The Basics of Key Performance Indicators (KPI)

https://www.thebalance.com/key-performance-indicators-2275156

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[Key performance indicators](https://www.thebalance.com/what-are-key-performance-indicators-2296142), also known as KPI or [Key Success Indicators](https://www.thebalance.com/critical-success-factors-in-business-2275171), help managers and employees gauge the effectiveness of various functions and processes important to achieving organizational goals.

**Some Examples of KPI**

KPIs are intrinsically linked to a firm's strategic goals and are used to help managers assess whether they're on target as they work towards those goals.

* A sales team might track new revenue, total revenue, new customer capture, average deal size, and deal pipeline size to assess progress toward corporate revenue targets.
* A customer support team might measure the average on-hold time for customers, as well as the percentage of calls that result in a high post call survey rating and overall [customer satisfaction](https://www.thebalance.com/monitor-customer-satisfaction-2275994).
* A marketing group will look at the contribution of marketing generated sales leads to total revenue over time to gauge their effectiveness.
* Other areas of the business will look at the efficiency of processes and various quality metrics.
* Human resources will look at employee engagement, employee turnover, time-to-fill open positions and other related metrics.

Managers and key stakeholders will monitor these indicators over time and adjust plans and programs as needed to improve the KPIs in support of the firm's strategic goals.

**Leading and Lagging Performance Indicators**

There's both art and science to the development of proper performance indicators. The objective is always to identify those measures that meaningfully communicate accomplishment of or progress toward key goals.

* **Some indicators are lagging indicators and simply tell you how you've performed**. Financial metrics are classic examples of these types of measures. They simply indicate results of past programs and campaigns. They have no value in predicting future performance.
* **Other measures are leading indicators offering guidance on future results**. For example, an improvement in employee engagement is likely to forecast improvement in many key indicators, including customer satisfaction, innovation and overall participation in running the business.

The goal is to have the right balance of both leading and lagging KPIs.

**Six Big Challenges in Developing Key Performance Indicators**

It takes considerable effort to develop a high-quality set of performance indicators. Managers and functional experts work together to propose a set of measures and to debate the relative importance of the various measures. A number of key challenges include:

1. If the firm's [strategy](https://www.thebalance.com/the-manager-s-guide-to-understanding-strategy-part-1-2276148) and key objectives are not clear, measures tend to focus on just financial outcomes.
2. Too much reliance on financial indicators offers a very imbalanced and incomplete view on the health of a business.
3. Measures deemed important by one area may not be viewed as important by others.
4. If compensation is tied to key targets for the performance indicators, this introduces a conflict of interest and considerable bias into the process.
5. Identifying leading indicators is a difficult process.
6. The ability to accurately measure and report on the identified measures may be difficult or impossible given internal reporting system limitations.

A healthy process for identifying and implementing key performance indicators involves the managers and contributors regularly revisiting and revising the measures.

This fine-tuning process takes time and diligence by all parties.

**The Proper Use of Key Performance Indicators:**

A properly developed and implemented KPI program incorporates regular review processes where managers and other stakeholders assess the meaning of the results. Improvement in employee engagement and customer satisfaction measures are positive, but diligent managers will assess the causes and impact of the improvements then decide how to continue to strengthen in these areas.

Similarly, a decline in sales results from the prior period or same period last year might be reasonably assessed as negative. However, the measures alone don't tell you what happened or how to improve. A set of proper sales-focused KPIs will include measures that showcase where conditions deteriorated and how likely they are to improve.

Armed with these insights, sales team members can take action to strengthen the leading indicators and drive improved future results.

**The Bottom Line:**

KPIs are much like instruments that measure temperature and barometric pressure. It might be interesting to know that the temperature increased or decreased, but it's more critical to know whether a storm is imminent. The measures work together to provide a more complete picture of the total situation.