How to Implement Winning KPIs

By David Parmenter

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1 The great KPI misunderstanding

"Show me a company with over 20 KPIs and I will show you a lack of focus, a lack of alignment and under achievement"

For years organisations that have had, what they thought were, KPIs. They have not had the focus, adaptability, innovation and profitability that they were seeking. KPIs themselves were mislabelled and misused. Some organisations try and manage with over forty KPIs, many of which are not KPIs.

I have developed a hypothesis that performance measures are divided into four types (**key result indicators**, **result indicators**, **performance indicators and key performance indicators**).

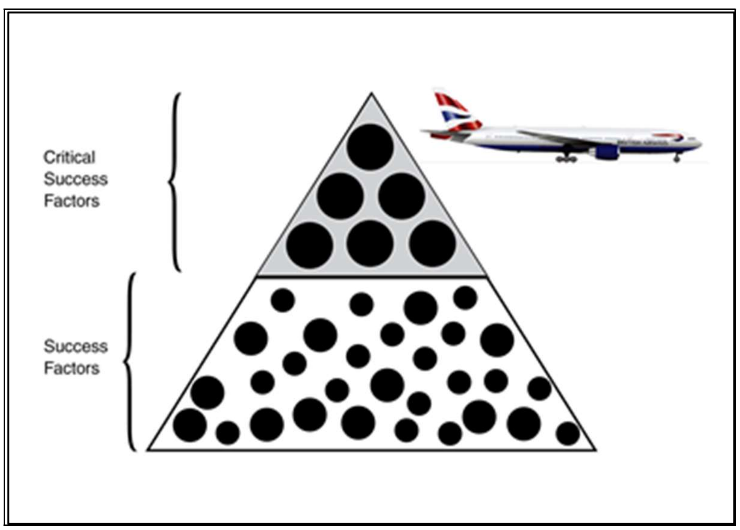
Let me explain what a KPI is through two KPI stories.

1.1 An airline's KPI story

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 turnaround 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 aeroplanes, see Exhibit 1.1. Finding the CSFs and narrowing them down to no more than five to eight is a vital step in any KPI exercise, and one seldom performed.

Exhibit 1.1 The importance of knowing your critical success factors



Lord King was however not impressed as everybody in the industry knows the importance of timely planes. However, the consultants then pointed out that this is where the KPIs lay and they proposed that Lord King focus on late plane KPI.

He was notified, wherever he was in the world, if a BA plane was delayed over a certain time. 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. I imagine the conversation going like this.

"Pat, Its Lord King on the phone, I am ringing up about BA135 that left Kennedy airport over two and a quarter hour late, what happened?"

"Lord King, the system will tell you that the plane was late leaving Hawaii. In fact, it was one and three quarters hours late and everything was in order at our end except we lost an elderly passenger in duty free shopping. We had to offload their bags and as you can see we did it in record time, only half an hour!"

"Pat, how long have you worked for British Airways?"

Pat, realising this conversation was not going well responded, "About thirty years, Lord King"

"In fact, Pat it is thirty-two. With all that experience with us you are telling me that with six hours of advance notice that the plane was already late you, and your team, could do nothing to bring it forward, instead you added half an hour. Quite frankly Pat, I am disappointed as you and your team are better than this!"

For Pat and many others employed by the airline had the "not invented by us" syndrome. A late plane created by another team was their problem not ours. With Pat's new attitude and awareness, the troops were gathered the next day and undertook many proactive steps to ensure they recaptured the lost time, no matter who had created the problem. Actions such as:

- doubling up the cleaning crew, even though there was an additional external cost to this,
- communicating to the refuelling team which planes were a priority
- superior communication to the external caterers so they could improve management re-equipping the late plane
- staff on the check-in counters asked to watch out for at risk customers and chaperone them to the gate.
- not allowing the business class passenger to check-in late, yet again. This time saying "Sorry Mr Carruthers we will need to reschedule you as you are too late to risk your bags missing this plane. It is on a tight schedule. I am sure you are aware that the deadline for boarding passed over 30 minutes ago."

