Developing Performance Metrics in a Service Organization

Managers in service companies often find that one of the biggest challenges they face is to drive the performance of their businesses. The fundamental issue that underlies this challenge is the difficulty of defining effective performance measurements within an environment that does not lend itself to hard and fast metrics.

The key asset in a service industry is people and the key product is a service or a suite of services. All people are obviously completely unique and unpredictable to some extent, and services are typically sold and provided as customized solutions for each individual purchaser. Consequently, both of those key elements have a high degree of variability. In contrast, the goal in a manufacturing environment is to reduce variability by creating standardized processes that are performed repeatedly until all inefficiencies are removed. Progress is measured by the reduced waste and faster production time that come with process improvements that minimize variability.

Variability is inherent for service industries, so how can you measure performance in order to improve it? How can you reduce inefficiencies when full standardization is impossible? It can be tempting for managers to accept increased staff sizes and cushioned price contracts that will simply absorb those inefficiencies, but such practices will not support a sustainable, competitive business. Managers of service companies must, no matter how difficult it seems, define effective performance metrics (Key Performance Indicators or KPIs) for their businesses. This paper examines how to develop KPIs to drive performance improvements for service organizations.

Step 1: Understand your Client Base and Client Interface

Service industry managers can begin by carefully examining their client base, and what variances exist within that base. Managers must develop a consistent methodology to clearly define each client segment and to collect and analyze data for each segment that will drive the development of performance metrics.

Step 2: Prepare the Organization for Change

The KPIs will impact multiple units or departments within the company, and the manager implementing the metrics can probably expect some measure of resistance. The resulting data may be questioned because it is not an exact measure of the way the area is actually performing.

It is critical that everyone understands that no performance metric will ever perfectly measure the results of every part of an organization, and this is especially true in a service organization. It is the responsibility of the team developing the KPI to do meticulous analysis so that the final metrics are effective, and also to communicate to everyone that perfection is not the standard. The measurements should be as accurate as possible, applied consistently, and most importantly they should provide important information to the management team who will use the information to make critical strategic decisions to improve performance at every level.

Step 3: Developing Metrics and The Metric Perspective

In the book *"The Balanced Scorecard"* David P. Norton and Robert S. Kaplan questioned the efficacy of utilizing what have become the most popular performance measures - financial accounting measures. Norton and Kaplan state, "*The success of organizations cannot be motivated or measured by financial metrics alone."* Financial metrics provide primarily historical information and are based on accounting data. Norton and Kaplan argue that the practice of managing a business utilizing only historical financial data is flawed, and that forward-looking estimates that reflect the strategic direction of the company is immensely more valuable to managers.

As an alternative to managing performance using traditional financial measures, Norton and Kaplan developed what they call the "balanced scorecard." Some suggested categories of metrics to be used within the scorecard include (but are not limited to) the following:

1. Financial
2. Customer
3. Internal
4. Learning and Growth

Thomas E. Lah the author of Mastering Professional Services in his White Paper Metrics that Matter: Measuring Professional Services Business developed some perspectives to consider when introducing performance measurements into a services organization. In his Paper, Lah states the following:

"Every metric provides a certain perspective on your business. In other words, different metrics tell you different things about your business. Some metrics tell you there is a problem today. Some metrics give you a heads up that there will be a problem down the road. Also, metrics naturally have different scopes.

Total services revenue indicates how the overall business is doing, but provides little insight on how individual consultants are doing. Individual utilization metrics provides insight on individual performance and the overall health of the business. Continuing this logic, there are at least five unique metric perspectives you can consider:

1. Functional Perspective: What business function does this KPI help evaluate? Your sales organization? Your delivery teams? Service Marketing?
2. Economic Perspective: Almost every internal company initiative has one of two objectives: improve operational efficiency or create future revenue (economic value). Does the metric track improvements in operational efficiency or assess the economic value of the business?
3. Timeframe Perspective: Just like economic data, is the metric a leading or lagging indicator of how the business is performing? Does the metric indicate you currently have a real problem, or does the metric warn that soon you will have a problem if the current trend continues?
4. Scope Perspective: Does the metric measure the performance of specific individuals, specific projects, or the entire business unit?
5. Stakeholder Perspective: Does this metric provide insight on how your external stakeholders view you? External stakeholders would include customers and partners."

Step 4: Maintaining the Effectiveness of Performance Metrics

The task of the service manager is not over once the KPIs are in place. To ensure that the metrics continue to drive performance, it is important to evaluate them continuously. The service manager should:

1. Revise the KPIs as needed when changes are made in the organization, client base, or services offered.
2. Continue to track improvements in performance and communicate them to the company as a whole so that the momentum of success drives further improvements.
3. Ensure that compensation packages continue to incent those responsible for the improved performance.

This may seem a daunting exercise to deploy and track these service KPIs. But until you fully understand your numbers, you cannot make impactful and sustainable changes to improve service, margins and profit.