A STUDY ON LINKAGES AMONG BALANCED SCORECARD PERSPECTIVES: THE CASE OF INDONESIAN LOCAL BANKS

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Abstract

Ever since Kaplan and Norton introduced the Balanced Scorecard (BSc), as a performance measurement tool more than two decades ago, the framework received much attention regarding its applicability in many industries. The Banking industry, including local banks in Indonesia, also started to implement this tool. This research aimed to address the issues regarding performance management in the perspective of the bank and attempted the practicality of employing the Balanced Scorecard as a tool to improve performance management systems in local banks to achieve their strategic objectives. This research attempted to analyze the most effective variable of the Balanced Scorecard to achieve a strategic objective. The result will benefit local banks in Indonesia, particularly the bank studied to improve the most influential variable in order to gain a competitive advantage and finally become a regional champion as expected. Stepwise regression analysis was performed to investigate the relationships among the variables from the Corporate Strategy established by the Local Bank, wherein this strategy was composed by four perspectives of BSc and represent every existed division in the company.This regression test assessed any direct effects from each of the perspectives and compares the relative strength of the relationships among the four BSc perspectives. The result of this study finds that there is a strong relationship among the BSc perspectives proposed in the Corporate Strategy of the Local Bank.

Keywords: Balanced Scorecard; BSc relationship; Corporate Strategy; Local Bank

1. Introduction

Performance management has become an increasingly popular topic. One of the most common frameworks of performance management system is Balanced Scorecard that was introduced by Kaplan and Norton in the 1990s. In both research and practice, the BSc has received much attention, particularly as a tool for driving unit level strategy within many industries, including hospitality, health, manufacturing and banking (Ashton, 1998; Kaplan et al., 2001). It is indicated that the Balanced Scorecard is applicable in the finance industry, particularly banking. Some of international banks have successfully utilized Balanced Scorecard in order to improve their performance.

The banking sector has started adopting comprehensive performance systems like the Balance Scorecard to exhibit stakeholders that this sector provides performance information regarding financial and non-financial measures. It was designed as a tool to analyze the performance of Bank's strategy that can be further maintained as fundamental requirements to gain a competitive advantage in the industry.

This research is aimed at addressing the issues regarding performance management with the perspective of the bank and attempted the practicality of employing Balanced Scorecard as a tool to improve performance management systems in local banks to achieve their strategic objectives.

2. The Problems of Performance Management in Local Banks

With the rapid growth of the banking industry, local bank are dealing with intense competition. Based on the Association of Local Bank (ASBANDA) in Indonesia, local bank find difficulties to compete against commercial bank in each region. Further, ASBANDA established a joint program called Local Bank Regional Champion (BRC) to encourage local banks in Indonesia to be more competitive and become a regional champion comparable with commercial banks.

In order to obtain this BRC objective, ASBANDA has indicated four comparative weaknesses of the local bank that needs to be improved, such as: (1) Human Capital, (2) Credit Loan, (3) Recording Governance System, and (4) Performance Management System. Related to the fourth aspect, Performance Management System, BRC suggested that local banks start to implement the Balanced Scorecard as tool to improve current performance systems to achieve their strategic objective.

This research is aimed to analyze the most effective variable of the Balanced Scorecard to achieve strategic objective. The result will help benefit local banks in Indonesia, particularly the bank studied to improve the most influential variable in order to gain a competitive advantage and finally become a regional champion as expected.

3. Implementation of the Balance Scorecard and Performance Management Systems At Local Banks

A. The Basic Theory of Balance Scorecard

Balance scorecard is a strategic management system that helps organizations to identify strategies and make it executable (Braam&Nijssen, 2004; Chen, Chen&Peng, 2008). BSC was devised and designed by Robert Kaplan of Harvard University and David Norton, who was working as a consultant in the Boston area in 1992 (Kaplan&Norton, 1992). Kaplan and Norton thought that measuring financial performance is not enough and affected the companies' ability to create value These companies must also concern itself with issues relating to the customer, internal processes and commercial matters relating to staff and stakeholders can effectively contribute to the assessment of organizational performance. Kaplan and Norton called this tool the "Balance Scorecard"(Kaplan&Norton, 1996; Feizi&Solukdar, 2014). Balance scorecard has several particular functions such as (Sharma, 2009):