The BA 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 worked as it was linked to most of the critical success factors for the airline. It linked to the 'delivery in full and on time' critical success factor namely the 'timely arrival and departure of aeroplanes'; it linked to the 'increase repeat business from key customers' critical success factor etc.

The late planes in the air KPI affected many aspects of the business. Late planes:

1. Increased cost in many ways, including additional airport surcharges and the cost of accommodating passengers overnight as a result of planes being prevented from departing due to noise restrictions late at night.
2. Increased customer dissatisfaction leading to passengers trying other airlines and changing over to their loyalty programmes.
3. Alienated potential future customers as those relatives, friends or work colleagues inconvenienced by the late arrival of the passenger avoided future flights with the airline.
4. Had a negative impact on staff development as they learned to replicate the bad habits that created late planes.

5. Adversely affected supplier relationships and servicing schedules, resulting in poor service quality.
6. Increased employee dissatisfaction, as they were constantly firefighting and dealing with frustrated customers.

It is interesting that Ryanair has a sole focus on timeliness of planes. They know that is where they make money often getting an extra European flight each day out of a plane due to their swift turnaround and their uncompromising stand against late check-in. They simply do not allow customers to get in the way of their tight schedules.

1.2 A freight company's KPI story

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. A large train truck, capable of carrying more than 40 tonnes, was being sent out with small loads as despatch managers were focusing 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 would enable better utilisation of the trucks. In most cases the customer could have received it earlier or later, fitting in with a past or future truck going in that direction. The impact on profitability was significant.

In a scenario, similar to the airline example, staff members did their utmost to avoid a career-limiting phone call from the CEO.

(Both these examples are provided in greater detail in my webcast, "Introduction to Winning KPIs," which can be accessed via www.davidparmenter.com.)

1.3 Waymark research

In international polls, see Exhibit 1.2, waymark conducted during a webcast resulted with the following.

Exhibit 1.2: International Poll (web presentations)

How many KPIs are there in your organisation?	What is the most common timeframe KPIs are reported within?
72% less than 20	9% 24/7
16% between 20-50	22% daily
3% between 51-100	14% weekly
2% over 100	55% monthly
Population: 467 respondents	Population: 121 respondents

Clearly there is a move to fewer measures with just over 70% with under 20 KPIs and the reporting period is still very historic with nearly 70% saying monthly or quarterly.

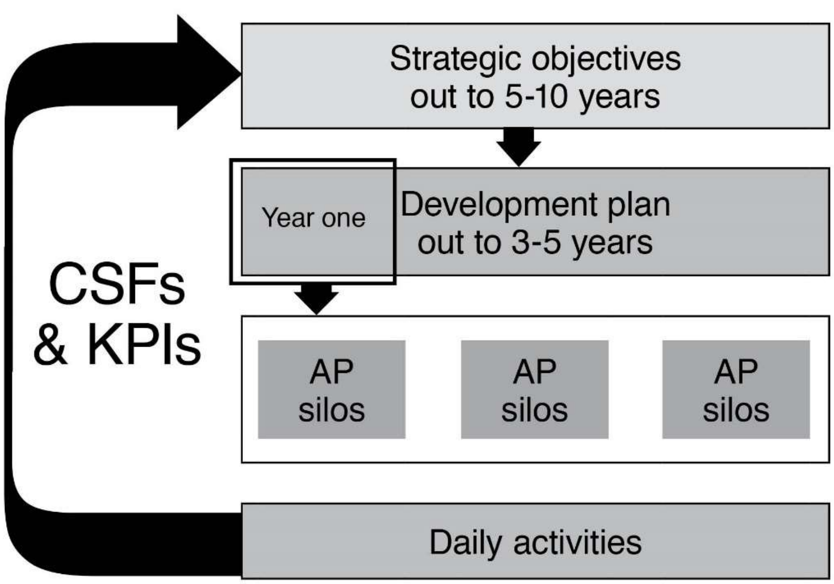
1.4 Role of performance measures

It is worth reflecting on what the role of performance measures are intended to be. It is my belief that the role of performance measures includes:

- linking daily actions to the strategies, as shown in Exhibit 1.3
- giving an organisation direction
- ensuring a more balanced performance
- creating wider ownership and empowerment
- gaining behavioural alignment (as the late planes KPI clearly did)

It is also my belief that KPIs are the only thing that truly links day to day performance in the work place to the organisation's strategic objectives. Some people think that because the annual planning process comes from a medium-term view (called the development plan in Exhibit 1.3), which in turn is linked to the strategic plan, Strategy is linked to day to day activities. It looks good on paper but never works in practice. Strategy is broad and wide ranging whereas the annual planning process is a dysfunctional silo-based process!

