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Reimagining the Balanced Scorecard for the ESG Era

by [Robert S. Kaplan](#) and [David McMillan](#)

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Summary.

Companies are increasingly aware that their customers and society in general expect businesses to adopt and work towards social and environmental objectives as well as the traditional financial ones. This involves not only re-evaluating firms' models but re-imagining new, more inclusive ecosystems from a multi-stakeholder point of view. In this article, the authors propose an update to the Balanced Scorecard, one of the most successful management tools of all time, so that it can better help align stakeholders coming from very different places around each other's goals as well as their own.

In August 2019, the U.S. Business Roundtable, the leading gathering for Fortune 500 CEOs, stated that "each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country." This re-orientation acknowledges widespread concerns that companies who focus only on their shareholders ignore and may even contribute to the societal problems of environmental degradation, growing inequality, and persistent poverty.

Many retail customers seem to agree. According to the New York University Center for Sustainable Business, virtually every product category saw consumer preference shift towards more sustainable products. 50% of CPG sales growth between 2013 and 2018 went to the 17% of products that advertised sustainable attributes, such as FairTrade sourcing. Following this logic, a chocolate company's value proposition to its customers would include not only delicious taste and texture but also certification of smallholder cocoa farmers' higher quality of life, reduced environmental degradation in cultivating the coca beans, and zero used of child labor.

Employees, too, want their companies to make socially responsible business decisions. Wayfair employees protested when their company began selling furniture to migrant detention centers. Amazon's employees objected when the company fired two employees who had advocated for greater safety precautions during the Covid-19 pandemic. Fulfilled workers are twice as likely to stay for five years at a company compared to those who work just for a weekly paycheck. Such loyalty benefits the company through lower recruiting and onboarding costs, stronger institutional memory, and employees better aligned to the business strategy.

Environmental and social factors also influence companies' decisions about supply chain partners. While global food companies may have great relationships with the large aggregators they directly purchase from, they usually have no knowledge about the living and working conditions of the multitude of local aggregators, cooperatives, and

smallholder farmers at the far end of their supply chains. With increased consumer advocates' demands for transparency and accountability, companies must shift from short-term purchasing decisions, driven mainly by price, into deeper, long-lasting relationships with pricing that promotes poverty alleviation among their primary producers; sustainable, carbon-neutral production and distribution processes; and safe and ethical employment practices.

The Rise of the Inclusive Ecosystem

All these changes fundamentally alter the way businesses work with customers, employees, suppliers, communities, and local governments. Traditionally, firms have acted as independent agents jostling for a share of the customer's wallet, and attempting to extract the greatest profit from their industry's value chain. Today, companies that want to meet both shareholder and societal expectations must work collaboratively with multiple and diverse players to implement "win-win" strategies that benefit all system participants.

In a 2018 Harvard Business Review article, Robert S. Kaplan, George Serafeim, and Eduardo Tugendhat illustrated how companies can join with other firms, non-profits, and communities in positive-sum networks that create economic value while simultaneously addressing poverty, social exclusion, and environmental degradation. Such collaboration can produce great benefits in the low to middle income countries where the most impoverished people live, socially excluded and surrounded by serious environmental damage. Inclusive growth strategies can also be applied in poverty-stricken and high unemployment regions of developed nations.

Companies that make such connections and co-create ecosystems that encompass the full range of potential stakeholders can produce transformational outcomes for those previously left behind by economic growth. As Kaplan et al described in their HBR article, AB InBev's Nile Brewery used its position as a key product off-taker to transform the maize farming ecosystem in Uganda. The new strategy enabled Nile Brewery to access high-quality and lower cost inputs, a local aggregator to increase its revenues by orders of magnitude, and local smallholder farmers to realize income gains of more than 100%.

The Challenge of the Triple Bottom Line

Companies that want to pursue inclusive growth strategies, however, must overcome the limitations of their accounting and control systems that prioritize only financial outcomes. The Balanced Scorecard (BSC) system overcomes the limitations of these traditional management systems by introducing two principal tools: the scorecard itself, which offers a framework for adding non-financial performance metrics to traditional financial ones, and the strategy map, which enables a visual representation among a company's multiple and linked strategic objectives. We have seen companies deploy these two tools, not only to enhance their own performance, but also to achieve alignment across organizational barriers, such as in customer-supplier relationships, joint ventures, and, more recently, in inclusive growth ecosystems.