- Translate vision and strategy;

- Defines the strategic linkage to integrate performance across organizations;

- Communicates objectives and measures to a business unit, joint venture, or shared service;

- Aligns strategic initiatives;

- Align everyone within an organization so that all employees understand how and what they do supports the strategy;

- Provide a basis for compensation; and

- Provides feedback to the senior management if the strategy is working

Balanced Scorecard has four perspectives;
- Financial perspective

- Customer perspective

- Internal business perspective

- Learning and growth perspective

Four perspectives from the balance scorecard were assessed to see if these companies are fit and proper to generate profit. This is because all perspectives from balance scorecard representing relationship analysis both from internal and external factors directly to business. In terms of building the strategy, balance scorecard transforms the strategy objectives of the company into the strategic level with assessment of performance organization (Yansheng&Longyi, 2009).

B. BSC Performance Management System Model Related with Bank Industry

Similar to other industries, banks can not only focus on financial perspective, they need to evaluate their   performance activities and to assess the achievement of strategic objectives (Secme, Bayrakdaroglu&Kahraman, 2009). When competitiveness is increasing, banks need to be able to find their competitive advantage to evaluate the performance of the organization and find the appropriate ways (Wu, Tseng&Chen, 2009). Bank has special ways to analyze and evaluate their performance activities with specific calculation or framework. Otherwise, the framework design is able to set it as a tool to analyze the performance of the Bank's strategy is one of the fundamental requirement (Jiang&Liu, 2013). The implementation of Balanced Scorecard in Bank as follow:

Financial perspective. In the Balanced Scorecard framework, financial perspective acted as a parameter of the organization result. Bank in particular, have many financial indicators measured to define which indicators are parts of the chain that caused and affected existing strategic objectives (Rostami, Goudarzi&Zaj, 2015).

Customers. Banking industry has high sensitivity in customer satisfaction, and it is also applied in the local bank. Despite of local bank already having a major customer such local government, which reflects no significant threats of decreasing customers. It is not like local banks to put aside the main objective ofimproving their customer satisfaction. However, local bank needs to concern on other factors in customer perspective such as customer retention rate, customer profitability level and market share (Yansheng&Longyi, 2009).

Internal business process. In the internal business process, it is related to operation excellence and improvement. The main purpose from internal business process improvement is to meet the requirement of shareholders, especially in financial returns, and for stakeholders in terms of customer need and requirements (Perlman, 2013).

- Learning and growth. Similar with commercial bank, local bank needs to consider their learning and growth as an investment for the long-term performance. The concern is not only for ability improvement, but focus is on implementation of information system integration, and being vision of the company (Perlman, 2013).

C. Performance Indicator at Local Bank

There are five principles of successful organizations emerged from Kaplan and Norton's research on successful balanced scorecard users. These key elements of building an organization able to focus on strategy and deliver breakthrough result (Sharma, 2009), they are;

- Mobilize change through executive leadership;

- Translate the strategy into operational terms;

- Align the organization to the strategy;

- Make strategy everyone's job and

- Make strategy a continual process.

