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Performance measurement under Balanced Scorecard: the case study of a Co-operative Credit Bank in Piedmont.

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Keywords: performance measures, balanced scorecard, strategic map, bank, co-operative credit.

Abstract

This paper aims at studying the implementation of a management control system in a Piedmont Cooperative Bank: the system is based on Balanced Scorecard model (BSC) suggested by Kaplan and Norton (1996, 2001) applied in the services sector.

The paper starts with the research method and the theoretical background concerning the business model of Cooperative Banks.

Next section is devoted to the presentation of the case study: specifically, the section outlines the competitive position and the organizational structure of the bank, that is wide spread in Piedmont (North of Italy), compared with the other main Cooperative Banks in Italy.

The section includes short comments about the bank's control needs, also considering Risk Management and the way Basel 2 Accord has caused a more extensive need of managerial information.

The following section contains

- the design of the BSC for the bank (corporate) and for the bank's branches (organizational units);
- the operative tools required for the implementation of the system (e.g. current and future performance measures under the different perspectives of BSC);
- the main critical aspects connected to the implementation of the control system itself.

The results obtained confirm the need of a control system based on a comprehensive framework that translates company's strategy into a coherent set of performance measures for the bank (corporate) and, as a consequence, for the bank's branches (organizational units) as well.

The paper ends with conclusions, especially regarding the care required in choosing the suitable operative tools to translate BSC into practise, implications and suggestions for future researches.

1 – Introduction¹

The paper concerns the implementation of a management control system in a co-operative bank located in the North of Italy in Piedmont region.

The co-operative credit banks are generally small in size and work in a local area: at present this is a limit because they work in a more and more dynamic and competitive environment characterized by international companies that can easily reach economies of scale and scope.

In the past banks worked in a stable and protected market, they played a key role in the financial market and had a strong control over competitive relations, but, nowadays the environment has changed: competition's degree has increased, stakeholders' needs are more customized, clients are better informed, therefore banks are required to develop competitive advantages (Porter 1985).

To survive in the long term and be competitive in dynamic businesses, it is important to improve instruments to analyze, forecast and influence the competitive environment. Each bank needs correct and well-timed information and, above all, instruments to estimate alternatives, to control actions and correct deviations (Amigoni, Miolo Vitali 2003; Brusa 2007).

The aim of the paper deals with the implementation of a Balanced Scorecard model for the bank (the corporate) and for its branches, considering the difficulties connected with the alignment of the organizational units to the strategy (Kaplan and Norton 1996; Brusa 2007).

Therefore, there is the identification of the operative tools needed to translate the model into practise, especially the set of performance measures for the bank and its branches.

In the following paragraph the empirical research method will be presented.

¹ This paragraph is by Paola Vola.

2 – The research method²

The research has been conducted through an empirical analysis of exploratory case study. The choice of a case study is one of the most appropriate method of empirical inquiry, because qualitative studies are necessary where organizational processes are involved.

Case study research excels at bringing us to an understanding of a complex issue or object and can extend experience or add strength to what is already known through previous research.

Case studies emphasize detailed contextual analysis of a limited number of events or conditions and their relationships. Researcher Robert K.

Yin defines the case study research method as an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly (Yin, 1984).

A strength of the case study method is that the emergent theory is likely to be testable with constructs that can be readily measured and hypotheses that can be proven false. Measurable constructs are likely because they have already been measured during the theory – building process.

The resulting hypotheses are likely to be verifiable for the same reason (Huberman, Miles 2002) .

The results are based on interviews with branches' managers. The interviews were semi-structured to be kept within the main question area but still open the possibility to get the interviewees own ideas and feelings. The interviews also included some questions to verify the good quality of answers.

The choice to examine a cooperative bank is supported by the fact that cooperative banks are an important part of many financial systems and the literature devotes disproportionately little attention to cooperative banks in comparison with commercial banks. Moreover, the share of cooperative banks has been increasing in recent years. Cooperative banks are particularly numerous and large in Europe.

The five largest cooperative banks in the European Union (EU) rank among the EU's top 25 banking groups in terms of consolidated equity. Reflecting the cooperative banks' focus on retail banking, their market share in retail business is even more substantial: for example, five EU member countries have more than a 40 percent market share of cooperative banks in terms of branch networks (Heiko Hesse and Martin Èihák, 2007).

The gathered issues, analyzing this cooperative bank, are largely present in the most of Italian cooperative banks, consequently this research is to a relevant degree generalisable.

² This paragraph is by Laura Broccardo.