At their core, strategy maps and scorecards describe causal chains up and down an organization, charting the stages through which final outcomes are achieved. The cause-

and-effect linkages start with how the organization's intangible assets of people, information, and culture, described within the *learning and growth* perspective, drive improvement in the critical *processes* that create the value proposition for the organization's *customers*. Customer success, in turn, translates into the ultimate outcome metrics of *financial performance*. Strategic objectives and associated performance metrics get defined within each of these perspectives.

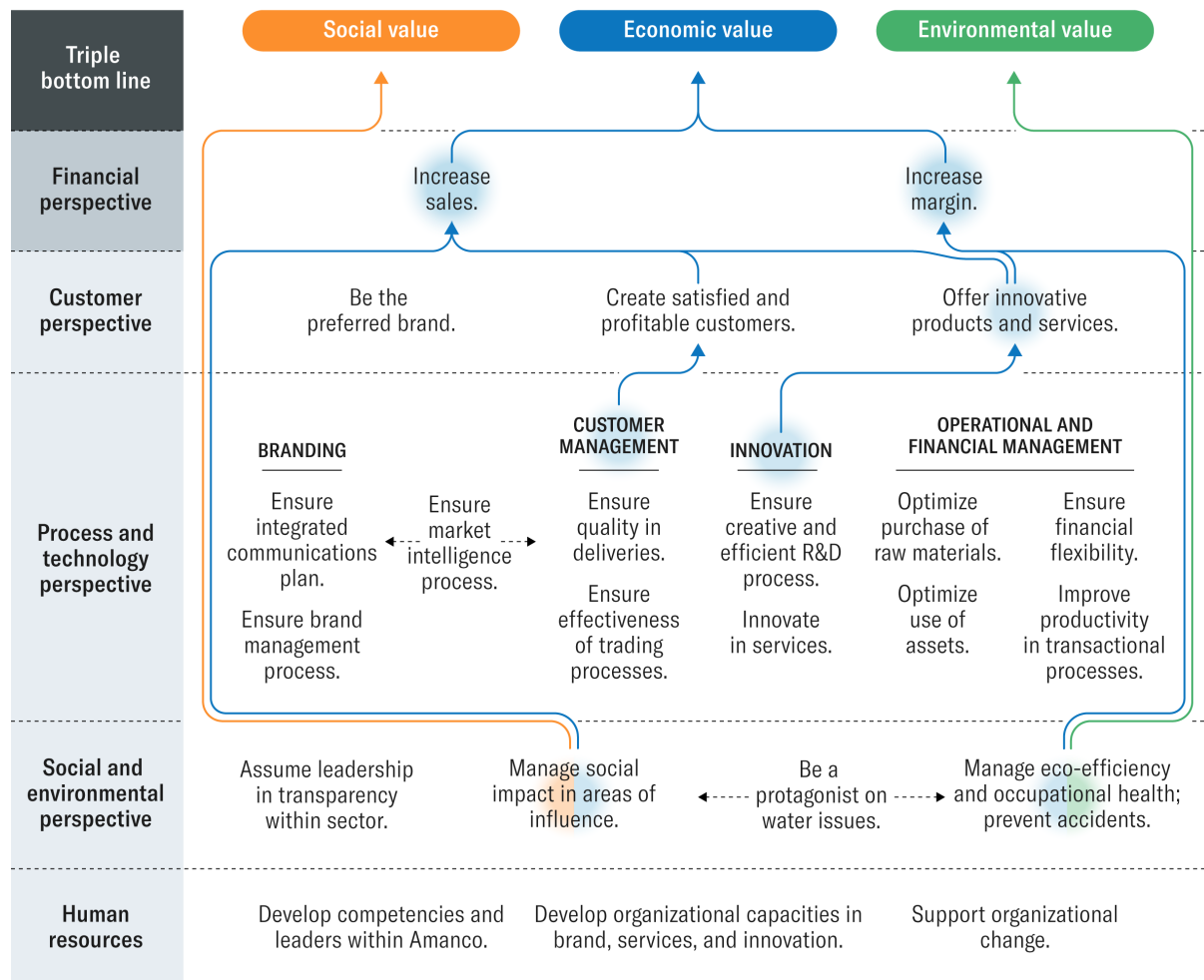
These four traditional BSC perspectives work fine in the commercial world, neatly capturing a company's long-term value creating business model, which is why it has proven to be so popular with businesses. And with minor modification, strategy maps and scorecards have also proved helpful in the public sector, particularly by introducing non-financial metrics that enable a government agency or NGO to be accountable for its performance for citizens and constituents.