These principals lead to the establishment of performance indicators that have been implemented in various industries, including banking industry. Most of the bank (commercial bank, local bank, etc) determine the variable and indicators which are suitable to their strategy as seen in the picture below:
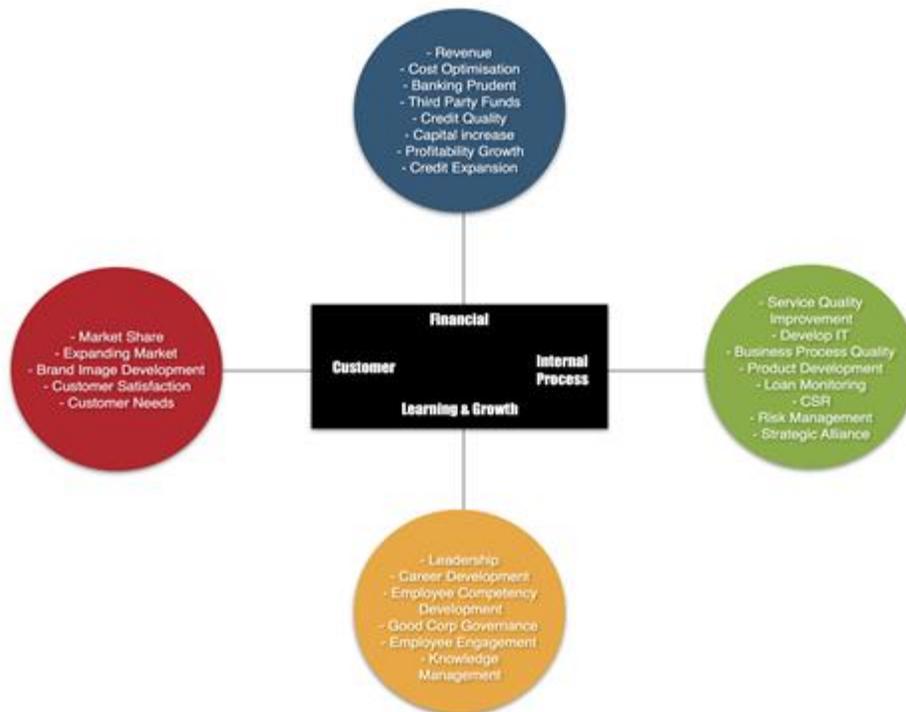
Figure 1.1. Common Indicator Performance at Bank Source: Authors (2015)

D. BSC Implementation at Local Bank

The local bank determines their strategy projection that disembogues from the consolidation strategy of product innovation, operation excellence, market penetration and market development. In term of product innovation, local bank purposes to improve markets through either innovation development of existing product and services, creating the new product and services, or both.

Regarding the operation excellence in local bank, their mission is to keep the profitability rate by conducting the efficiency in whole area. While market penetration is associated with leverage, the market with extra marketing efforts in the existing market is successful. For the last aspect, market development in local bank is related to aiming for potential market.

The strategy projection was composed from many direct factors to local bank such as scope, time, measurement, objectives and the operation processes. The Figure below illustrates the linkage using a subsample from the Corporate Strategy established by the Local Bank team, wherein composed by four perspectives of BSc and represent every existed division in the company
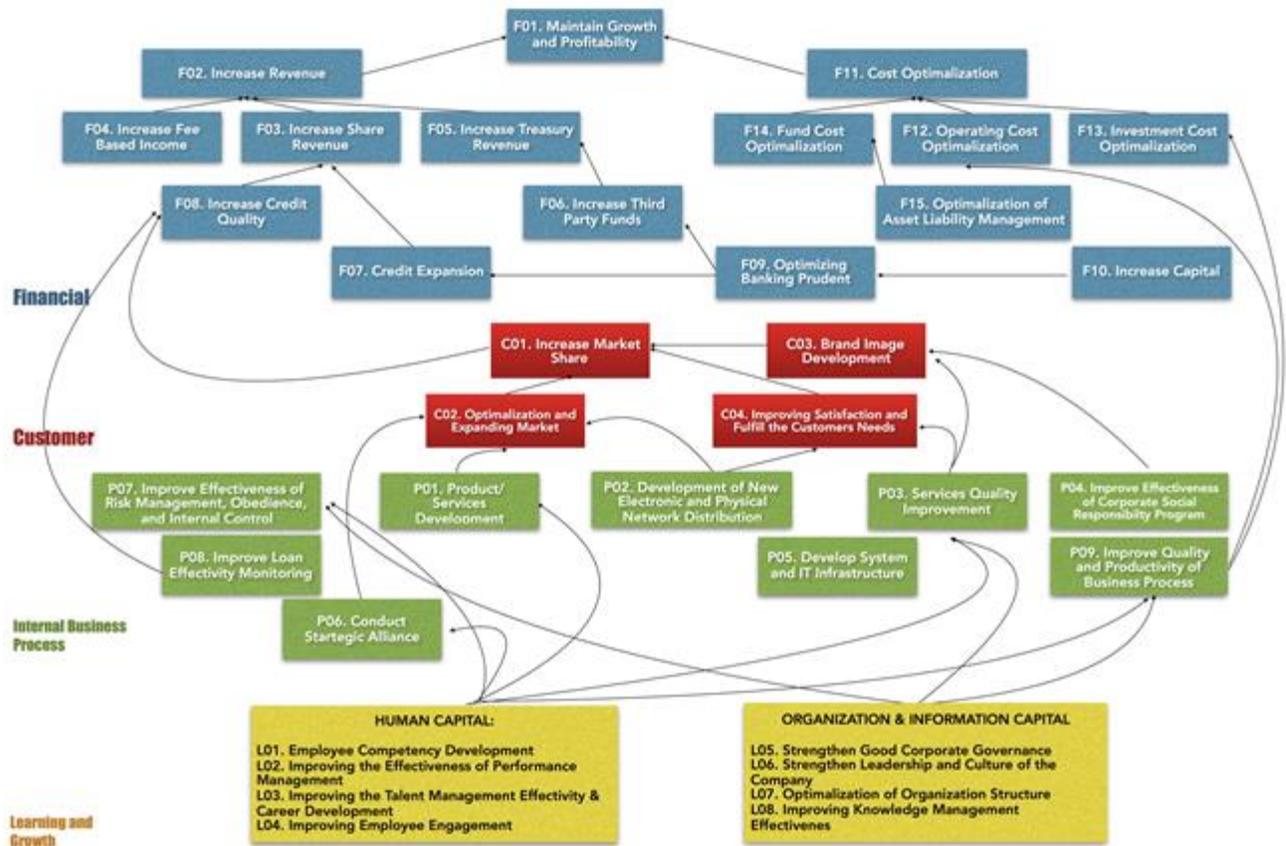
Figure 1.2 Local Bank Corporate Strategy
Source: Authors (2015)