Exhibit 1.3: Linkage of KPIs to strategic objectives



2 Critical success factors are the origin of performance measures

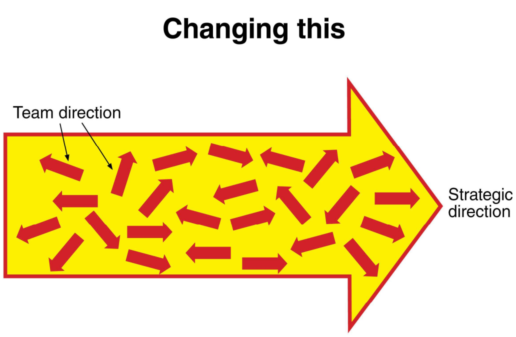
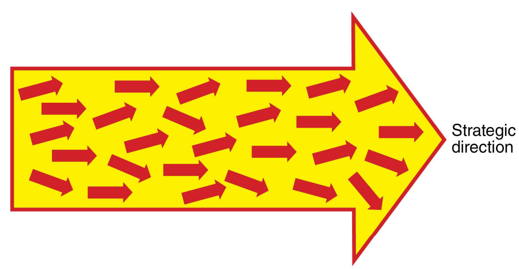
I was first introduced to critical success factors (CSFs) by the talented people who wrote the KPI manual for AusIndustry (an Australian government department). They defined critical success factors as the

"List of issues or aspects of organisational performance that determine ongoing health, vitality, and well-being."

I have always seen these as operational issues or aspects that need to be done well day-in day-out by the staff in the organisation. They are about what the staff inside the organisation can do and should do to get alignment to the strategic direction.

It is the CSFs, and the performance measures within them, that link daily activities to the organisation's strategies. This alignment, as shown in Exhibit 2.1, is I believe the El Dorado of management.

Exhibit 2.1: Getting alignment to the strategic direction through the CSFs and KPIs

Status quo, a lack of alignment	Alignment through CSFs and winning KPIs
	

2.1 Characteristics of critical success factors (CSFs)

There are a number of characteristics of CSFs that are worth dwelling on. Critical success factors:

- Are worded so a 14-year-old could understand them and realize what is important to the organisation.
- Will be no surprise to management and the board/government official, as they will have talked about them as success factors.
- Apply to more than one balanced-scorecard perspective (e.g., "Innovation is a daily activity" impacts nearly all the balanced-scorecard perspectives).
- Are focused on the organisation and thus should not be broken down into department CSFs.
- Are few in number; five to eight is sufficient.
- Have a great influence on other success factors.

- Are focused in a precise area, rather than being the broad statements that are commonly called strategic objectives.

The traditional balanced-scorecard (BSC) approach uses performance measures to monitor the implementation of the strategic initiatives, and measures are typically cascaded down from a top-level organisational measure such as return on capital employed. This cascading of measures from one another will often lead to chaos, with hundreds of measures being monitored by staff in some form of BSC reporting application.

Getting staff to focus every day on the organisation's operational CSFs is, I believe, the El Dorado of management. Thus, instead of using the strategies as the source of your measures, clarify what your organisation's operational CSFs are and then determine what measures would enforce alignment to these Operational CSFs. You will find that your operational CSFs will create the vital linkage between daily activities and the organisation's strategies.

Operational CSFs are the origin of the performance measures that really matter, the KPIs. It is the operational CSFs, and the performance measures within them, that link daily activities to the organisation's strategies. The operational CSFs impact the business all the time, 24/7, and it is therefore important to measure how the staff in the organisation are aligning their daily activities to these operational CSFs.