Some companies adapted their scorecards to reflect their interest in pursuing triple bottom line strategies encompassing economic, environmental and societal performance. Take the case of Amanco, a Latin American producer and installer of plastic pipes for water treatment solution. The owner's mission for Amanco was to "profitably produce and sell complete, innovative, world-class solutions for the transportation and control of fluids, operating in a framework of ethics, eco-efficiency and social responsibility." He believed that the components encompassing triple bottom line performance were not in conflict; that the company's customers, which included local governments, wanted to purchase products that protected the environment and improved local communities.

Amanco built its strategy map to include environmental and social objectives in parallel with financial ones, and added a new perspective, as shown in Exhibit 1, to highlight processes that drove environmental and social progress.

Amanco's Triple Bottom Line Strategy Map

The financial perspective (traditionally the final value output) now has a triple bottom line perspective superimposed on top of it. This new perspective highlights the organizational processes required to drive social and environmental objectives as well as economic value. The causal linkages shown below illustrate some of the connections between strategy map objectives.



Source: "Amanco: Developing the Sustainability Scorecard," by Robert S. Kaplan and Ricardo Reisen de Pinho, January 2007 HBR

Managers at every level were held accountable for performance along the triple bottom line metrics. Putting the new objectives on the strategy map did not make them easy to achieve. But it did mean that any proposed investment or initiative would be assessed by its environmental and societal impact as well as its financial payback. This led to initiatives to train local dealers so they could help farmers in their region use Amanco products for sustainable irrigation. The company established relationships with financial institutions for farmers to access micro-loans, enabling them to purchase Amanco products, along with high-quality seeds, and sustainable fertilizer and crop protection products. Amanco also took the lead in having all companies in its industry pledge to eschew corruption and bribery of government officials, allowing competition to take place on a level playing field.

While we can celebrate Amanco's leadership and actions, our experience has been that actions by a single entity, whether private or public, are insufficient to transform the economic, environmental and social conditions in a region. With each player pursuing its own individual mission and objectives, the whole ends up less than the sum of its parts. Breakthrough performance in triple bottom line performance requires multiple players from multiple sectors to become *aligned around a shared set of desired outcomes*. These players include distributors, suppliers, local cooperatives, community-based organizations, public funding entities, and impact investors, and the community residents who are the ultimate beneficiaries from getting connected to global supply chains. The Balanced Scorecard (BSC), originally developed to describe and implement a single organization's strategy, needs to be adapted to reflect such multi-stakeholder strategies for triple bottom line performance.

Redefining the Scorecard Perspectives

Building upon the Amanco experience, we have relabeled the original top perspective on the strategy map from Financial to Outcomes to highlight the measurable financial, environmental, and societal benefits the inclusive ecosystem intends to achieve.

Beyond the financial benefits to each participant, which includes the smallholders and their families, the social component in the Outcomes perspective can include metrics for better health, education, and employment in local communities, and for improved women's roles and family cohesion. The environmental component can measure reduced deforestation, lower emissions of greenhouse gases, cleaner and more abundant water, and less soil degradation.

The single-entity Customer perspective becomes a Stakeholder perspective because each participant in the ecosystem must be treated as its "customer." The scorecard will reflect the value that each player expects to obtain from active participation. In a health system ecosystem, for example, the multiple customers include patients and their families, payers, physicians, communities, and the academics benefiting from the system's educational and research programs.