4. Research Methodology

In this research, authors tried to calculate the relationship between variables that come from different perspective from Corporate Strategy established by the Local Bank team, to indicate which strategic objective that most optimal to achieve profitability of local bank. Based on the above discussion, authors formulated the following hypotheses as illustrated in figure below:
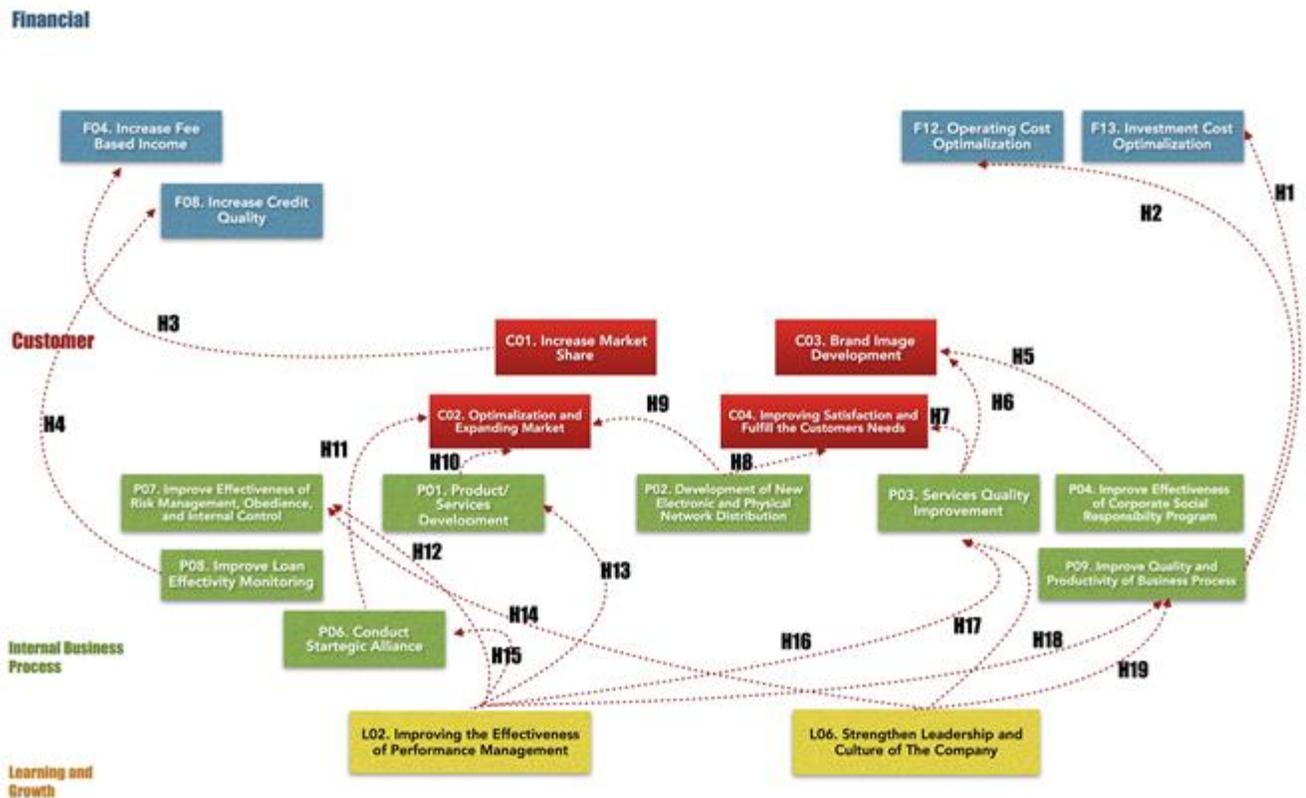
Figure 1.3 Hypothesis Based on Local Bank Corporate Strategy
Source: Authors (2015)

