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THE HIDDEN DISADVANTAGES OF PERFORMANCE INDICATORS

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Abstract:
Measuring organizational performance is crucial for assessing the effectiveness of an organization's strategies, processes, and overall health. There are various methods and metrics that can be used to measure organizational performance, and the choice of these methods often depends on the organization's goals, industry and specific context. However, even when we know what should be measured we should make sure that we are measuring the right dimension, "the length" or "the width", in order to obtain the correct and appropriate assessment of the situation. This paper will present some common approaches to establishing key performance indicators (KPIs) as well as, the pitfalls management should be aware of during this process.

Key words: key performance indicators (KPIs); lagging KPIs, leading KPIs, performance; results; organization; benefits; advantages; disadvantages;

1.Introduction

Organizational performance measuring plays a vital role in the success and sustainability of any organization. Measurements are important for aligning the organizational goals, analyzing activities and identifying organizational strengths and weaknesses thus, obtaining the elements which will support an informed decision making process. An efficient performance measurement process is based on properly identified Key Performance Indicators (KPIs). There are Key Performance Indicators that can significantly impact and improve organizational performance however, the specific KPIs that are most relevant to improving performance can vary based on the nature of the organization, its goals, and its domain of activity.

Nevertheless, here are some universally important KPIs that often contribute to enhancing organizational performance: lagging vs. leading KPIs and high vs. low KPIs. We shall explain their characteristics in the following chapter. [1]

2.Prerequisites for establishing organizational KPIs

Measuring organizational performance is crucial for assessing the effectiveness of an organization's strategies, processes, and overall health. However, before establishing KPIs, those in charge with the activity should align KPIs' objectives with organization's objectives.

In the introduction we mentioned two main categories of KPIs based on which we can establish out organizational ones:

Lagging KPIs:

Lagging indicators are retrospective measures that assess the performance based on historical data. They indicate the success or failure after an event has occurred. For example, the revenue, profit, customer satisfaction scores and employee turnover etc. Such metrics reflect the outcomes of past actions.

Leading KPIs:

Leading indicators are forward-looking metrics that provide insights into potential future performance. They help predict outcomes and guide actions to achieve desired results. For example, customer engagement metrics, and employee training hours can be leading indicators. These metrics provide insights into activities and trends that may impact future outcomes.

High KPIs:

High KPIs refer to key metrics that are deemed desirable and indicative of positive performance. For example, high revenue growth or high customer satisfaction scores, are examples of KPIs that are typically viewed positively by organizations.

Low KPIs:

Low KPIs are key metrics that are considered undesirable or indicative of suboptimal performance. For example, low profit margins, low customer retention rates, and low employee productivity are examples of KPIs that may raise concerns and require attention.

It's important to note that the interpretation of whether a KPI is high or low depends on the specific goals and benchmarks set by an organization. A KPI that is considered high in one context might be considered low in another, depending on the objectives and industry standards. [2]

2.1 Impact of KPISs on organizational performance

Effective performance management involves monitoring a combination of lagging and leading indicators to gain a comprehensive understanding of current performance and to make informed decisions to improve future outcomes.

Even if they are essential metrics used by organizations to evaluate their success in achieving specific goals and objectives, they can deform and harm the way these are set thus leading to incorrect measurements. Below, there is a breakdown of the pros and cons associated with using organizational KPIs:

Pros of Organizational KPIs:

- Clarity of Goals: KPIs provide a clear understanding of organizational goals, ensuring that everyone is aligned with the strategic objectives.
- Measurable Objectives: KPIs are measurable, allowing organizations to quantify their progress toward specific outcomes.
- Focus and Prioritization: KPIs help in focusing efforts and resources on critical areas, enabling better allocation of time, money, and manpower.
- Performance Evaluation: KPIs provide a basis for evaluating the performance of departments, teams, and individuals, fostering accountability.
- Decision Making: KPI data assists in informed decision-making processes, enabling organizations to adapt strategies based on real-time insights.
- Motivation and Engagement: Clear KPIs can motivate employees by providing achievable targets, fostering a sense of accomplishment and motivation to perform well.
- Benchmarking: KPIs allow organizations to compare their performance against industry standards and competitors, identifying areas for improvement.

