How the balanced scorecard complements the McKinsey 7-S model

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In Search of Excellence, the 1982 best-selling book by McKinsey partners Tom Peters and Robert Waterman, introduced the mass business audience to the firm's 7-S model. The model, also influenced by an earlier collaboration between McKinsey and management scholars Richard Pascale and Anthony Athos (*The Art of Japanese Management*, 1980), describes the seven factors critical for effective strategy execution[1]:

1. *Strategy*. The positioning and actions taken by an enterprise, in response to or anticipation of changes in the external environment, intended to achieve competitive advantage.
2. *Structure*. The way in which tasks and people are specialized and divided, and authority is distributed; how activities and reporting relationships are grouped; the mechanisms by which activities in the organization are coordinated.
3. *Systems*. The formal and informal procedures used to manage the organization, including management control systems, performance measurement and reward systems, planning, budgeting and resource allocation systems, and management information systems.
4. *Staff*. The people, their backgrounds and competencies; how the organization recruits, selects, trains, socializes, manages the careers, and promotes employees.
5. *Skills*. The distinctive competencies of the organization; what it does best along dimensions such as people, management practices, processes, systems, technology, and customer relationships.
6. *Style/culture*. The leadership style of managers – how they spend their time, what they focus attention on, what questions they ask of employees, how they make decisions; also the organizational culture (the dominant values and beliefs, the norms, the conscious and unconscious symbolic acts taken by leaders (job titles, dress codes, executive dining rooms, corporate jets, informal meetings with employees).
7. *Shared values*. The core or fundamental set of values that are widely shared in the organization and serve as guiding principles of what is important; vision, mission, and values statements that provide a broad sense of purpose for all employees.

After a search for the ''perfect'' organizational structure, the authors, and others, concluded that structure alone could not solve the problem of how to coordinate resource allocation, incentives, and actions across large organizations. The 7-S model posits that organizations are successful when they achieve an integrated harmony among three ''hard'' ''S's'' of strategy, structure, and systems, and four ''soft'' ''S's'' of skills, staff, style, and super-ordinate goals (now referred to as shared values). While not all the companies Peters and Waterman praised for ''excellence'' sustained their leadership performance

DOI 10.1108/10878570510594442

during the 1980s and 1990s, the 7-S model continues to be used in practice and in business school teaching as a diagnostic and prescriptive framework for organizational alignment.

Within the academic literature, economists and strategy scholars tend to focus on the more tangible and measurable hard ''S's'' of strategy, structure and systems through studies of the impact of mergers, alternative organizational forms, and incentive and reward systems. Scholars in other social sciences (organization behavior, psychology, sociology, and anthropology) focus on the more intangible and difficult-to-measure softer ''S's'' of skills, staff, style, and shared values.

Ten years after Peters and Waterman introduced the 7-S model, Dave Norton and I presented the balanced scorecard (BSC) (see ''The balanced scorecard: measures that drive performance,'' *Harvard Business Review*, January/February, 1992), a new measurement approach that organizes performance objectives and measures in four perspectives:

1. The *financial perspective* describes the tangible outcomes of the strategy in traditional financial terms, such as return on investment (ROI), shareholder value, profitability, revenue growth, and lower unit costs.
2. The *customer perspective* defines the drivers of revenue growth. It includes generic customer outcomes, such as satisfaction, acquisition, retention, and growth, as well as the differentiating value proposition the organization intends to offer to generate sales and loyalty from targeted customers.
3. The *internal process perspective* identifies the operating, customer management, innovation, and regulatory and social process objectives for creating and delivering the customer value proposition and improving the quality and productivity of operating processes.
4. The *learning and growth perspective* identifies the intangible assets that are most important to the strategy. The objectives in this perspective identify which jobs (the human capital), which systems (the information capital), and what kind of climate (the organization capital) are required to support the value creating internal processes. Managers use the scorecard to describe and communicate their strategy, to align business units and shared services to create synergies, to set priorities for strategic initiatives, and to report on and guide the implementation of the strategy.

For more than a decade now, diverse organizations around the world (manufacturing and service, private sector and public sector, for profit and not-for-profit – have used that BSC to achieve performance breakthroughs through focused and effective strategy execution. We established the Balanced Scorecard Hall of Fame (http://bscol.com/bscol/hof/) to recognize and publicize the organizations that have been most effective in implementing the concept and realizing benefits from it.