Most organisations know their success factors; however, few organisations have:

- Worded their success factors appropriately.
- Segregated success factors from their strategic objectives.
- Sifted through the success factors to find their critical ones—their operational CSFs.
- Communicated the operational CSFs to staff.

If your organisation has not completed a thorough exercise to know its operational CSFs, performance management cannot possibly function. Performance measurement, monitoring, and reporting will be a series of random processes, creating an army of measurers producing numerous numbing reports, full of measures that monitor progress in a direction very remote from the strategic direction of the organisation. Very few, if any, of the measures in these reports could be defined as "winning KPIs" as they have been derived independently from the operational CSFs.

2.2 The benefits of understanding your organisation's CSFs

Knowing, communicating and measuring progress in an organisation's CSFs is the El Dorado of management, the 'Holy Grail'. There are some profound benefits of knowing your CSFs including:

Leads to the KPIs	It leads to the discovery of an organisations 'winning KPIs'
Helps eliminate measures	Performance measures that **do not** relate to your CSFs, or impact them cannot, by definition be important and thus can often be eliminated
Linked daily actions	Staff know what should be done as a priority and thus their daily actions are now linked to the organisation's strategies e.g., like they do at Toyota
Challenge unnecessary meetings	Staff meetings, reports and tasks will be challenged for their validity. All activities that have no direct link to the critical success factors will be seen as non-critical. Over time meetings and reports that occurred because we did it last week/month will disappear.
Leaner reports	Report layout will be more concise as many extraneous issues will be removed.
More CEO walkabout	The CEO's linkage to the workface will be a daily activity through the phone calls and walkabouts amongst front line staff.

I will explain the importance of critical success factors on the emergence of KPIs through two stories.

3 The characteristics of KPIs

Key Performance Indicators represent a set of measures focusing on those aspects of organisational performance that are the most critical for the current and future success of the organisation. KPIs are rarely new to the organisation. Either they have not been recognized or they were gathering dust somewhere unknown to the current management team.

I believe KPIs have certain characteristics, and I have developed a seven-point checklist, see Exhibit 3.1

Exhibit 3.1: Characteristics of KPIs

1. Nonfinancial	Nonfinancial measures (not expressed in dollars, yen, pounds, euro etc.).
2. Timely	Measured frequently e.g. 24 by 7, daily or weekly.
3. CEO focus	Acted on by the CEO and senior management team.
4. Simple	All staff understand the measure and what corrective action is required.
5. Team based	Responsibility can be tied down to a team or a cluster of teams who work closely together.
6. Significant impact	Major impact on the organisation e.g. it impacts more than one of the CSFs and more than one balanced scorecard perspective.
7. Limited dark side	They encourage appropriate action (e.g., have been tested to ensure they have a positive impact on performance, whereas poorly thought through measures can lead to dysfunctional behaviour).

Non-Financial: 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 term any sales indicators expressed in monetary terms as result indicators, which will be further explained in this paper. In many organisations a KPI may rest with certain activities undertaken with your key customers who often generate most, if not all, of your profit.

Timely: KPIs should be monitored and reported 24/7, daily and a few perhaps weekly. How can a KPI be measured monthly, as this 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.

CEO focus: 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.

Simple: 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.

Team based: A KPI should be deep enough within an organisation so that it can be tied down to a team or a cluster of teams who work closely together. In other words, the CEO can ring a 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."

Significant impact: 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.

Limited dark side: Before becoming a KPI a performance measure needs to be tested to ensure it creates the desired behavioural outcome e.g., helping teams to align their behaviour in a coherent way to the benefit of the organisation. This has been discussed in section 4.

