.
- **Performance indicators (PIs)** tell staff and management what to do.
- **Result indicators (RIs)** tell staff what they have done.
- **Key performance indicators (KPIs)** tell staff and management what to do to increase performance dramatically.

I use an onion analogy to describe the relationship of these four measures. The outside skin describes the overall condition of the onion, how much sun, water and nutrients it has received, how it has been handled from harvest to

supermarket shelf. The outside skin is thus a key result indicator. The layers represent the various performance and result indicators and the core is where you find the key performance indicators.

Another way to look at it is to say there are two groups of measures, result indicators that summarise activities and performance indicators that are tied to a precise activity.

The 10/80/10 rule

Kaplan and Norton recommend no more than 20 KPIs, and Jeremy Hope (of beyond budgeting fame) suggest less than 10. To aid those involve in performance measurement I have developed the 10/80/10 rule. This means an organisation should have about 10 KRIs, up to 80 PIs and RIs and 10 KPIs. Very seldom is there a need for more measures than these numbers, and in many cases, less measures can be used.

Key Result Indicators (KRIs)

The common characteristic of KRIs is that they are the result of many actions. They give a clear picture of whether you are travelling in the right direction, and of the progress made towards achieving desired outcomes and strategies. They are ideal for governance reporting as key result indicators show overall performance and help the Board focus on strategic rather than management issues.

KRIs do not, however, tell management and staff what they need to do to achieve desired outcomes. Only performance indicators and KPIs can do this.

KRIs are measures that have often been mistaken for KPIs include:

- Customer satisfaction
- Net profit before tax
- Profitability of customers
- Employee satisfaction
- Return on capital employed

Separating out KRIs from other measures has a profound impact the way performance is reported. There is now a separation of performance measures into those impacting governance (up to ten KRIs in a Board dashboard) and those RIs, PIs and KPIs impacting management.

A one page dashboard with the KRIs going in the right direction, will give confidence to the Board that the management know what they are doing and the "ship" is being steered in the right direction. The Board can then concentrate on what they do best, coaching the CEO, as required; focusing on the horizon for icebergs or looking for new ports to call. This is instead of parking themselves on the "bridge" and thus getting in the way of the captain who is trying to perform important day-to-day duties.

Performance and Result Indicators (PIs and RIs)

The 80 or so performance measures that lie between the KRIs and the KPIs are the performance and result indicators (PIs). The performance indicators while important are not "Key to the business". The PIs help teams to align themselves with their organisation's strategy. PIs complement the KPIs and are shown with them on the organisation's, divisions', departments' and teams' scorecards.

PIs could include:

- Percent increase in sales to the top 10% of customers
- Number of employees' suggestions implemented in last 30 days
- Customer complaints from key customers

- Sales calls organized for the next one to two weeks
- Late deliveries to key customers

RIs could include:

- Net profit on key product lines
- Sales made yesterday
- Weeks sales to key customers
- Debtor collections in week
- Bed utilization in week

Looking at the difference between KRIs vs KPIs and RIs vs PIs

Often in workshops one question emerges time and time again. "Please explain again the difference between KRIs and KPIs, and RIs and PIs. Exhibits 4 and 5 will hopefully clarify the differences.

Exhibit 4: The difference between KRIs and KPIs

KRIs	KPIs
Can be financial and non financial, e.g. Return on capital employed, and customer satisfaction percentage	Non financial measures (not expressed in \$s, Yen, Pds Euro etc)
Measures mainly monthly and some times quarterly	Measured frequently e.g. daily or 24 by 7
As a summarise of progress in an organisation's critical success factor it is ideal to a Board.	Acted upon by the CEO and senior management team
It does not help staff or management as no where does it tell what you need to fix	All staff understand the measure and what corrective action is required
Commonly, the only person responsible for a KRI is the CEO.	Responsibility can be tied down to the individual or team
A KRI is designed to summarise activity within one CSF	Significant impact e.g. it impacts on more than one of top CSFs and more than one balanced scorecard perspective
A KRI is a result of many activities managed through a variety of performance measures	Has a positive impact e.g. affects all other performance measures in a positive way
Normally reported by way of a trend graph covering at least the last fifteen moths of activity	Normally reported by way of an intranet screen indicating activity, person responsible, track record etc so a phone call can be made.

A cars speedometer provides a useful analogy to show the difference between a result indicator and a performance indicator. The speed the car is travelling is a result indicator since the cars speed is a combination of what gear the car is in and what revolutions the engine is doing. Performance indicators might be how economically the car is being driven e.g. a gauge showing how many kilometres per litre, or how hot the engine is running e.g. a temperature gauge.