As we studied the two models, we came to realize that the 7-S model and the BSC strategic alignment models share many features in common. They both articulate that effective strategy implementation requires a multi-dimensional approach. They both stress interconnectedness. For example, the diagram for the 7-S model looks like a spider-web, with each of the ''S's'' connecting with all the other six; the BSC strategy map (see Figure 1) illustrates cause-and-effect linkages across its four perspectives. Both models help managers align their organization for effective strategy execution (see Table I).

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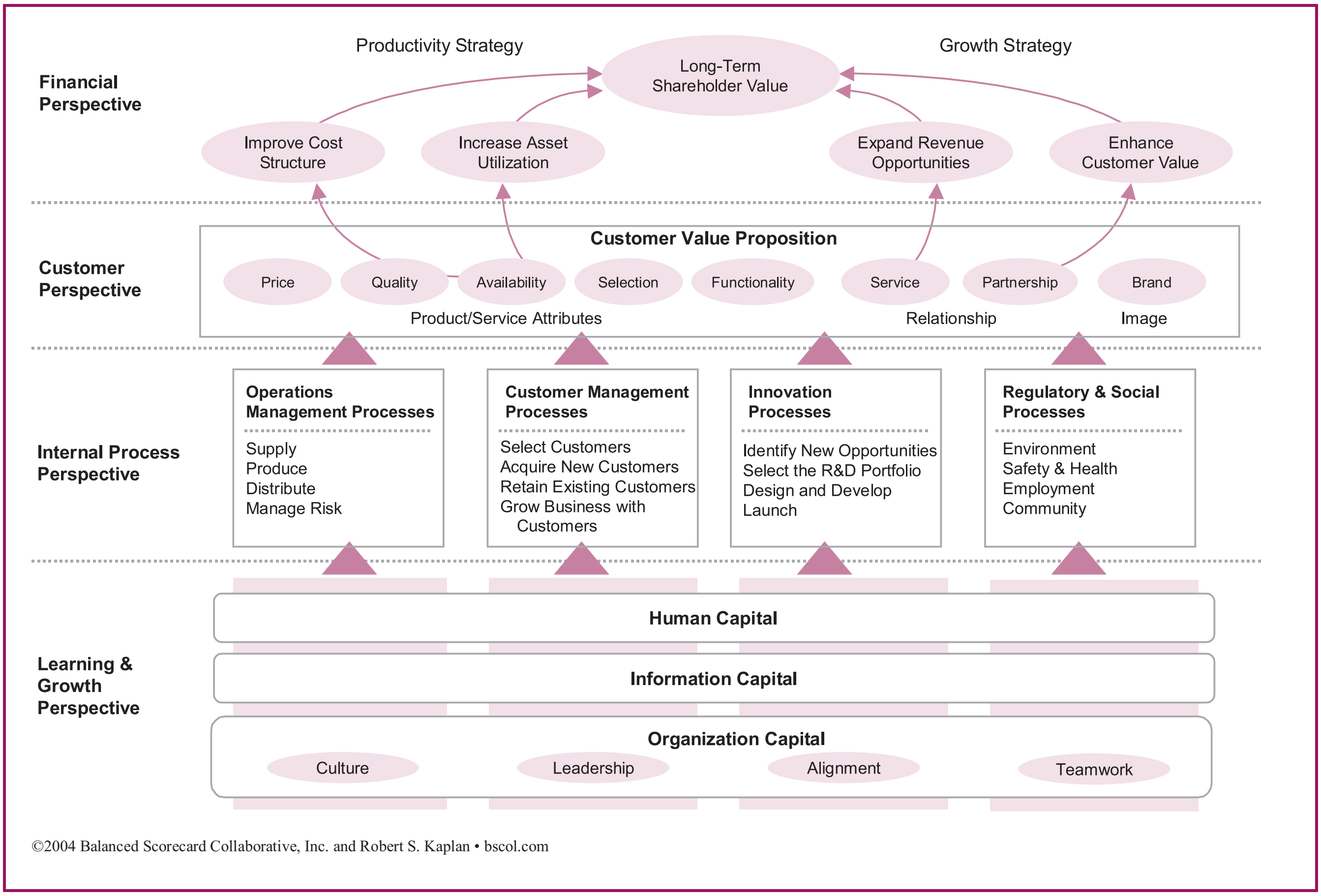
Figure 1 BSC strategy map



Beyond these similarities, I believe that the BSC is not only fully consistent with the 7-S framework, but can also enhance it in use. The BSC's most obvious benefit arises when managers use it to design a customized reporting and performance management system, the ''S,'' that many organizations fail to align with their other six S's. The BSC enables management reports to focus on measures specifically selected to represent the organization's strategy. The BSC also influences other organizational systems when managers use it to align their planning, budgeting, and resource allocation systems, and their incentive and reward systems to strategy (as described in Kaplan and Norton, ''Using the balanced scorecard as a strategic management system,'' *Harvard Business Review*, January/February, 1996).