According to the above figure, this research is aimed at formulating 19 hypotheses that the relationship would be assessed and tried to indicate the strongest influential strategic objective. The Independent variable in this Local Bank Corporate Strategy is Learning and Growth, Internal Business, and Customer Perspective. Special case for Internal Business and Customer Perspectives, these variables functioned both as an independent variable and dependent variable (affecting and affected). Meanwhile, financial perspectives on this research are dependent variables (as a goal of strategy), which means it is affected by other perspectives.

Furthermore, after ascertain every existed variables, Expert Judgment Method was implemented in order to figure out measuring instrument that is most applicable for every strategic objectives. Expert Judgment collected from Chief Executive Office (CEO) of the Local Bank combined with head division of related Corporate Strategy.

Authors performed stepwise regression analysis in order to comprehend more about the relationship between several independent or predictor variables and a dependent or criterion variable and to investigate the relationships among the variables described in Figure above. In Stepwise regression analysis, variables stated to have relationships when the result of the value is above 0.5 (<0.5). This regression test assessed any direct effects from each of the perspective, and compares the relative strength of the relationships among the four BSc perspectives.

5. Result and Discussion

In this research, the hypothesis of the Corporate Strategy at local bank consists of several variables that is linked around BSc perspective at the local bank. To achieve the final result of this research, the data from local bank calculated uses stepwise regression among perspectives. There are 19 linkage measured using this method, and resulted as follows:

Table 1.1 Regression Value

Linkage	Variables		Adjusted R Square Value
	Independent	Dependent	
H1	P9	F13	0,586
H2	P9	F12	0,96
H3	C1	F4	0,882
H4	P8	F8	-0,038
H5	P4	C3	0,829
H6	P3	C3	0,344
H7	P3	C4	0,815
H8	P2	C4	0,843
H9	P2	C2	0,937
H10	P1	C2	0,886
H11	P6	C2	0,843
H12	L2	P7	0,723
H13	L2	P1	0,832
H14	L6	P7	0,76
H15	L2	P6	0,785
H16	L2	P3	0,734
H17	L6	P3	0,785
H18	L2	P9	0,730
H19	L6	P9	0,769

Source: SPSS 22 Result processed by Authors

Based on the above table, from 19 perspectives that have been calculated, there are two variables that have adjusted ratio less than (<) 0.5. Those variables are P8 (Improve Loan Effectivity Monitoring) towards F8 (Increase Credit Quality) and P3 (Services Quality Improvement) towards C3 (Brand Image Development). This result means that these factors do not contribute significant impact to Strategic Objective.