Exhibit 5: The difference between RIs and PIs

RIs	PIs
Can be financial and non financial	Non financial measures (not expressed in \$s)
Measured weekly, fortnightly, monthly, some times quarterly	Same
Cannot be tied to a team or a discrete activity	Tied to a discrete activity, and thus to a team
Does not tell you what you need to do more or less of	All staff understand what action is required to improve PI
Designed to summarise some activity within a CSFs/SFs	Specific activity impacts on one of the CSFs /SFs

A result of more than one activity	Focuses on a specific activity
Normally reported in a team scorecard	Same

To fully understand the differences you will need to listen to the accompanying webcast on www.bettermanagement.com.

Removing the lead/lag confusion

Many management books talk about "lead and lag indicators" which I believe merely clouds the KPI debate. Using this new way of looking at KPIs we dispense with the terms lag (outcome) and lead (performance driver) indicators. I have presented to nearly two thousand people on KPIs and I always ask "is the late planes in the air KPI, a lead or lag indicator?" The vote count is always evenly split. Surely, this is enough proof that lead and lag labels are not a useful way of defining measures.

Key result indicators replace outcome measures, which typically look at activity over months or quarters. PIs, and KPIs are now characterised as either past, current or future measures. The new concept called "current measures" are those monitored 24/7 or daily. You will find the real KPIs in your organisation are either "current" or "future" measures.

Past measures (last week / fortnight / month / quarter)	Current measures (24/7 and daily)	Future measures (next day / week / month / quarter)
e.g. number of late planes last week/ last month	e.g. planes over 2 hours late (updated continuously)	e.g. number of initiatives to be commenced in the next month / two months to target areas which are causing late planes.

The lead lag division did not focus adequately enough on the timing of the measures. Most organisations who want to create alignment and change behaviour need to be monitoring what corrective action is to take place in the future. In other words if quality improvements are to happen we need to measure the number of initiatives which are about to come online in the next week, fortnight, month. If we want to increase sales it is important to know what meetings have already been organised/scheduled with our key customers in the next week, fortnight, month.

Finding the critical success factors

Most organizations know their success factors, however few organizations have:

- worded their success factors appropriately
- segregated out success factors from their strategic objectives
- sifted through the success factors to find their critical ones - their critical success factors
- communicated the critical success factors to staff

Finding the success factors and narrowing them down to no more than five to eight CSFs is a vital step in any KPI exercise. If your organization has not completed a thorough exercise to know its critical success factors (CSFs) performance measurement will be a random process creating an army of measurers producing numerous numbing reports, and who often "measure" progress in a direction very remote from the strategic direction of the organization. To understand the significance of what I am saying please listen to my critical success factors webcast on www.bettermanagement.com.

Next steps

- Listen to the [KPI webcasts](#) I have recorded on BetterManagement.com
- Acquire my KPI starter kit, available on www.davidparmenter.com
- Engage an in-house or external public relations expert to help sell the concept

- Deliver a PowerPoint presentation to the SMT to get buy-in for your KPI/BSC project
- Start the exercise to list all the success factors and then sort which ones are critical - the CSFs
- Link with an external expert who can contribute to brainstorming sessions designed to ascertain the CSFs for your organization.

Writer's biography



David Parmenter is an international presenter who is known for his thought provoking and lively sessions, which have led to substantial change in many organisations. David is a leading expert in: the development of winning KPIs, replacing the annual planning process with quarterly rolling planning, quick month-end processes and converting reporting to a decision based tool.

His work on KPIs has received international recognition. He has speaking engagements as far a field as Auckland, Wellington, Sydney, Melbourne, Brisbane, Adelaide, Canberra, Perth, Kuala Lumpur, Singapore, Tehran, Prague, Dublin, London, Birmingham, Manchester and Edinburgh. John Wiley & Sons Inc have published his first two books "Key Performance Indicators -

developing, implementing and using winning KPIs" and "Pareto's 80/20 rule for corporate accountants".

David has also worked for Ernst & Young, BP Oil Ltd, Arthur Andersen, and Price Waterhouse. David is a fellow of the Institute of Chartered Accountants in England & Wales.

He has written over 30 articles for the accounting and management Journals including "Quarterly rolling planning - removing the barriers to success", "Throw away the annual budget", "Beware corporate mergers", "Implementing a Balanced Scorecard in 16 weeks not 16 months", "Convert your monthly reporting to a management tool", "Smash through the performance barrier", "Is your board reporting process out of control?" "Implementing winning Key Performance Indicators", "Quick month end reporting" etc.

He can be contacted at parmenter@waymark.co.nz or telephone +64 4 499 0007. He has recently completed a series of white papers which can be purchased from his website <http://www.waymark.co.nz>. His recent thinking is accessible from www.davidparmenter.com