Often, senior executives pay insufficient attention to adapting and aligning their systems even while they are introducing new strategies and structures. They continue to employ traditional budgets and financial systems that are ill suited for the new strategies and structures[2]. Some successful organizations, such as the pharmaceutical and medical appliance giant Johnson & Johnson, cleverly use their traditional financial planning, budgeting, and variance reporting systems in a highly interactive manner to foster alignment to strategy and structure[3]. But most companies have learned that financial systems alone cannot describe, communicate, guide, or evaluate their strategies. The BSC, by expanding measurement systems to include the nonfinancial indicators of the organization's strategy, has given managers a new tool to design and customize their system – the third ''S'' (to their strategy.

For structure, the second ''S,'' companies face a complex choice among organizing by function, product groups, technologies, channels, market segments, or regions, or some

Table I Comparing the 7-S model and BSC

7-S model	*BSC*
Strategy	Describes and measures the strategy, including balance between short-run cost savings and long-term revenue growth, the customer outcomes expected from a successful strategy, the customer value proposition at the heart of the strategy, and the critical internal processes that create and deliver the differentiated customer value proposition
Structure	Applying BSCs to diverse, decentralized units allows alignment across these units and to the corporate value proposition that enables synergies to be created, along with accountability for contributing to local and global performance
Systems	Organizations use the BSC to design their communication, reporting and evaluation systems for their unique strategy. Also, the BSC allows organizational systems such as incentive and reward, planning, budgeting, and resource allocation to be focused and aligned on successful strategy implementation
Staff	The BSC's learning and growth perspective identifies the critical job families that have the greatest impact on the strategy, and establishes measures for the knowledge, skills and experience of staff performing the most strategic internal processes
Skills	The BSC's internal process perspective measures the organizational skills, competencies, and processes that are most critical for the strategy to be effectively executed.
Style culture	The BSC provides the agenda for leadership meetings, and keeps executives focused on the most important tasks for strategy implementation. Specific measures in the organizational capital component of the learning and growth perspective enable an organization to specify and measure the leadership style and skills it desires
Shared values	Communicating the BSC throughout the organization creates shared understanding and commitment about the organization's long-term objectives and its strategy for achieving them. Adherence to values and cultural norms can be measured within the learning and growth's organizational capital component

combination thereof, such as in a matrix or networked organization. But even the best choice cannot solve the complex trade-offs between specialized local expertise and cross-unit integration and synergies. The BSC reduces the pressure on managers to find and install the perfect structure. Whatever structural choice they make, when managers apply the enterprise scorecard to functions and units, these units become better aligned with each other and to the enterprise. The process starts by applying the BSC at a high level, and letting the strategic objectives and themes cascade down to lower levels, where they are interpreted and customized to the specific situation faced by lower level organizational units. This is the process by which decentralized units become aligned with each other and to the corporate strategy.

Executives can also use the comprehensive performance measures on the unit's BSC to assign clear responsibility and accountability for local and global performance. By using the BSC as the primary organizational ''system,'' decentralized unit scorecards reflect both the specific competencies and strategies of the unit for local success, and also how each unit links with other units and the enterprise as a whole for the enterprise strategy to be achieved.

When strategy, structure and systems are tightly integrated, the odds for successful strategy implementation are raised substantially. But the BSC need not be limited solely to completing the alignment of the three ''hard'' S's. It also contributes a great deal to the four ''softer'' S's. The BSC's learning and growth objective specifically links the staff, the employees' knowledge, capabilities and skills, to the strategy. The process to identify strategic job families highlights those positions that have the highest impact on delivering the organization's distinctive value proposition[4]. Further, the strategic objectives for these employees in the learning and growth perspective set the agenda that ensure the staff develop the requisite knowledge, capabilities, and skills to perform the strategic processes at the targeted levels.

