Getting FOCUSED On PERFORMANCE MEASUREMENT

Supply chain managers need to balance between getting enough information and having too many measures that result in information-overload and confusion. Focusing on the "Vital Few" Key Performance Indicators will help your company avoid the metrics maze.

by Kate Vitasek

Are You Stuck in a Metrics Maze?

There's no shortage of business performance measures. Literally hundreds of metrics have been used to evaluate and measure performance.

The number of metrics has proliferated, thanks to software applications like Enterprise Resource Planning (ERP), Warehouse Management Systems (WMS), and Customer Relationship Management (CRM) that have automated business transactions. Many systems proudly proclaim they can automatically generate upwards of a hundred predefined metrics that are readily available in easy-to-read "management reports."

Unfortunately, it's easy to end up measuring everything that moves, but learning little about what's important to your business. Having too many metrics becomes an issue as a typical manager can really only deal with seven (plus or minus two) Key Performance Indicators (KPIs) effectively on a continual basis.[1]

A key indication that you're caught in a metrics maze is when you get your "metrics report"—often several pages long—briefly peruse it, then pile it on top of another stack of paperwork on your desk. Having too many measures stifles your ability to understand what's most important, creating information-overload and confusion.

Getting to the Vital Few

In order to be successful today, companies need to have a vision of where they want to be in three, five, even ten years from now. Management then needs to select the key performance indicators that will best monitor their progress against their specific goals and objectives.

Translating your company's goals into a clear metrics portfolio will help your organization stay focused as this will provide direct feedback based on performance against its KPIs. A company such as GE, for example, strives to be #1 or #2 in the markets it competes in. Undoubtedly, GE measures market share. If its market share is not #1 or #2, it exits the market. The key is that the metric (market share) is aligned with the company's strategy, and it takes action based on performance achievement.

A simple rule of thumb for weeding out the non-critical metrics is to ask yourself "does knowing this measure help me achieve my company's goal?" If not, the metric is simply data, and not a true performance measure. When put to this simple test, most managers find that their company's "metrics reports" are more of a laundry list of nice-to-know data versus a true key performance indicator.

Once extraneous "data" has been filtered out, the challenge then becomes to produce aggregate views for management while leveraging the data for analysis and support of "root cause analysis" that employees and different functional departments need to manage the business.

Aggregate views presented to the CEO may well be "bundled" measures. One way to do this is through metrics "indexing." The Perfect Order Index is a great example of how this works.

The Perfect Order Index

A perfect order typically is defined as on time, complete, damage-free, and having the correct invoice. The perfect order is calculated by multiplying the metrics to each other. If a firm is experiencing 95% on-time delivery, fill rate, a correct invoice, and damage-free shipments, the resulting perfect order index would be 81.4% (95% x 95% x 95% x 95%).

Had each of the measures been 90%, the perfect order index would drop significantly—to 65.6%. Using an index versus looking at the individual metrics can help a company get to the heart of what really matters for a customer-focused firm, which is "Did the customer get what they want, when they wanted it, and how they wanted it?"

Although improving customer service is the primary objective of achieving the perfect order, cost savings can be a big factor as well. The cost of doing "wrong" can be very high. While it's difficult for a company to pinpoint the cost of an imperfect order, some obvious costs include resources and costs required to correct an order, such as shipping a replacement product, refunding the purchase price, or providing a credit. In some industries—such as the retail environment—costs for failure to comply with the retailer's specific order requirements can add up to millions of dollars in compliance charges.

Unfortunately, this money comes straight out of the profits. However, the biggest cost is probably not in correcting the order or in compliance fees, but rather in the costs associated with a lost customer or account.

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Driving the Need to Improve

It's not enough to simply have metrics; it's what you do with them that matters. Measuring for measurements sake is simply a wasted effort. Peter Drucker summed it up best when he stated, "There is surely nothing quite so useless as doing with great efficiency what should not be done at all."

Performance measurements should be used as a trigger for understanding what improvements a company should make in their business. The best companies don't just stop at the numbers, they take action to make the needed changes to get performance gains. ■

[1] *Michael Smith, Audrey Apfel and Ken Bergstrom, "Standard Non Financial Business Measurement: the time has come;" Gartner 2003.*

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