3 – The case study

3.1 – *The business model of the Cooperative Banks*³

Co-operative credit banks are non profit entities which provide credit and financial services to the local community, especially households and small to medium enterprises.

These banks were born as Rural Banks at the end of 19th century to help craftsmen and farmers who were subjected to poverty and usury. Their aim was to enable as many people as possible to obtain loans at more favourable conditions than those offered by traditional banks.

Since 1994 the co-operative bank law has introduced changes that can be summarized as following:

- loans were available not only to craftsmen and farmers but to anybody in need;
- the majority of loans have to be mainly granted to members;
- the minimum number to establish a co-operative credit bank is 200 members;
- each member can own more than one share but the overall nominal value of the shares may not exceed 50.000 Euros; despite the number of shares owned, each member has only one vote;
- co-operative credit banks must allocate at least 70% of net profit to statutory reserve not subjected to distribution; 3 % of net profit must be invested in a special mutual-aid fund to promote and develop the co-operation.

If it's true that these banks can provide the same products as other banks, it's also true that there are some differences between banks in general and co-operative banks that can be identified with the orientation towards solidarity and support to local economy.

Since the beginning, co-operative credit banks have maintained a close link to the local area where they operate.

Therefore, it's possible to identify the main characteristics of this kind of banks; in fact they are :

- co-operative: they mainly provide credit to their own members;
- local: they play a role in providing financial support for households and enterprises in a geographically limited area;
- solidarity-oriented: they promote mutual aid between members. One of the main aims of this kind of bank concerns the supply of goods, services and work to members at more favourable conditions than those of the market. The mutual aim has to be mainly carried out to benefit members (the credit is mainly supplied to members);
- part of a system: they are part of a system of partnership so called co-operative credit which enables each bank to obtain services, products, economies of scale, therefore offering a high-standard range of services to their customers.

³ This paragraph is by Elisa Truant.

Nowadays the co-operative credit is composed by 438 banks (the 54,3 % of Italian banks) with a widespread presence throughout Italy.

3.2 – Brief history of Bank A

Bank A was born at the end of 1998 after a merger with three local banks. The three banks were founded at the end of XIX century and have always been a reference point for the support and the development of local activities.

The merger has allowed operational and financial dimension achievement which enable Bank A to face the strong competitiveness that characterises the co-operative credit market.

In fact this credit market is players are both local and international. The merger has enabled a capillary presence in a specific geographic area (Piedmont).

The local development has been planned to reach the following targets:

- increase of presence in the original area by opening new branches;
- extension of the presence in new areas by opening of a secondary office in Turin and new branches near Turin (Piedmont).

Thanks to this expansion the Bank area has grown: nowadays Bank A operates in 130 municipal areas.

The year after the merger was a year of adjustment (a lots of branches' directors resigned because they didn't believe in the new project). It was necessary to find the directional and organisational stability again.

The development and the growth began in 2000 thanks to the fact that targets in strategic planning were reached. Some of the most important targets reached are the following:

- presence consolidation in the local community;
- an increasing number of members: nowadays Bank A is one of the most important co-operative banks in Italy regarding the number of members thanks to innovative services that it offers. In fact the number of members grew from 5.278 units in 1994 to 23.846 units at the end of 2007 (+351%);
- this increase is due to the fact that membership has been open to all social categories;
- in 2007 the number of members has grown to 7%;
- extension of product range.

The following exhibit, Exhibit 1, explains the competitive position of Bank A, compared to other co-operative credit banks in Northern Italy for the year 2007.

The sample examined is made up of 26 co-operative credit banks in Northern Italy.

The following table contains the calculations of the most important position's indicators.

Exhibit 1 – Structure and performance of Bank A.

BENCHMARKING	MEDIAN	MEAN	BANK A.	RANKING	% BANK A. (-) MEDIAN
CLIENT COLLECTION / 000	861.271	1.030.124	1.344.438	3	56,10%
TOTAL ASSETS / 000	1.037.692	1.248.877	2.233.937	5	48,00%
EQUITY / 000	121.884	143.687	167.719	14	0,00%
EBITDA / 000	12.908	14.302	23.193	10	10,40%
NET PROFIT / 000	12.571	13.976	19.568	13	5,80%
N. OF COUNTERS	26	29	47	2	69,20%
N. OF EMPLOYEES	226	255	383	3	48,70%
COST/INCOME RATIO %	65	63,3	68	18	4,40%
EQUITY/TOT ASSETS RATIO	11,80%	11,90%	7,50%	26	-3,80%
R.O.E.	10,50%	9,90%	12,90%	9	0,50%
NET PROFIT / EBITDA RATIO	0,97	1,14	0,85	17	-3,40%
COLLECTION / COUNTERS RATIO	32.699	35.378	30.555	14	-6,60%
COLLECTION / EMPLOYEES RATIO	3.899	4.093	4.001	11	2,60%
EMPLOYEES / COUNTERS RATIO	8,8	8,7	7,6	4	-13,00%

Source: personal elaboration based on internal data.