For an ecosystem to be aligned and effective, each player should know how all other stakeholders gain value from participating. That is why the first step in designing a new ecosystem requires mapping out the value creation process and how that value gets distributed among the multiple stakeholders. For example, the fruit import substitution strategy of one global beverage company we worked with identified agricultural input and service providers, farmers, fruit aggregators and processors, buyers (including itself), financial institutions, and the government as key stakeholders in addition to the customers it directly sold to. The perspective of each was reflected in the stakeholder perspective.

We have found it helpful to write each stakeholder's objective through the voice of the stakeholder. In a cocoa supply chain, for example, the farmer's objective could be written as "Help me receive a fair share of the value I create," and quantified with the metric, "percentage of smallholder farmers strongly agreeing with, 'I feel I am a partner in the cocoa business.'" Such farmers feel they are now a valued stakeholder in a profitable, ethical, and ecologically-sustainable supply chain. By writing stakeholder objectives in

this way, every stakeholder voice is heard and measured, and helps them see how their participation in the ecosystem contributes to the value it creates.

The one perspective that needs no redefinition is Process. This continues to include the critical activities that must be performed exceptionally well to deliver value to all stakeholders and that allow the triple bottom line objectives to be achieved.

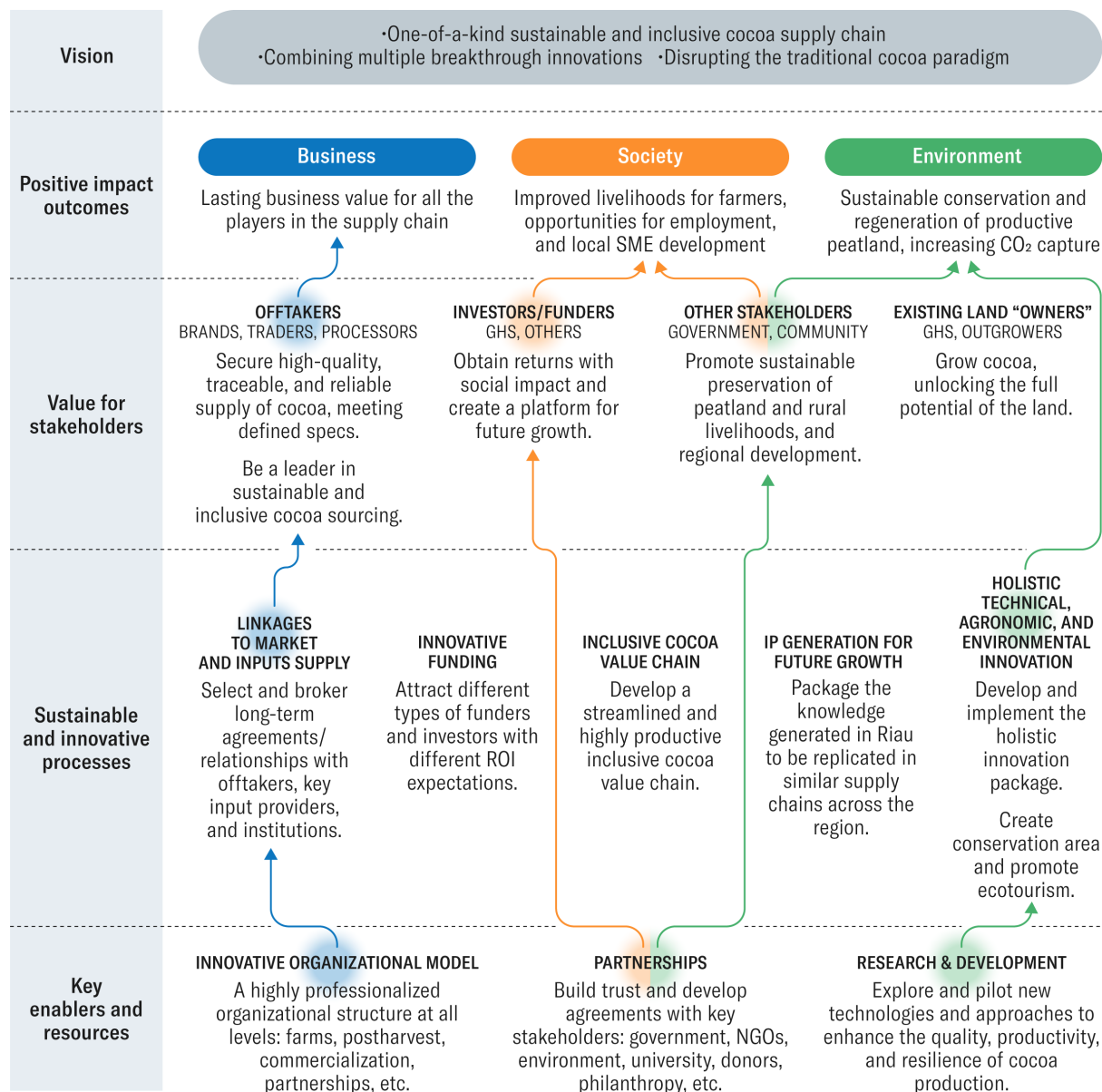
The final and foundational perspective of the new BSC, like the first two, needs to be expanded. Relabeled from Learning & Growth to Enablers, this perspective reflects the diverse capabilities, across all participants in the ecosystem, required for successful implementation. Many of them must be created jointly. These common capabilities include the raising and distributing of external funding, operating under a new governance structure, extensive and candid communication among all members, and a shared accountability for strategy execution and outcomes.