For the private sector, *key performance indicators*, that fit the characteristics I have proposed, could include:

- Number of CEO recognitions planned for next week or two weeks.
- Staff in vital positions who have handed in their notice on a given day. (The CEO has the opportunity to try to persuade the staff member to stay).
- Late deliveries to key customers.
- Key position job offers issued to candidates that are more than 48 hours outstanding (The CEO has the opportunity to try to persuade acceptance of offer).
- List of late projects, by manager, reported weekly to the senior management team.
- Number of vacant leadership positions at in-house course (reported daily to the CEO in the last three weeks before the course is due to run).
- Number of initiatives implemented after the staff-satisfaction survey (monitored weekly for up to three months after survey).
- List of level 1 & 2 managers who do not have mentors, reported weekly to the CEO. This measure would only need to be operational for a short time on a weekly basis.
- Number of innovations planned for implementation in next (30, 60, 90 days). Reported weekly to the CEO
- Number of abandonments to be made in next (30, 60, 90 days). Reported weekly to the CEO
- Major projects awaiting decisions that are now running behind schedule (report weekly to CEO)
- Complaints from our key customers that have not been resolved within 2 hours (report 24/7 to CEO and GMs)

- Key customer enquiries that have not been responded to by the sales team for over 24 hours (report daily to the GM)
- Date of next visit to major customers by customer name (report weekly to CEO and GMs)

For government and non-profit agencies, *key performance indicators* could also include:

- Emergency response time over a given duration (reported immediately to the CEO).
- Number of confirmed volunteers to be street collectors for the annual street appeal (monitored daily in the four to six weeks before the appeal day).
- Date of next new service initiative

4 Performance measures fit into two groups

From the research, I have performed which I have accumulated through workshop feedback across diverse industries and, as a by-product of writing my book, "Key Performance Indicators – developing, implementing and using winning KPIs", I have come to the conclusion that there are four types of performance measures in **two groups of two**, see Exhibit 4.1.

Exhibit 4.1 Two groups of two

Result Indicators	Measures that summarize the collective effort of a wide number of teams. Some of these result indicators summarize the collective efforts of all the teams. I call these **Key Result Indicators**.
Performance Indicators	Measures where the responsibility can be tied down to a team or a cluster of teams who work closely together. Some of these performance indicators tell staff and management what to do to increase performance dramatically. I call these **Key Performance Indicators**.

There are measures that summarise the collective effort of a wide number of teams. I call these Result indicators. Some of these result indicators summarise the collective efforts of all the teams and I call these **Key Result Indicators**.

There are measures where the responsibility can be tied down to a team or a cluster of teams who work closely together. I call these **Performance indicators**. Some of these performance indicators tell staff and management what to do to increase performance dramatically, and I call these **Key Performance Indicators**.

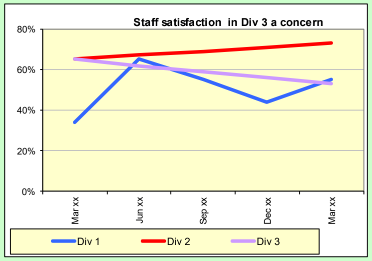
4.1 Key result indicators

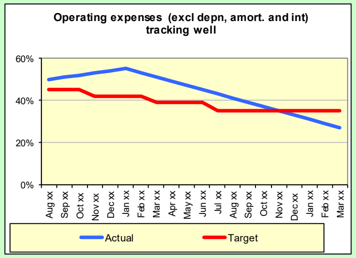
The common characteristic of key result indicators (KRIs) is that they are the result of many actions. They give a clear picture of whether you are travelling in the right direction, and of the progress made towards achieving desired outcomes and strategies. They are ideal for governance reporting as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

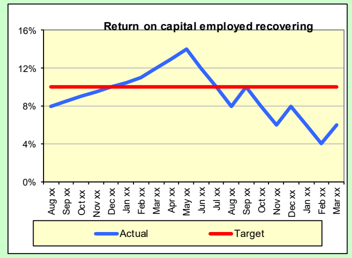
KRIs do not tell management and staff what they need to do to achieve desired outcomes. Only performance indicators and KPIs can do this. For a list of KRIs see Exhibit 4.2.