For each indicator mean and median have been calculated paying particular attention to the position of Bank A compared to the sample and the median variance.

Bank A is one of the most important co-operative credit bank in the North of Italy for dimension of client collection, number of employees and number of counters. In fact Bank A is the second co-operative credit bank for the number of counters and the third for the client collection and number of employees. However these results are not lacking in consequences:

- the high number of counters involves a lack of efficiency in collection: the collection per counter is lower compared to the median (-6,60%), so Bank A is fourteenth in the ranking;

- the difference between the number of employees per counter of Bank A and the median is negative (-13%). However, even if the median variance is negative, Bank A is fourth in ranking;
- the low number of employees per counter involves a collection per employee higher than the median, even if the number of counters is high.

A further consideration about Exhibit 1 is that Bank A has a low equity, compared to the total assets too.

The equity of Bank A is 167.719 Euros and this figure puts it the fourteenth position in ranking.

3.3. - The organizational structure of Bank A⁴

The organizational dimension is crucial for the implementation of an effective control system: in fact, besides the quantitative data required by a management control system, the organizational dimension is necessary for the definition and the allocation of the economic responsibilities through the whole organization (Lorsch 1970; Brunetti 1992; Brusa 2000).

The term structure is usually referred to organizational elements such as the degree and the type of horizontal differentiation, vertical differentiation, mechanisms of coordination and control, formalization, and centralization of power (Mintzberg 1979).

As far as concerns the structure of the Bank A, after the merger a process of re-design of the organizational structure was necessary.

These activities led to a new structure's chart, that contains:

General Division (with Directors) and Staff Units (General Secretary, Organization and Human Resources Unit, Planning and Control Unit)

Auditing Board

Central Departments:

Sales Department

Local Branches

Internal Auditing Department

Technical Department

Credit Department

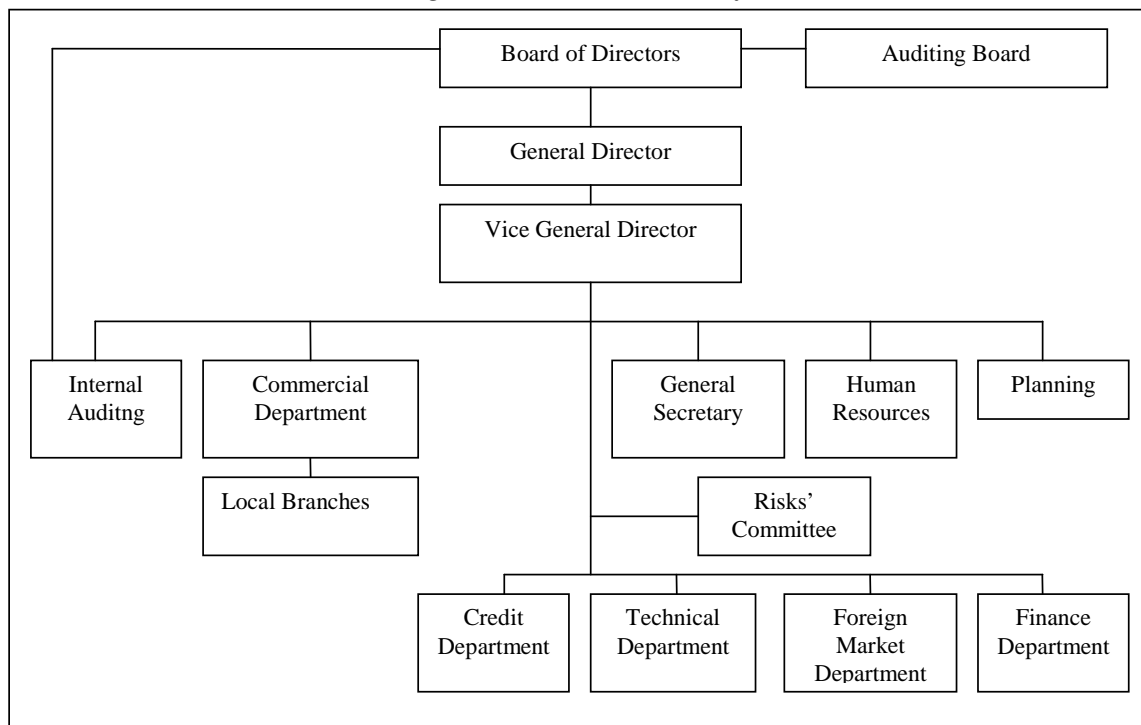
Finance Department

Foreign market Department

The structure can be represented as follow:

⁴ This paragraph is by Paola Vola.