Mapping the Inclusive Ecosystem

The updated multi-stakeholder strategy map is a powerful tool to communicate an ecosystem's value creating process. As a specific example, consider the strategy map in Exhibit 2, which was created for the Riau Cocoa project of PT Guntunghasrat Makmur (GHS), part of the Sambu Group, the world's largest integrated coconut processor.

Riau Cocoa Ecosystem Strategy Map

This strategy map portrays how stakeholders across the new cocoa production ecosystem envisioned by PT Guntunghasrat Makmur (GHS) would work collaboratively to create measurable value for businesses, the environment, and society. The causal linkages shown below illustrate some of the connections between strategy map objectives.



Source: PT Guntunghasrat Makmur

HBR

GHS wanted to use the abundant but environmentally sensitive peat soil on its Indonesian plantation holdings to grow coca beans. GHS currently had 50,000 inefficient farmers harvesting and selling small quantities of coconuts at spot prices to local traders. The Riau Cocoa project would enable the farmers to diversify into coca bean production, enabling them to increase income by 60-70% per hectare and reduce their dependence on a single crop. The farmers would also have new job opportunities to work in the main plantation and/or in post-harvest facilities.

GHS's long-term offtake commitment for coca beans would provide financial security for local intermediaries to invest in post-harvest facilities and farm services, and also help farmers access financing to acquire seeds, fertilizer and technology. Training them to use modern agroforestry methods would make existing holdings of peat fields more productive and more sustainable. The strategy, while building upon existing relationships from the coconut business, still requires GHS to forge new relationships with (i) a large chocolate distributor to purchase the cocoa production, (ii) the government to validate the peatland preservation approach, and (iii) impact investors for project funding. The interests of all these stakeholders are represented on the Riau Cocoa strategy map.

The GHS project is currently a work in progress, but the company believes that the re-imagined version of the BSC system will be a necessary component for aligning all the stakeholders to succeed in new inclusive ecosystem. Three decades after its introduction, the BSC's intuitive and robust structure continues to be the dominant framework for a company's strategy execution and management-by-objectives systems. By evolving the Balanced Scorecard and Strategy Map's perspectives to reflect today's expanded role for business in society, we believe that the BSC will help businesses focus and deliver on society's expanded expectations for sustainable and inclusive economic growth.

Robert S. Kaplan is a senior fellow and the Marvin Bower Professor of Leadership Development, Emeritus, at Harvard Business School. His most recent HBR articles include: "[Inclusive Growth: Profitable Strategies for Tackling Poverty and Inequality](#)" (with George Serafeim and Eduardo Tugendhat), "[How to Pay for Health Care: The Case for Bundled Payments](#)" (with Michael E. Porter), and "[How to Solve the Cost Crisis in Health Care](#)" (with Michael E. Porter).

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