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Effects of balanced scorecard on performance of firms in the service sector

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ABSTRACT
This study sought to establish the effects of the Balanced Scorecard (BSC) on performance of firms in the service sector. The study location was in Kakamega Municipality, Kenya and a survey research design involving 200 service providing firms was utilized. Stratified random sampling procedure was adopted with the strata organized based on the nature of services offered. After the stratification, simple random sampling was utilized to select the respondent firms. Semi-structured questionnaires were employed to collect primary data which were analyzed through descriptive statistics. The study revealed that non-financial criteria are as important as financial criteria in measurement systems and when both measures are integrated in the system, they lead to superior results.

Keywords: Balanced scorecard, firm performance, service sector

INTRODUCTION

The purpose of measuring performance is not only to know how a business is performing but also to enable it to perform better. The ultimate aim of implementing a performance measurement system is to improve the performance of an organization so that it may better serve its customers, employees, owners, and other stakeholders (Johnson, 1981). Performance measurement generates data that will inform the users where the business is, how it is doing, and where it is going. A performance measurement system enables an enterprise to plan, measure and control its performance according to a pre-defined strategy (Okwo & Marire, 2012).

Researchers assert that there has been a paradigm shift from the traditional financial performance measurement approach to an approach integrating both financial and non-financial measures (Atkinson & Kaplan, 2003; Hoque & James, 2000; Malina & Selto, 2001; Simons, 2000). Organizations have a variety of goals and objectives and hence it is more unlikely that a single measure or even several measures of the same type will effectively assess organizational progress towards all of those goals and objectives. A primary goal is to be financially solvent. Since solvency is determined by the relationship between cash inflows and outflows, cash flow has often been used as a performance measure. If the organization is profit oriented, its goal will be to provide satisfactory returns to shareholders. Accordingly, some measurement of income is used by virtually all businesses to assess performance.

Firms have established goals relative to customer satisfaction rates, product defect rates, lead time to market and environmental social responsibility. Such goals are not measured directly by income. Firms producing inferior goods, delivering late, abusing the environment or in general making customers dissatisfied will lose market share and be forced out of business (Spraakman, 2005). Non-financial performance measures can be developed to indicate progress (or lack thereof) towards achievement of the important, long-run critical success factors of world class companies. Research has shown that the strongest drivers of competitive achievement are the intangibles, especially intellectual property, innovation, and quality. Since what is measured gets done, and because these factors are important, then they should be measured.

Some of the most important intangible assets a company can have are relationships with customers and with employees. Employee loyalty and customer loyalty are closely linked, and retaining both is essential for success. Both are stakeholders; and there is no conflict between satisfying stakeholders and shareholders. The quality of important relationships must be reflected in a performance measurement framework, often called a scorecard. Performance measures are usually used to track progress towards a target. The measures are a surrogate for the target itself. They determine how, and on what bases, managers and other employees focus their time and efforts. Non-financial indicators are, in effect, surrogate measures for financial performance. Financial and non-financial performance measures can be combined through the BSC that ultimately links all aspects of performance to the firm's strategies.

The BSC is a performance measurement conceptualization that translates an organization's strategy into clear objectives, measures, targets, and initiatives organized in the four perspectives: financial, customer, business

processes, and human resources or innovation and learning (Kassahun, 2010). The BSC is the most widely applied performance management system today. It was originally developed as a performance measurement system in 1992 by Dr. Robert Kaplan and Dr. David Norton at the Harvard Business School and later developed into a performance management tool. The basic idea of a BSC is that learning is necessary to improve internal business processes; this improvement is necessary to improve customer satisfaction; which in turn leads to improved financial results. The BSC emphasizes improvement and not just attainment of certain objectives and if an organization does not continually improve, it will eventually lose out to competitors that do (Kaplan, 2010). With the BSC, company executives can measure and manage how their business units create value for current and future customers, how they must build and enhance internal capabilities, and the investment in people, systems, and procedures necessary to improve future performance. This study attempts to investigate the effects of the BSC on organizational performance in the service sector. It follows that survival in the service sector demands for improved service delivery at the business unit level. Firms will strive to maintain a balanced performance measurement system with the cause-effect relationship.

LITERATURE REVIEW

According to Chaudron (2003), the BSC is a way of: measuring organizational, business unit or departmental success; balancing long-term and short-term actions; balancing the following different measures of success; Financial; Customer; Internal Operations; Human Resource Systems & Development (learning and growth); tying the firm's strategy to measures of action. Much of the success of the scorecard depends on how the measures are agreed, the way they are implemented and how they are acted upon (Bourne, 2002).