The fifth ''S,'' skills, generally refers to organizational skills and competencies. These are captured in the internal process perspective of the BSC, where organizations identify those operating, customer management, innovation, and regulatory and social processes that: create and deliver the distinctive customer value proposition; and lead to achieving the financial perspective's productivity objectives. In developing the strategic objectives and measures for the BSC internal perspective, the organization enhances its skills by aligning human, information, and organization capital (from the learning and growth perspective) to critical processes, and also by selecting strategic initiatives specifically aimed at enhancing the performance of the internal processes. Thus the BSC becomes a powerful tool for aligning skills, the organizational competencies, to strategy.

The final two ''S's'' are perhaps the most soft and intangible, yet they are still influenced by the BSC. Leadership style generally refers to how executives spend their time and what they pay attention to. The BSC keeps executives' attention focused on a balance between short-term operational improvements and the drivers of long-term value creation. In addition, leadership attributes and style are captured in an organization capital component in the learning and growth perspective[5]. Organizations differ in the leadership style that is most effective for them. By defining the specific, measurable behaviors desired in leaders, the BSC forces previously implicit choices to become explicit, actionable (developing the leaders' style or choosing leaders with the desired style), and accountable. The organization style is also included in the organization capital component when the enterprise selects specific objectives for teamwork, knowledge-sharing, and organization culture and climate. These choices are difficult to make and measure, but the robust framework of the BSC enables the leadership and organization style dimension of the 7-S framework to be highlighted and integrated into the strategic system.

We come finally to the seventh ''S,'' shared values (or, as it was called in the earlier 7-S literature, super-ordinate goals). Vision, mission, value, and purpose statements are not explicitly recognized in an organization's BSC. These beliefs systems, though, should be the starting point, the jumping off platform, for developing the organization's strategy, which articulates how it will deliver on its mission and achieve its vision, while living its core values and statement of purpose. Some companies have put their shared values at the base of their strategy map, below the learning and growth perspective, to signal that these are the foundation for everything that the organization does. Similarly, they place the vision or mission at the top of the strategy map to signify that ultimately the success of the strategy will be judged by how it helps the organization achieve its vision and deliver on its mission.

Some organization establish explicit objectives and measures in the learning and growth perspective, as an organization capital component, for whether employees are aware of and understand the vision, mission, and values statements. They measure whether employees believe they practice the principles in these statements in the workplace, and, most importantly, whether they believe that their managers and co-workers are practicing these principles. Thus, the BSC can translate even the most intangible ''S'' of them all into quantifiable objectives that lead to action (education, training, and practice initiatives) and feedback.

Even though the two strategy implementation frameworks were developed completely independently from each other, the 7-S model and the BSC align remarkably well. Many

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organizations throughout the world are now using the BSC as their system for effective strategy implementation. The application of the BSC to diverse organizational units aligns companies' structure to business unit and corporate strategy. The learning and growth objectives integrate staff, style, and shared values to enhance organizational skills and critical processes in the internal perspective. Thus, one can view the BSC as the contemporary manifestation of the 7-S model, helping to explain its popularity as a practical and effective tool for aligning all the organizational variables and processes that lead to successful strategy execution.

Notes

1. Adapted from R. Waterman, T. Peters, and J. Phillips, ''Structure is not organization,'' *Business Horizons*, June, 1980, and J. Clued, ''Organizational alignment: the 7-S model,'' HBS Case 9-497-045.
2. This is a long-standing problem, as described by Steve Kerr, ''On the folly of rewarding A, while hoping for B,'' *Academy of Management Executive*, 1995, originally published in 1975; also R.S. Kaplan and H.T. Johnson, *Relevance Lost: The Rise and Fall of Management Accounting*, HBS Press, Boston, MA, 1986.
3. See R. Simons, ''Control in an age of empowerment,'' *Harvard Business Review*, March/April, 1995, pp. 86-8.
4. R.S. Kaplan and D.P. Norton, ''Measuring the strategic readiness of intangible assets,'' *Harvard Business Review*, February, 2004, and *Strategy Maps*, HBS Press, Boston, MA, 2004.
5. R.S. Kaplan and D.P. Norton, ''Measuring the strategic readiness of intangible assets,'' pp. 60-3; also *Strategy Maps*, pp. 275-316.