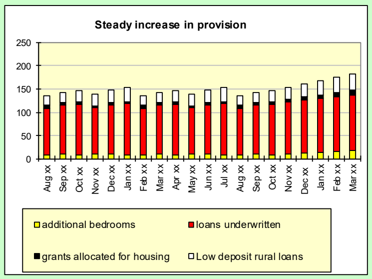
Exhibit 17.9 An A3 page (Ledger size USA) Board Dashboard

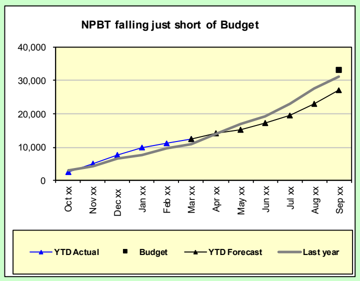
Dashboard for Board - March 20___

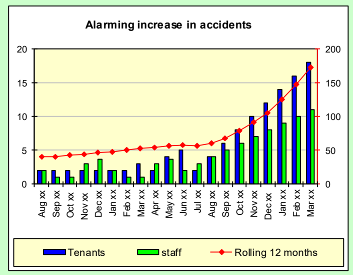


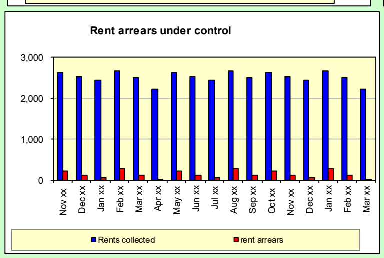


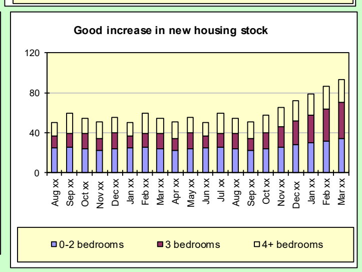


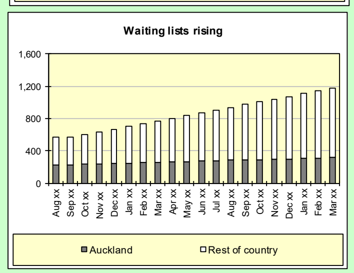












Areas of concern

- The expected shortfall at year-end is largely a result of the electrical consumer division and the __________ division.
- ____ ____
- ____ ____

Areas to Note

- The electrical consumer division decline is of concern. A special strategy meeting is being held on xx June to investigate new revenue avenues to help weather this storm.
- ____ ____
- ____ ____

Financial Performance for the __ months ended ______ 20__

All figures are $Ms	YTD Actual	YTD Budget	Variance[1]	Forecast	Full Year Plan	Variance
Revenue						
________	55.2	60.1	(4.9)	73.6	85.9	(12.3)
________	42.1	41.7	0.4	56.1	59.6	(3.4)
Total Revenue	**97.3**	**101.8**	**(4.5)**	**129.7**	**145.4**	**(15.7)**
Expenses						
Personnel	50.2	53.4	3.2	66.9	76.3	9.4
Accommadation costs	28.1	26.0	(2.1)	35.6		
Telecommunication costs	10.2	11.5	1.3	14.7	16.4	1.7
________	4.5	3.0	(1.5)	5.0		(5.0)
________	5.1	5.3	0.2	6.8	7.6	0.8
Total	**98.1**	**99.2**	**1.1**	**11.8**	**7.6**	**6.9**
Surplus/(deficit)	**(0.8)**	**2.6**	**(3.4)**	**117.9**	**137.9**	**(8.8)**

1. Positive numbers represent under expenditure or additional revenue
2. xx.xx% of the year has been completed.

Statement of Financial Position

All figures are $Ms

	As at ____	Previous month	Movement
SHAREHOLDERS' FUNDS	**25.5**	**25.0**	**0.5**
Represented by:			
Bank and Cash	6.3	9.5	(3.2)
Debtors	5.3	5.5	(0.2)
Total Current Assets	**11.6**	**15.0**	**(3.4)**
Property and equipment	16.2	18.1	(1.9)
Intangible assets	22.6	18.2	4.4
Total LT Assets	**38.8**	**36.3**	**2.5**
Total Assets	**50.4**	**51.3**	**(0.9)**
Creditors and payables	9.1	9.5	(0.4)
Unearned income	5.3	6.1	(0.8)
Employee entitlements	6.3	6.5	(0.2)
Total Current Liabilities	**20.7**	**22.1**	**(1.4)**
Non Current Liabilities	4.2	4.2	-
Total Liabilities	**24.9**	**26.3**	**(1.4)**
NET ASSETS	**25.5**	**25.0**	**0.5**