Financial perspective

The financial performance measures define the long-run objectives of the business unit (Kaplan & Norton, 1992). Financial measures indicate whether the organization's strategy implementation and execution are contributing to bottom-line improvement. A well-designed financial control system can actually enhance an organization's management system. The performance measures in this perspective include improved cost structure and increased assets utilization using the productivity improvement strategy, on one hand and on the other hand enhanced customer value and expanded revenue opportunities through revenue growth strategies. The financial perspective emphasizes cost efficiency, that is, the ability to deliver maximum value to the customer at minimum cost and sustained stakeholder value (Gekonge, 2005).

Customer perspective

This perspective captures the ability of the organization to provide quality goods and services, the effectiveness of their delivery, and overall customer service and satisfaction. This will result from price, quality, availability, selection, functionality, service, partnerships and brand value propositions, which will lead to increased customer acquisition and retention (Gekonge, 2005). The BSC demands that managers translate their general mission statement on customer service into specific measures that reflect the factors that really matter to customers (Kaplan & Norton, 1992). Customers' concerns tend to fall into four categories: time, quality, performance and service, and cost. Satisfied customers buy a product again, talk favorably to others about the product, pay less attention to competing brands and advertising, and buy other products from the company (Kotler & Armstrong, 2004). Recent management philosophy has shown an increasing realization of the importance of customer focus and customer satisfaction in any business (Chabrow, 2002; Holloway, 2002; Needleman, 2003).

Internal processes perspective

According Gekonge (2005), internal processes perspective focuses on the internal business results that lead to financial success and satisfied customers. To meet the organizational objectives and customers' expectations, organizations must identify the key business processes at which they must excel. These key business processes are monitored to ensure that outcomes will always be satisfactory. The internal processes perspective reports on the efficiency of internal processes and procedures. The premise behind this perceptive is that customer-based measures are important, but they must be translated into measures of what the organization must do internally to meet its customers' expectations (Kaplan & Norton, 1992).

Innovation, learning and growth perspective

The learning and growth perspective examines the ability of employees (skills, talents, knowledge and training), the quality of information systems (systems, databases and networks) and the effects of organizational alignment (culture, leadership, alignment and teamwork), in supporting the accomplishment of organizational objectives (Gekonge, 2005). Processes will only succeed if adequately skilled and motivated employees, supplied with accurate and timely

information and led by effective leadership, are driving them. They will lead to production and delivery of quality products and services; and eventually successful financial performance (Gekonge, 2005).

PERFORMANCE MEASUREMENT AND MANAGEMENT

Gekonge (2005), interpret performance measurement as a process of assessing progress towards achieving pre-determined goals and objectives. It includes information on the efficiency with which resources are transformed into goods and services (outcomes), the quality of those goods and services (how well they are delivered to customers and the extent to which customers are satisfied), and outcomes (the results of the program activity compared to its intended purpose), and the effectiveness of the company operations, in terms of their specific contribution to creating value for stakeholders.

Performance measurement systems were developed as a means of monitoring and maintaining organisational control (Nani et al, 1990), which is the process of ensuring that an organisation pursues strategies that lead to the achievement of overall goals and objectives. A performance measure can be defined as a metric used to quantify the efficiency and/or effectiveness of an action. Edson (1988) and Talley (1991) stressed the need for performance measurement systems to focus attention on continuous improvement. Kaplan & Norton (2001) observes that an effective performance measurement system should provide timely and accurate feedback on the efficiency and effectiveness of operations. The following dimensions: planning, controlling and evaluating, managing change, communication, measurement and improvement, resource allocation, motivation, have been identified by Sinclair & Zairi (1995), as the need for measurement.

PERFORMANCE AND THE BALANCED SCORECARD

According to Abernathy (2000), the typical employee does not understand the organization's strategy and consequently fails to focus on the right things; does not know his or her personal role in accomplishing the strategy and as a result does what is required, not what is needed. In addition, employees in many organizations pursue personal rather than organizational goals, because of disharmony between employee and organizational strategies and goals, and because of existing reward structures that focus on individual or sub-unit achievements rather than the achievement of corporate goals (Kerr, 1975). In such a corporate environment, organizational sub-optimization is the result of sub-organizational optimization. Frigo & Krumwiede (2000) suggest that the BSC can help remedy this situation because it requires organizations to engage in several beneficial activities. These activities delineate the major strengths of the BSC. Interest among both academics and practitioners in performance measurement systems as a tool for delivering strategic objectives is now well established in the management literature (Kaplan & Norton, 1992; Eccels & Pyburn, 1992).

Performance measurement incorporating non-financial measures has been a topic of great interest throughout most of the 1990s. This is because non-financial measures overcome the limitations of just using financial performance measures. "Soft" measures, such as employee satisfaction and commitment, are coming to the fore as protagonists of the business performance measurement revolution urge organisations to complement their traditional financial focus with softer data. Kaplan & Norton (1992) suggest that what is needed is "a balanced presentation of both financial and operational measures". In addition, while traditional financial measures report on what happened during the last period without indicating how managers can improve performance in the next, the scorecard functions as the cornerstone of the organisation's current and future success (Kaplan & Norton, 1996).