- Communication: KPIs facilitate communication within the organization by providing a common language for discussing performance and objectives. [3][4]

Cons of Organizational KPIs:

- Overemphasis on Numbers: Excessive focus on KPIs may lead to a narrow perspective, ignoring qualitative aspects that are crucial for overall organizational health.
- Misalignment with Strategy: If not chosen carefully, KPIs can be misaligned with the overall organizational strategy, leading to efforts that don't contribute to the broader goals.
- Unintended Consequences: Employees might focus solely on achieving KPIs, potentially neglecting other essential aspects of their roles, such as innovation or customer satisfaction.
- Data Quality Issues: Inaccurate or incomplete data can distort KPIs, leading to misguided decisions and actions.
- Resistance and Stress: Employees may feel stressed or demotivated if KPIs are set unrealistically high or if they are used punitively rather than supportively.
- Lack of Adaptability: Rapid changes in the business environment may render certain KPIs irrelevant, requiring constant monitoring and adjustment.
- Short-term Focus: Some KPIs encourage short-term thinking and might discourage investments or efforts that yield results in the long run.
- Complexity: Managing and analyzing numerous KPIs can be complex, especially for large organizations, requiring sophisticated data management systems and skilled analysts. [5] [6]

3.Important preconditions for setting KPIs

In order to develop efficient KPIs, not only accurate in measurement, but also measuring the appropriate elements, we need to know the organization, its specific, purpose, strong and weak points. Below, we have constructed a list of necessary preconditions for setting up efficient KPIs:

a) Clearly defined organizational objectives and goals. KPIs should align with and directly contribute to the achievement of specific, measurable, and time-bound objectives. Without clear objectives, it becomes challenging to identify relevant KPIs.
b) Involvement of key stakeholders in the KPI development process. Inclusion of diverse perspectives ensures that KPIs reflect the priorities and concerns of various stakeholders, fostering greater buy-in and support for the performance measurement system.
c) KPIs must be relevant to the organization's industry, business model, and strategic priorities. Relevant KPIs provide meaningful insights into performance and help prioritize efforts toward achieving strategic objectives.
d) The ability to measure and quantify the selected KPIs accurately. KPIs should be based on data that is accessible, reliable, and can be measured consistently over time. This ensures that performance can be objectively assessed.

e) KPIs should be specific and well-defined. Vague or ambiguous KPIs can lead to confusion and misinterpretation. Clearly defined KPIs provide a basis for effective decision-making and performance improvement.
f) Access to relevant benchmarks or industry standards for comparison. Benchmarks provide context for interpreting KPI values. Comparing performance against industry standards or best practices helps identify areas for improvement and sets realistic performance expectations.
g) Adequate availability of data required for measuring and analyzing KPIs. Without reliable and timely data, it is challenging to monitor and evaluate performance accurately. Organizations must ensure that the necessary data sources and infrastructure are in place.
h) KPIs should align with the overall organizational strategy. KPIs should directly support the organization's strategic goals, ensuring that efforts are focused on activities that contribute to the broader mission and vision.
i) Regular review and adjustment of KPIs to reflect changes in the business environment or organizational priorities. Business conditions and priorities evolve over time. Periodic reviews ensure that KPIs remain relevant and continue to provide valuable insights.
j) Clear communication and education regarding the purpose and significance of selected KPIs.
k) Ensuring that all relevant stakeholders understand the importance of KPIs fosters a shared commitment to achieving organizational goals and facilitates effective use of performance data. [7] [8] [9]

By addressing these preconditions, organizations can develop a robust set of KPIs that contribute to a culture of continuous improvement and strategic alignment.

Conclusion

After analyzing the elements presented above, we can conclude that while organizational KPIs offer valuable insights and benefits, they should be chosen and managed thoughtfully, with a balanced approach that considers both quantitative and qualitative aspects of organizational performance and which looks backward and forward in the organizational life.

KPIs are very fashionable, everyone in a managerial position wants to measure the organization's activity for various reasons and such an approach, as much as it can be beneficial, it is dangerous if performed incorrectly. Therefore, before starting the measurements, we should have the clearest idea about the objective(s) we want to reach, our means of reaching them and only then, we should identify which element of the activity should be measured and to what purpose. We should not mistake the outputs for the outcomes, the quantitative measurements for the qualitative ones. For example, measuring the number of reports written and obtaining a high number is not the most appropriate measurement unless we do not care for quality. The correct metrics should measure the number of correctly completed reports (quantity and quality). Quantity is easier to be measured, but most of the time it offers the image of a fake success or performance. Also, when measuring the performance of an educational institution, KPIs should not stop only at the number of graduate, but go further to the number of ex-students employed based on their studies.

As final remarks, we would recommend avoiding the usage of metrics just because they are fashionable and they provide good cover. Measurements should be made with the clear purpose of assessing organizational health and improving what is necessary to reach performance. We should not stop at numbers even if they are satisfactory and we should always look at quality and what supports it.

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