Exhibit 2 – Organizational Structure of Bank A.



Source: personal elaboration.

The new structure corresponds to a “short bank”. There is a decentralization of the decisional power, in order to obtain a more rapid flow of information and, therefore, a more effective structure, oriented to the market.

The main goals to reach through the re-design of the structure were the following:

- the development of the foreign market, thanks to the implementation of a proper service;
- the empowerment of the selling department, especially with reference to the sales of financial products;
- the empowerment of the control and organizational activities, considering the limits imposed by the National Authority (Bank Supervision), in order to guarantee the identification of the risks of the bank’s activity, the quality and security of operational processes;
- the improvement of the planning and control management activity, with the aim of monitoring the economic and financial performance of each division and product.

In the due course, the focus will be on the Corporate and the local branches.

4 – The comprehensive measurement control system for the Bank A⁵

⁵ This paragraph is by Laura Broccardo.

The banks are facing innovation process that involve all the market's system. In fact, in the last years, we can observe some radical changes like globalization of financial market, innovation of financial products, new provisions and changes in the customers' behavior.

So also banks have to use managerial tools that enable themselves to control each success key factor.

It occurs a comprehensive measurement system to estimate every improvement in order to understand the effect on the business activities, employed resource and reached results.

It's very important to adopt an effective the management control, because it's a tool that permits to consider the most important variables to help the bank in the decisional process. The aim is to manage the bank with more awareness and rationality.

Comprehensive management systems, in fact, should derive from company's strategies and capabilities: they could allow the company to measure performances not only from a financial point of view (Kaplan and Norton, 1996).

Also for Bank A, in the last years, comprehensive management control systems assumed greater importance, considering new rules that Basel Accords imposed.

Basel 2 Accord establishes:

- minimum assets requirements;
- prudential control of assets appropriateness;
- enforcement of the control role on intermediaries' behaviour played by markets.

The minimum assets requirements is referred to the assets coverage: the goal is to guarantee more sensibility to risks. Every issue of a loan generates a cost for the bank in term of capital reserves needed.

The Accord, with the prudential control of assets appropriateness, considers also the riskiness of the invested capital; in fact more risky is the loan, greater are the possible losses for banks and, as a consequence, greater must be the capital reserves.

Naturally these reserves are a cost for banks that have to be regained by the interest rate applied to loans.

Considering all these elements, correctly Basel 2 Accord imposes to identify the credit risk and so to analyse the solvency capability of each customer that requires loans.

But there are some problems applying these rules, especially regarding the collection of information needed to build an internal rating system referred to the Bank's A customers.

In particular small and medium banks, like Bank A, have not the possibility to acquire evolved procedures of risk management.

There is also another problem bound with internal rating. In fact the rules, imposed by Basel 2 Accord, frequently led to consider the main customers of these banks risky.

As a consequence, Bank A could be forced to reduce the credit for these customers or to increase the interest rate on those loans.

In the past, Bank A, as the other co-operative banks, granted loans to customer considering different element such as their relationship with the bank, their reputation and the personal knowledge of the customer. It's true that also objective standards were important, but they were not crucial as now that Basel 2 Accord has imposed new limits.

At present Bank A has implemented a proper internal rating system that enables the Bank to evaluate each capital investment under risk profile.

As a consequence, for each loan granted it's possible to record the correct interest rate that should be applied (Cencioni, 2005).

Considering the structure of the Bank A, that is made by many local branches, it's important that the branches, that grant loans, apply to each loan the right interest rate (connected to the riskness of the loan itself).

Since risky loans cause costs for the Bank A, local branches have to apply an high interest rate to risky customers or refuse the loan.

These decisions have an elevated impact on profitability and competitiveness of the Bank A (corporate).

It's important to introduce the interest rate fixed by the branches within their performance measures in order to stimulate an economic behaviour.

The latter influences Bank A performance through an higher level of capital reserves required by Basel 2 Accord standards.

The Accord's standards affect the management of the Bank and so their influence must be include into the control system that should be comprehensive.

