**The Importance Of Metrics**

Performance metrics are one of the main things that drive decisions and actions in a business. Your people understand the metrics that they are responsible to accomplish. That understanding, along with the review process that reinforces them, put the metrics upfront in the decision-making process used by individuals. They then act so as to improve the metrics. So, *the metrics better be the right ones*.

Most performance metrics used in companies today are from the financial statements or the cost accounting system. Not many companies go out of their way to collect other data – the existing data is used by everyone, and it seems to be correct. These metrics are accepted out of hand even though in many instances the metric seems to indicate the wrong answer or behavior is the right behavior. It is counter-intuitive or misleading.

For example, if an ops manager is able to reduce the labor it takes to complete different jobs in kitting, the number of labor hours will probably go down, saving labor expense. However, if overhead absorption is based on labor hours versus a plan, then the overhead will be under-absorbed, which is bad.

**Accounting Dominance of Metrics**

As stated above, many metrics are based on accounting numbers or standard metrics that come out of your ERP system. I call these, “standard metrics” which are responsible for average results in company. Some examples of metrics from the accounting/ERP systems include:

* Budgets and income statements:
  + Expense categories on the P&L
  + Accruals
  + Deferrals
  + Deferring expenses to inventory to abide by the accounting “matching principal”
  + Labor categories (direct and indirect, exempt or non-exempt, etc.)
* Cost accounting based metrics:
  + Machine and labor utilization
  + Depreciation
  + Overhead absorption
  + Gross margin/contribution margin
  + Rate per labor hour or machine hour
  + Cost of a PO, customer order, etc.

Most of these metrics are making management look in the wrong direction – focus on the wrong things. Just because a number can be calculated does not mean it is worthwhile. Typically, the accounting answer for metrics is to keep getting more detailed, often to the point that the intent of the metric gets lost. An example of that is activity-based costing (ABC), which puts a cost on virtually everything that is done in a business. These types of costs are completely irrelevant.

For example, the cost per purchase order is $100. Logic would suggest that should go down. But if a business starts using blanket orders, the cost will probably go up. An example of a detailed analysis of expenses, but unfortunately it is not only wrong, but it is irrelevant and misleading.

**Most Important Metrics**

Most important about safety, quality, and cash flow. Cash flow based metrics are almost never used in most businesses. In fact, management typically does not even review the statement of cash flows (one of the three main financial statements) each month, instead focusing on the income statement for 90% of the answers and the balance sheet for the remaining 10%.

Cash is king. How much you have in the bank and how much you generate per week or month is extremely important. How much time does your management team spend on truly understanding that? Profit is an accounting number that can have 20 different answers based upon how accounting rules are applied. Those 20 different numbers can vary significantly. So, which one is right? Why do you focus on making that better? Cash is more important. Ask your banker.

*In the next two articles I will explain why most traditional metrics are irrelevant and misleading. The second of these two articles will give replacement performance metrics that are much better in truly understanding what is happening in your business.*

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**About the Author:** Bob Krausert is the owner of STRATE***X***, a Twin Cities based firm that works nationwide. Bob is the author of the book, ***Extreme Lean***, published in 2018. Bob has worked with over 60 printing companies, mostly mid-sized companies, but also with larger companies like Jostens and Banta, now part of RR Donnelly. During his career, Bob has trained over 12,000 people at both public and private events. Bob has been working with PIM since 2010, periodically providing educational seminars for its members. Bob can be reached at [stratexlean20@gmail.com](mailto:stratexlean20@gmail.com) or by phone at 612-743-8706. If you would like to have a specific question or topic covered in one of the articles, feel free to make the suggestion!