A Guide for Developing Key Performance Indicators

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A Key Performance Indicator (KPI) is a measurable value that demonstrates how effectively a company is achieving key business objectives. In business, it is important to measure the performance of a business. This is done to track performance, to make improvements and to drive business strategy. Organizations use KPIs at multiple levels to evaluate their success at reaching targets. High-level KPIs may focus on the overall performance of the business, while low-level KPIs may focus on processes in departments such as sales, marketing, HR, support and others.

KPIs are important to business objectives because they keep objectives at the forefront of decision making. The success of any business strategy is not determined by its definition and documentation. Some of the greatest strategies have been defined carefully with great thought and insight. They are masterpieces that could not be faulted other than being left on the shelf in head-offices around the world and never implemented. Most companies and organisations are good at defining strategy; very few are good at successfully implementing strategy. In order to successfully implement strategy KPIs should be attached to the strategic objectives using the following five (5) step methodology.

Step 1 – Start with Strategy

The Golden Rule of setting KPIs is that they should be based on objectives. A KPI should not exist unless it contributes to an objective. When developing KPIs You should always start with the business strategy. Without a firm stake in the ground around what your business is seeking to achieve, it is easy to end up with a dauntingly long list of possible indicators that you feel you could or should measure.

The most common mistake businesses make when developing KPIs is focusing on activities rather than results. Objectives, like KPIs, are concerned with results. It is essential to create a target for each objective using a results-oriented language. This forces us to think more precisely about what we are actually trying to achieve.

Step 2 – Identify Both Lagging and Leading Performance Indicators

The difference between lagging and leading indicators is essentially knowing how you did, versus how you are doing. Lagging indicators measure the output of an activity that has already happened. Staff turnover, absenteeism, or the number of workplace accidents delivered are all examples of lagging indicators. These types of metrics are good for purely measuring results, as they solely focus on outputs.

On the other hand, leading indicators measure inputs, progress and your likelihood of achieving a goal in the future. These types of metrics serve as predictors of what is to come. Traditionally most organizations have solely focused on lagging indicators. One of the main reasons for this is that lagging indicators tend to be easy to measure since the events have already happened.

You can think of leading indicators as business drivers because they come before trends emerge, which can help you identify whether or not you are on track to reaching your goals. If you can identify which leading indicators will impact your future performance you will have a much better shot at success.

Step 3 – Interpret Results

Once there is a useful set of historical actual data on performance, it will be possible to effectively interpret the results. Finding the right measurement methodology is critical. Therefore, once you know what information you need to collect to objectively measure performance, you need to find the right measurement methodology to get it. This is especially true if you have to develop new KPIs or tweak existing ones.

It is always preferable to align measurement frequency with how and when the KPIs are used in the organisation, because all data has a "shelf life". This means measurement frequency must be in line with the reporting frequency. If it is not, the data may lose relevance.

Step 4 – Take Action

Taking Action comes in two major forms. The first is to put in place a remedial activity when a problem occurs; the second is to create strategic initiatives to promote change. Putting in place a remedial activity. Putting in place a remedial activity or assigning an action is a relatively simple process and something that organisations do almost every day. The key here is to ensure that the activity or action is well thought through. There are a number of things that should be taken into account when creating a remedial an activity or action:

- It should be associated with a KPI – The only way to confirm an action has had a positive effect is to observe a positive change in the KPI. Just because an action has been completed does not mean the situation has been resolved.
- Be sure to assign the action to an individual – Tasked individuals feel responsible and accountable, departments do not.
- Ensure the action is clear – in much the same way as a KPI has to be described properly, an equal amount of attention has to be given to describing an action. Be sure to ask the owner of the action if they understand what is required when it is required, and who will be involved.

Step 5 - Review the KPI on a regular basis

Checking in on your KPIs regularly is essential to their maintenance and development. Tracking progress against the KPI is important but equally essential is tracking your progress so you can assess how successful you were in developing the KPI in the first place. Not all KPIs are successful. Some have objectives that are unachievable. Some fail to track the underlying business goal they were supposed to achieve. Only by checking in regularly can you decide if it is time to change your KPIs.

KPIs are not created in a vacuum. To be of value to decision-makers, they must be part of the organisation's strategic framework. To this end, they need to be able to help communicate the strategy, as well as foster common purpose across departments and business units. Key Performance Indicators (KPIs) are important in business. But, it is important to remember that KPIs are only really useful if you identify the right ones for your business. And they will only deliver mission-critical data if you use the KPIs and analyse what they tell you on a regular basis to inform your decision making.

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