The Balanced Scorecard model could be useful to implement a comprehensive measurement control system for the local branches is coherent with the one of the corporate.

In this way it's possible to reach the alignment between the corporate and the branches.

Through the Balanced Scorecard it's possible to include financial measures (they are considered critical for the business performance) and other kind of measures; particularly, these measures regard customer satisfaction, internal processes, employees and capabilities which are linked to a system performance that should lead to long – term financial success.

This characteristic makes Balanced Scorecard different from other managerial tools, such as Tableau de bord (Epstein and Manzoni, 1998).

The management control system is made up by two dimensions: a structure and a process.

The first one, the organizational structure, concerns the economic responsibility distribution and presents some problems about congruence with the distribution of organizational responsibility.

The second one, the process, is the methodology that defines goals, coordinates aims (those of the corporate and those of the branches), verifies the activity's development and results, analyses variances and, eventually, re-defines goals.

The articulation of the control system is important to align the Balanced Scorecard of bank's branches to the one of the corporate.

The following paragraph will describe the dimensions of the management control system and points out its main limits.

4.1 - The organizational dimension of the management control system⁶

The management control system of Bank A is based on responsibility centres.

This kind of system aims at measuring the profitability of the different responsibility centres (organizational units) within the central structure (corporate); the results of branches depends on costs and revenues towards out-house, but also on some notional costs.

It's possible to define a responsibility centre as a company's unit that carries out proper activities whose costs and revenues can be recorded.

The identification of the centres depends on the organizational structure of the Bank and leads to the definition of profit centres, costs centres and revenues centres (Brusa 2004).

In the case of the Bank A, the branches are defined as profit centres: their goal is profitability obtained through the external relationships with the customers.

As a consequence, the centre's manager is responsible for the costs and revenues of the branch itself and rules a sort of income statement of the unit (Pavan 1997).

In this way it's possible to evaluate the contribute of each branches to the bank's profit.

The opportunity of handling these profit's levers changes according to the degree of centralization and the management behavior of the board of the bank.

Generally a bank's branch can be considered a semi-autonomous profit centre, because its manager can't control all the levers of profit; especially, the amount of invested capital of his branch is out of his influence.

The choice of defining a bank's branch as a profit centre is due to the consequences that it can cause on the behavior of its managers.

In fact, even if the branch's manager can't affect all the profit's levers, he will be led to consider the impact of his decisions on profit and not only on costs and revenues.

Therefore, the main goal of this system is to stimulate managers to take convenient decisions for the whole bank, rather than decisions targeted to the objects of a single organizational unit (e.g. a branch).

⁶ This paragraph is by Paola Vola.

That's why within Bank A each branch is considered a profit centre, with its own income statement.

The profitability of the whole bank is made by the difference between charged interests coming from investments and negative interests derived from funds' raising.

The income statement of each branch identifies the economic result of each business unit, that corresponds to the intermediation margin.

The latest is influenced by two elements:

- the interest rate towards the market;
- the cost of the capital for the branch.

4.2 - The process of management control system⁷

It's important to remember that structure and process are bound: the structure can influence the execution of process, but the implementation of process can involve relevant changes at structure.

In particular, in the Bank A, the attention is focused on branches and nowadays the process of management control system is based on economic result of single branch. In fact the goals assigned to the branch and later on controlled are the following:

- interests payable and financial incomes that derive from credits and debts of single branch;
- passive and active charges of single branch;
- interests payable and financial incomes that derive from application of internal transfer rate;
- direct costs (telephone costs, staff costs, etc.).

The economic result of branch includes also a share of general expenses, attributed to single branch, but there is no responsibility on these costs because they are not controllable by single branch.

This analysis about Bank A's branches control process underlines some criticalities:

- no explication about costs allocation to branches;
- no attribution of credits' losses to branches;
- lack of loans riskness consideration for the determination of the internal transfer rate;
- lack of set of qualitative indicators;
- lack of communication of corporate designed strategy to branches.

As regards overheads' allocation, it is not clear if it's respected the causal principle (Anthony, Hawkins, Macri', Merchant, 2001).

Instead, about credits' losses is important to include them into the margin of the branch that has granted the connected loan.

⁷ This paragraph is by Laura Broccardo.

Concerning the calculation of the internal transfer rate of every branch, it is important to consider the riskiness of the investment of the branch itself (Cencioni 2005). In other words, the branch that has granted loans to the more solvent customers will be charged of the lowest level of interest. In this way it could be possible, for the Bank A, to find a way to make branches economically responsible.

In Bank A the attention is on economic and financial goals and the process of management control does not monitor other important success's variables like customer satisfaction, market placing, staff motivation and innovation.