Meanwhile, the other 17 hypotheses occurred linkage variables that have adjusted ratio more than (>) 0.5 which means independent variable proved influenced dependent variable. Refer to to these finding, local bank can compare the value of variables in the same perspective. The value of each variable can be stated as follows:

Table 1.2 Independent Variables Average Value

Perspective	Independent Variables	Dependent Variable	Adjusted Rsquare Value	Average Value
Learning & Growth	L2. Improving the Effectiveness of Performance Management	P7. Improve Effectiveness of Risk Management, Obedience, and Internal Control	0,723	0,761
		P1. Product/ Services Development	0,832	
		P6. Conduct Startegic Alliance	0,785	
		P03. Services Quality Improvement	0,734	
		P09. Improve Quality and Productivity of Business Process	0,730	
	L6. Strengthen Leadership and Culture of the Company	P7. Improve Effectiveness of Risk Management, Obedience, and Internal Control	0,760	0,771
		P03. Services Quality Improvement	0,785	
		P09. Improve Quality and Productivity of Business Process	0,769	
Internal Process Business	P1. Product/ Services Development	C02. Optimalization and Expanding Market	0,886	0,886
	P02. Development of New Electronic and Physical Network Distribution	C02. Optimalization and Expanding Market	0,937	0,890
		C04. Improving Satisfaction and Fulfill the Customers Needs	0,843	
	P03. Services Quality Improvement	C03. Brand Image Development	0,344	0,580
		C04. Improving Satisfaction and Fulfill the Customers Needs	0,815	
	P04. Improve Effectiveness of Corporate Social Responsibilty Program	C03. Brand Image Development	0,829	0,829
	P06. Conduct Startegic	C02. Optimalization	0,843	0,843

	Alliance	and Expanding Market		
	P08. Improve Loan Effectivity Monitoring	F08. Increase Credit Quality	-0,038	-0,038
	P09. Improve Quality and Productivity of Business Process	F12. Operating Cost Optimalization	0,960	0,773
		F13. Investment Cost Optimalization	0,586	
Customer	C01. Increase Market Share	F04. Increase Fee Based Income	0,882	0,882

Source: SPSS 22 Result processed by Authors

Furthermore, from the table above, there are two linkage that have a high score. The relationship between P9 (Improve Quality and Productivity of Business Process) towards F12 (Operating Cost Optimalization) and relationship between P2 (Development of New Electronic and Physical Network Distribution) towards C2 (Optimalization and Expanding Market) has strong relationship. It means that improving these two factors could drive significant benefit for local banks in terms of developing their competitive advantage in the market.

In accordance to table 1.2, local bank able to define which perspective have significant impact on Corporate Performance. In learning and growth perspective, Improving the Effectiveness of Performance Management influenced five variables in internal business process and have 0.761 average value. While in other terms, Strengthen Leadership and Culture of The Company influenced three variables in internal business process but has higher average value with 0.771. Because of considerations on management with respect to investment, local bank shall concern on Improving Effectiveness of Performance Management because it has lower value and influence five other variables.

In terms of Internal Business Process, there are seven variables that have impact on customer perspectives, while the other three variables have impact on financial perspective. Moreover, the result also indicated that the Development of New Electronic and Physical Network Distribution is the highest variable with average value 0,89 in business process perspective. It means that these aspect have strong impact in internal business process, rather than other aspects in this perspectives.

Conclusion

This research aimed to analyze the relationship of non-financial perspectives to financial perspectives in BSc framework in Corporate Strategy of Local Bank. This research indicated that from 19 variables in hypotheses that been measured in this research, only 17 variables significantly influence local bank performances. Moreover, this research also provides information about the key variable of Local Bank that should be optimized in order to improve performance of the company.

Furthermore, this research generated evidence that Corporate Strategy could help company to determine the linkage among BSc perspectives. The Expert Judgment Method contributed to this research in terms of variable formulation.

However, this research has several limitations related to limited number of variable measured and specifically implemented in bank industry. Further research for other industries is recommended to enhance understanding about the application of BSc. Additional measures for the variables and different methodology also could be use in further research.

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