The balanced scorecard translates an organisation's mission and strategy into a comprehensive set of performance measures that provides the framework for a strategic measurement and management system (Kumari, 2011). The four perspectives of the scorecard permit a balance between short-term and long-term objectives, between desired outcomes and the performance drivers of those outcomes, and between the objective measures and softer, more subjective measures. While the multiplicity of measures on a balanced scorecard seems confusing to some people, properly constructed scorecards contain a unity of purpose since all the measures are directed towards achieving an integrated strategy. Currently, the Balanced Scorecard is a powerful and widely accepted framework for defining performance measures and communicating objectives and vision to the organisation. A balance of measures across these four perspectives is what gives the BSC its name. However, the measures that make up a scorecard do not exist in isolation from each other. They relate to a set of objectives that are themselves linked, the final link usually relating to financial outcomes of one form or another. Measures in this context can be used to communicate not simply control.

RESEARCH METHODOLOGY

A survey research design was adopted in order to allow an in-depth and representative analysis to be conducted. The population of study consisted of all the service providing firms in operating within Kakamega Municipality, Kenya as at December, 2007. According to the revenue officer in the municipality, there were 200 service providing firms operating at the time of the study. However, due to the nature of services provided and size of the firms, the population excluded some small and medium sized firms such as salons, shoe shiners, barbers and colleges. It also excluded some government institutions and NGOs. The sampling procedure used was stratified random sampling. The strata were organized based on the nature of services offered and included banking, insurance, hospitality, professional firms, transport and communication, security services and others. After the stratification, a simple random sampling approach was utilized to select the respondent firms. On average, 30% or more of each sub-group was analysed. For each sampled firm one person at the management level, preferably the managing director or the finance manager was chosen as the respondent. Semi-structured questionnaires were employed to collect primary data. The strata represented the various business lines within the service sector. Simple random sampling approach was used to select the respondent firms within a given strata. Descriptive statistics were used to organize, interpret and present the data collected.

DATA ANALYSIS

Table 1: Nature of Services Offered

Nature of Service	Frequency	Percentage
Banking services	5	8%
Insurance services	8	13%
Hospitality services	15	24%
Medical services	5	8%
Financial services	4	6%
Transport and Communication	4	6%
Educational services	5	8%
Consultancy and Professional services	14	22%
Security and Courier	3	5%
Totals	**63**	**100%**

Source: Research Data (2008)

Of the 63 respondent firms, 24% offered hospitality services, 22% consultancy and professional services, 13% insurance services, 8% banking services, 8% medical services, 8% educational services, 6% financial services, 6% transport and communication services and 5% offered security and courier services. This indicates that within Kakamega Municipality there are firms which offer a range of services. The hospitality industry has the highest number of firms, followed by consultancy and professional firms, then insurance firms, after which banking, medical and educational firms are equally distributed. Financial firms and transport and communication firms were equally distributed while security and courier firms are the least.

Table 2: Methods of enhancing employees' skills and performance

Method	Frequency	Percentage
Training	42	40%
Better employee rewards	25	24%
Enhancing team building	20	19%
Employee participation in decision making	16	15%
Compulsory annual leave	2	2%
Totals	**105**	**100%**

Source: Research Data (2008)

The findings reveal that 40% of the respondents enhanced their employees' skills and performance through training, 24% through better employee rewards, 19% through enhancing team building, 15% encourage employee participation in decision making while only 2% encourage compulsory annual leave to their employees. The information indicates that most of the firms train their employees to enhance their skills and performance, others give better rewards to employees and others enhance team building. Some firms also encourage employee participation in decision making and yet others offer compulsory annual leave as a way of enhancing performance.

Table 3: Effects of enhanced employee performance on the firm

Effect	Frequency	Percentage
Improved internal business processes	45	52%
Development of new products	7	8%
Increased customer loyalty	34	40%
Totals	**86**	**100%**

Source: Research Data (2008)

Outcomes confirms that out of the 63 respondent firms, 52% experienced increased efficiency in their internal business processes after enhancing their employees' skills and performance, 40% increased their customer loyalty while 8% developed new products. In the majority of firms, enhanced employees' skills and performance led to increased efficiency in their internal business processes while some attained more loyal customers. In addition, there were few firms that develop new products from the suggestions of their satisfied customers.

Table 4: Benefits of having satisfied customers to organizations

Benefits	Frequency	Percentage
Repetitive buying/ customer referrals	32	41%
Full-time customers/ cross-buying	38	48%
Does not bad-mouth our products	4	5%
Customer-initiated product innovations	5	6%
Totals	**79**	**100%**

Source: Research Data (2008)

Various firms benefit in different ways as a result of having satisfied customers. Results demonstrates that 48% of the firms benefit by acquiring full-time customers and cross-selling their products, 41% enjoy repetitive buying and customer referrals, while 6% enjoy customer-initiated product innovations. Moreover, 5% benefit from customers who do not bad-mouth their products.