Another limit in Banks A management control system is the lack of corporate strategy communication. A prerequisite for implementing strategy is that all branches, included the board of directors, understand the strategy and the required behavior to achieve the strategic objectives. It's also required a consistent program to educate the organization on the components of the strategy (Kaplan and Norton, 1996).

5 – The global strategic planning of the Bank A and the alignment problem of the branches⁸

Organizations, while drawing up the measures for themselves, are forced to rethink their strategic priorities and describe their strategy.

In other words, it's important to define the success key factors within a system: in it, there are linked with cause – effect relations.

Strategic map, which is a part of the process of constructing the Balanced Scorecard, is now the starting point (Kaplan and Norton, 2004; Brusa 2007).

After the design of the strategic map, with the success key factors, it's necessary to trace the indicators to monitor performances, according to the principle that it's impossible to manage what you cannot measure (Kaplan and Norton, 1996).

In the case of Bank A, the effort was to design a comprehensive control system made up by different kind of measures, coherent with the strategy of the Bank.

The step followed in the definition of strategic planning process are the following:

- design of the strategic map of the Bank A;
- design the Balanced Scorecard for the Bank's Corporate;
- design the Balanced Scorecard for the Bank's Branches.

The first two elements are presented in the next paragraph.

5.1 - Strategic map of Bank A and it's Balanced Scorecard

Designing the strategic map of the Bank, considering the Corporate, is a way of providing a macro view of the Bank's strategy and provide it with a language in which it can

⁸ This paragraph is by Paola Vola.

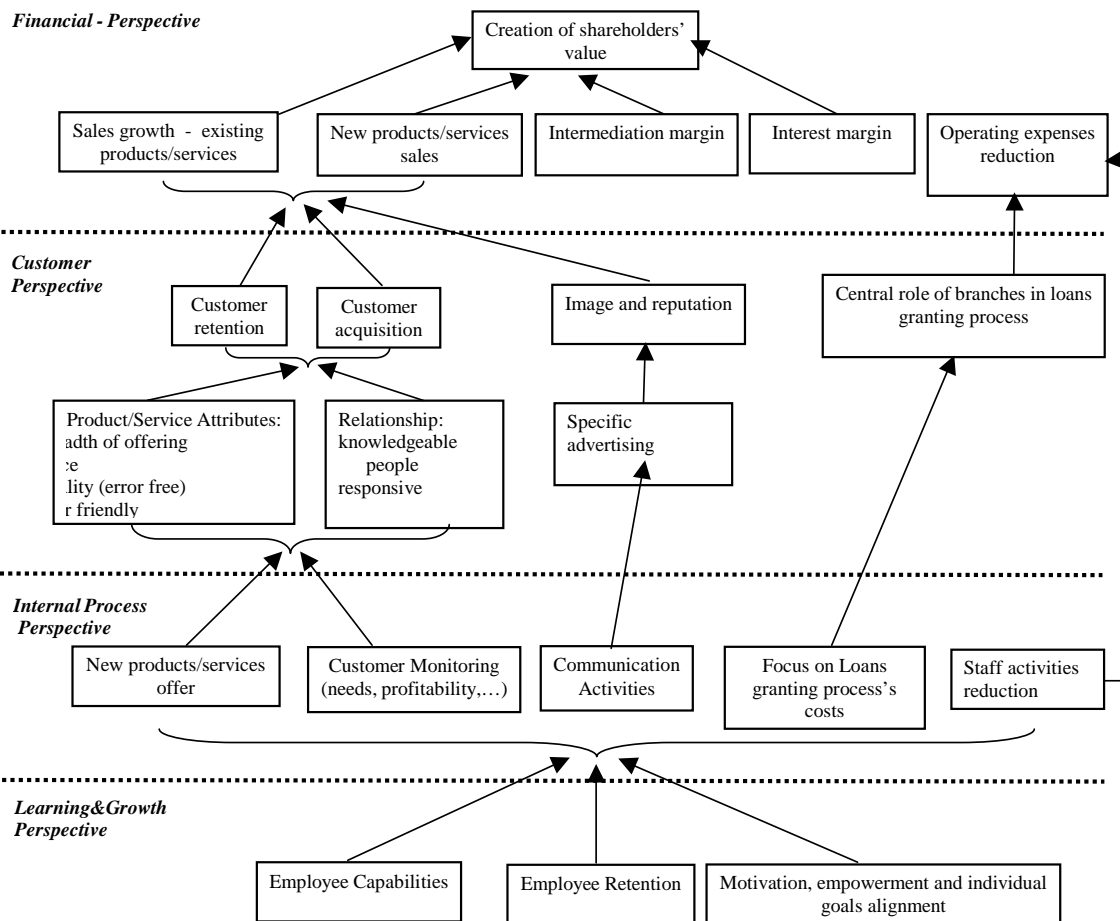
describe its strategy, prior to constructing measures to evaluate performance against their strategy.