1. Working capital ratio: __:1

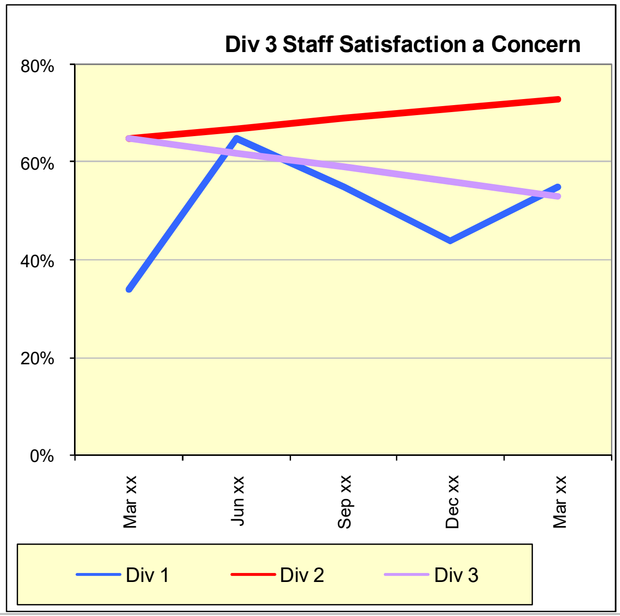
Areas to Note

Debtors have benefited from the work done to reduce outstanding debt.
The amount which is overdue more than 30 days is now $5.0m down from $5.5m
- ____ ____
- ____ ____

Exhibit 17.10 Examples of key result indicators for a Board dashboard

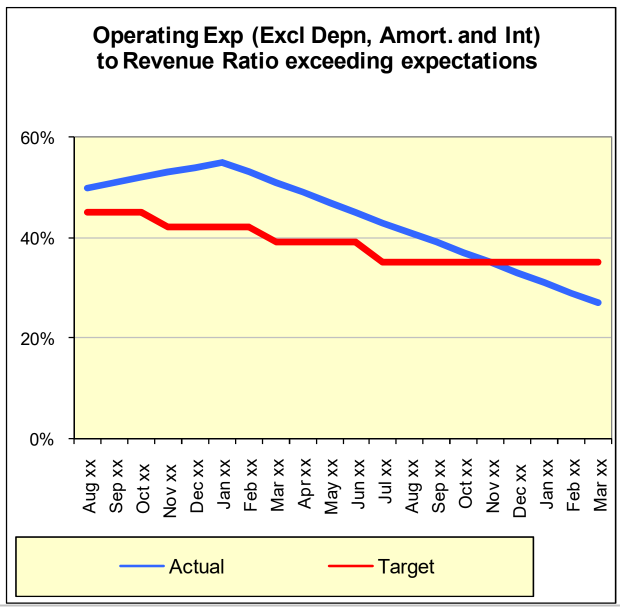
Staff satisfaction:

No different or less important than customers. As one person said, happy staff make happy customers which make happy shareholders. If you believe in this connection, run a survey now! A staff satisfaction survey need not cost the earth and should never be done covering all staff, instead it should be replaced by a rolling survey.



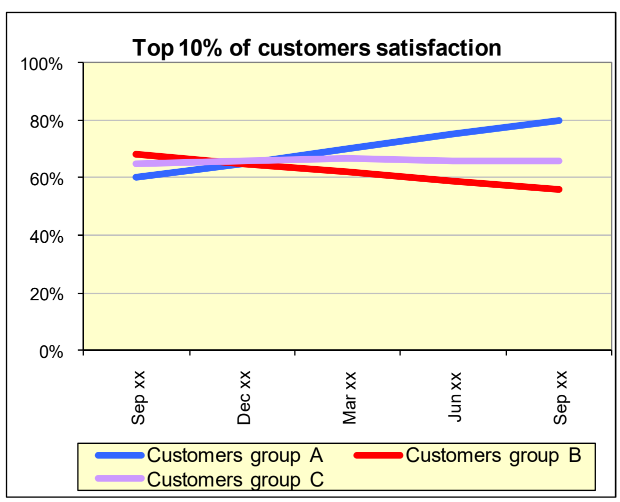
Expenses as a ratio to revenue:

The Board should be interested in how effective the organisation has been in utilising technology and continuous improvement to ensure cost of operations is tracking well against revenue.