Table 5: Training, innovation and customer satisfaction costs as a proportion to total expenditure

Level	Frequency	Percentage
High	18	29%
Medium	37	59%
Low	8	13%
Totals	**63**	**100%**

Source: Research Data (2008)

Findings disclose that 37 firms out of the 63 respondent firms moderately invest in training, innovation and customer satisfaction as a proportion to their total budgetary expenditures, 18 firms vastly invest while only 8 firms invest scantily. This implies that in the majority of firms, investment in training, innovation and customer satisfaction as a proportion to their total expenditure is moderate.

Table 6: Spill-over effect of increased profitability on other functions of the firm

Effect	Frequency	Percentage
Good employee reward system	33	37%
Payment of higher dividends	18	20%
Response to corporate social responsibilities	26	29%
Business expansion	12	13%
Totals	**89**	**100%**

Source: Research Data (2008)

Outcomes reveal that different firms have different spill-over effects on their functions as a result of increased profits. Majority (37%) of the firms gave better rewards to the employees, 29% undertook additional corporate social responsibilities, 20% paid higher dividends to their shareholders while 13% expand their businesses.

Rating the drivers of success

To rate the various drivers of success, the very important rate was allocated a weight of 5 points, important was allocated a weight of 3 points and not important was allocated a weight of 1 point. The various weights were multiplied by the number of respondents who gave a particular rate and then divided by the total number of respondents to get the weighted mean. The expected mean was the weight of 3 points (weight allocated for important rate).

Table 7: Rating the drivers of success

Drivers of success	Very Important	Important	Not Important	Total weight	Mean weight
Weight	**5**	**3**	**1**		
Learning, growth and innovation	175	84	-	259	4.11
Customer satisfaction	285	18	-	303	4.81
Improved internal business processes	180	81	-	261	4.14
Highly developed and motivated staff	140	105	-	245	3.89

Source: Research Data (2008)

The results indicate that all the drivers of success had a mean value above the expected mean. The customer satisfaction had the highest mean value of 4.81, improved internal business processes had a mean of 4.14, and learning, growth and innovation had a mean of 4.11, while highly motivated staff had the lowest mean of 3.89. This indicates that, on average, all the four measures are viewed to be more than important drivers of the firms' success.

Table 8: Measures of success

Measures	Frequency	Percentage
Financial gains	29	27%
Customer satisfaction	56	51%
More developed internal processes	10	9%
Highly developed and motivated staff	14	13%
Totals	**109**	**100%**

Source: Research Data (2008)

Finings reveal that majority (51%) of the firms measure their success based on the satisfaction of their customers, 27% consider financial gains, 13% consider highly developed and motivated staff while only 9% gauge their performance on more improved internal business processes.

DISCUSSIONS

The first objective was to ascertain whether the Balanced Scorecard is being used to measure and manage performance in the service sector. Findings revealed that, though differently, all firms develop their employees' skills and performance. Firms invest in training, innovation and customer satisfaction as such; the four perspectives of the BSC are the most important drivers of a firm's success. The second objective was examining the perceptions of the service sector managers regarding the BSC concept. Firms rated the four BSC perspectives as very important drivers of success. It was revealed that most managers strongly agreed that improvement in one BSC perspective led to improvement in the other perspectives. The third objective was to assess the effect of the BSC on the firm's overall performance. All firms develop their employees' skills and performance which led to increased efficiency in their internal business processes. This led to improved customer satisfaction and increased market share, which in turn led to an increase in the firm's profitability. It was affirmed that increased profitability boosted the other functions of the firms which improved rewards to employees and more participation in corporate social responsibilities. It also gave the firms a positive public image and increased competitiveness.

CONCLUSIONS

The BSC emphasizes performance measurement and management in four key business areas. These four perspectives provide a comprehensive evaluation of the organization than the traditional emphasis on tangible and financial assets of the organization. This is because learning improves the internal business processes; this improvement leads to improved customer satisfaction; which in turn leads to improved financial results. The BSC emphasizes improvement and if an organization does not continually improve, it will eventually lose out to competitors that do.

Incorporating these perspectives in the BSC offers a framework for translating strategic objectives into performance measurements that gauge the effects of implemented strategies and provide feedback on the performance of strategic initiatives. The BSC offers some useful generic performance measurements that apply to practically all organizations. Firms, small or large, need to know how they measure up to their own goals and standards, and the BSC can give them the advantage they need to evaluate themselves accurately and, as a result, place themselves in a better position to compete. The main goal for all businesses is to manage their overall performance so that they can make a profit.

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