For the Bank A, the model used in designing the map is the one proposed by Kaplan and Norton, in which are listed four main perspectives that an organization must have.

The following Exhibit contains the description of the strategic map of Bank A: the basic idea is that we start off by looking at a higher perspective to identify what we need; then, it's possible to see what work needs to be done at the lower perspectives in order to achieve the higher goals.

In the Exhibit 3, the arrows of effects are from lower perspectives to higher perspectives, but the arrows of strategic inference (that are not explicitly drawn in the strategic map) are from the higher perspectives to lower perspectives.

Exhibit 3 – Strategic Map of Bank A.



Source: personal elaboration.

The highest perspective involves explicitly the financial measures which summarize the measurable economic consequences of actions already taken.

Financial objective generally relate to profitability, measured by different indicators, such as operating income, return on capital employed, or economic value added.

In the case shown above, the financial objective is measured by the Return on Equity (ROE).

On revenues' side, it can be achieved by the rapid sales growth of both existing and new products/services; on the costs' side, the preservation of intermediation and interest margin, with the reduction of operating expenses are considered crucial in order to reach the object of profitability.

The customer perspective includes several core measures of the successful outcomes from well formulated and implemented strategy; some core measures include customer acquisition and retention, image and reputation, the importance of the local branches in the relationship with the customer.

But the customer perspective includes also specific measures of the value propositions that the Bank will deliver to customers in targeted market segments⁹.

The segment specific drivers of core customer outcomes represent those factors that are critical for customers to switch to or remain loyal to their suppliers.

For Bank A's customer, the most important value propositions are connected to the products/services attributes, especially the price, the quality and fact that they can be plainly useable.

In the internal business process perspective, the focus is on the critical processes in which the organization must excel.

These processes enable the Bank to deliver the value propositions that will attract and retain customers and satisfy shareholders expectations of financial returns.

The map proposed highlights existing processes, but also new processes that are not currently be performing at all.

For example, the customer monitoring is critical for the Bank's success because it enables the organization to understand customer's needs, but also evaluate the profitability of each customer.

Another critical process that the map outlines is the loans granting process: on one side, infact, it affects the costs through prospective losses, on the other side, it can cause an increase in the level of capital reserves required by Basel 2 Accord standards if the loans are granted to risky customers.

The support activities must be monitored to reduce overhead costs: in Bank A, infact, there is a great difference between the intermediation margin and the operating income due to the huge amount of this kind of costs.

The fourth perspective identifies the infrastructure that the Bank must build to create long-term growth and learning: the processes, in fact, must be supported by continuous improvement of technologies and capabilities. For Bank A, the role of the employee

⁹ With reference to the targeted market segment, Bank A's main segment is made up by small and medium enterprises (SMEs), considering the local geographic area in which the Bank works.

is crucial in order to obtain high performances; especially the branches' directors play a central role, because they manage the relationships with the customers and select them.

The decisions of the branches' directors regard also evaluating customer in case of granting loans, so they are directly responsible for the Bank performance¹⁰; so it's important to involve them in the general goals of the Bank.

In the map we propose the alignment of the individual goals of these directors with the general goals of the Bank.

The implementation of the involvement of directors can be reached through the introduction of a reward system, such as management by object system for the branches' directors, based on the economic and financial performance of the branches.

The next step is to identify what is important to make the strategy effective: the map, in fact, doesn't show the key actions to be carried out and the key performance indicators to be monitored.

In the next exhibit it's presented a scheme that clarifies, for the success key factors included in the strategic map, the connected key actions and key performance indicators.

Exhibit 4 –Balanced Scorecard of Bank A.

Strategic goals	Success key factors	KPI	Key Actions
Customer satisfaction	1. <i>Customer retention</i> 2. <i>Customer acquisition</i>	- market share - n° of customers year 1 / n° of customers year 0 - n° of customers at the end of year 1 / n° of customers at the beginning of year 1 - n° of new products/services offered per year - price of product/service (compared with competitors) - product's profitability / product's level of risk (compared with competitors) - n° of complains by customers - time required to do a job all over again	Focus on product/service attributes: - the range of products/services - the price - quality - user friendly
		- n° of customer / employee - n° of days to reply to customers' questions or problems	Relationship: - knowledgeable people (the employees must have a stable relationship with the customer) - responsive

¹⁰ The branches' directors have discretionary power of granting loans up to certain amounts.