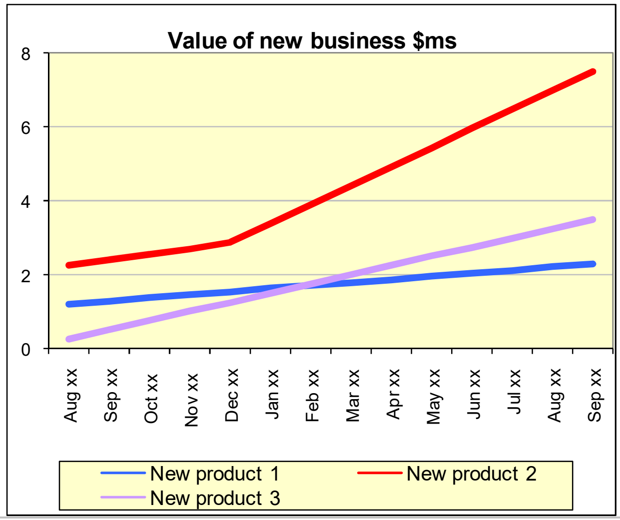
Customer satisfaction:

This needs to be measured at worst every three months. By using statistical samples and focusing on your top 10-20% of customers (the ones that are generating most if not all of you bottom-line). This process does not need to be overly expensive. Those who think once a year is adequate for customer satisfaction should stick to running a sports club as they are not safe in the public or private sectors.



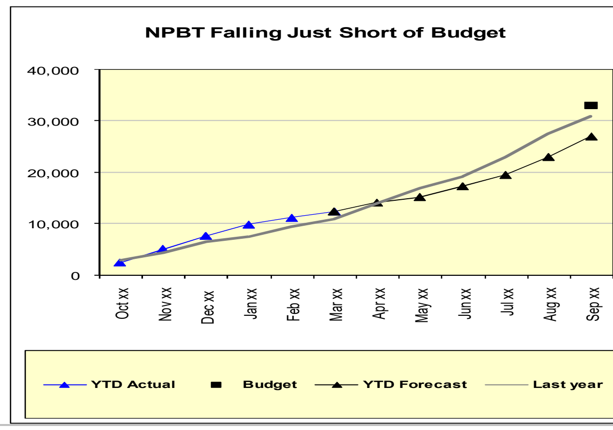
Value of new business:

All businesses in the private sector need to focus on the growth of their rising stars. It is important to monitor the pickup of this new business especially amongst the top 10-20% customers.



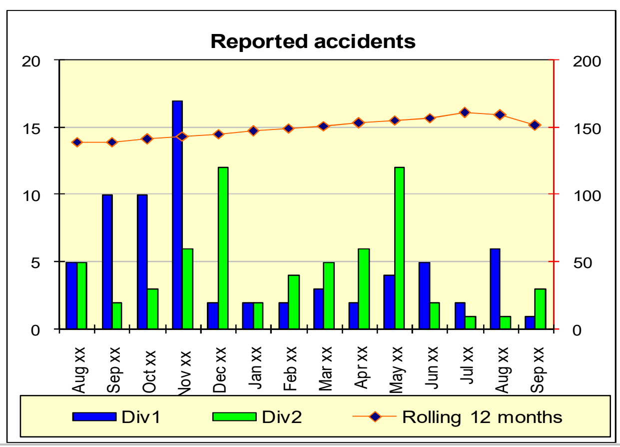
Net profit before tax (NPBT):

Since the Board will always have a focus on the year-end it is worthwhile showing the cumulative NPBT. This graph will include the most recent forecast which should be updated on a quarterly basis bottom-up.



Health & Safety:

All Boards are interested in this area as the well-being of staff is a major focus of responsible management.



Return on capital employed:

The old stalwart of reporting. The difference now that it is no longer a KPI but a KRI.