	3. <i>Image and reputation</i>	- advertising expenses - n° sponsorships - sponsorship expenses -	Specific advertising through different channel: - television - newspapers -
	4. <i>Central role of branches in loans granting process</i>	- cost of branches - profitability of each branches - risk level of the loans granted by the branch	Actions to involve branches' directors in the general goals of the Bank
Improvement of internal process referred to customers	1. <i>New products/services offered</i>	- expenses to developing new products/services - expenses to obtaining new products/services	Widen the range of products/services offered to customers
	2. <i>Customer Monitoring</i>	- profit of single customer - n° of transaction per year per customer - risk level of each customer (through a rating system)	Analyze the profitability of different customers
Improvement of internal process related to branches	1. <i>Granting Loans process's costs</i>	- profit generated by the branches considering the costs allocations for risk	Charge each branch of the costs connected to riskness of the loans granted
	2. <i>Staff activities reduction</i>	- overhead costs - n° of employees of the support units - survey on the quality of the support and general activities	Externalization of some staff activities
Employee empowerment /motivation	1. <i>Employee capabilities</i>	- % of coverage of key roles - education costs	Improve employee's capabilities
	2. <i>Employee retention</i>	- employee's turnover - specific survey	Monitor the satisfaction of employees and the retention rate
	3. <i>Individual goals alignment</i>	- n° of branch's directors evaluated on the basis of branch's profit - n° of branch's directors involved into a reward system (MBO)	Involve employee
Creation of shareholders' value	1. <i>Profitability</i>	- interests rate - intermediation profits and costs	Intermediation and interest margin
	2. <i>Reduction of operating expenses</i>	- n° of branches within a geographical area - n° customer per branch - volumes managed per branch	More rational organization of the branches
	3. <i>Asset management</i>	- general risk level of loans compared with the interest rate charged on customers	Improve the management of capital invested

Source: personal elaboration

5.2 - The alignment of the branches to the strategy of the Bank: the Balanced Scorecard of the branches

To gain the maximum benefit from the balanced scorecard system, it's necessary to share strategy with the whole organization.

By communicating the strategy and by linking it to personal goals, the system creates a shared understanding and commitment among all organization employees.

The alignment of an organization to a common direction is a complex and extended process (Kaplan and Norton, 1996; 2001; Brusa 2007)

In the case study, the way chosen to reach the goal of alignment is the definition of a balanced scorecard for each branch.

Usually, banks focus their attention on economic and financial measures, but they are not sufficient to preserve long term success.

In order to find out a complete set of indicators, we have considered economic and financial indicators but also propose other kinds of measures; all the measures must be coherent with the strategic goals and indicators proposed for the Bank.

The main existing indicators for a branch are summarized in Exhibit 5, while in the Exhibit 8 proposed measures are presented.

Exhibit 5 –Balanced Scorecard of Bank A.

Success Key Factors	EXISTING BRANCH'S KPIs
<i>Economic- financial performance</i>	Interest margin Intermediation margin Operating income Net profit Intermediation margin / n° of employees
<i>Customer Monitoring</i>	Total amount fund – raising (A) Total invested capital (B) Total volumes managed (A+B) Insolvency amount / Invested capital Loan's amount - 25% risk level Loan's amount – 50% risk level Loan's amount – 75% risk level Loan's amount – 100% risk level
<i>Activity</i>	n° of transactions n° of employees (monthly average)

Source: personal elaboration

The main criticalities connected to the KPIs shown above are connected to:

- limits in the calculation of the branch economic –financial result
- restricted type of indicators

As far as concern the calculation of the branches' result, the costs connected to the riskness of the loans granted and the prospective losses on loans are not considered and the criteria for the allocation of overhead costs are not explicit.

In fact, the net profit of the branch is given by operating income (interest margin – intermediation margin) minus the part of general costs allocated to the branch.

It could be useful finding different criteria for the imputation depending on the type of costs to allocate (Anthony, Govindarajan, Macri', 2001; Anthony, Hawkins, Macri', Merchant, 2001).

The costs relate to the riskness of loans granted must be considered while determining the performance of the branch (in fact, loans granted to risky customer creates costs for the Bank in terms of level of capital reserves required by Basel 2 Accord). To reach this aim, it's possible to calculate a notional cost of capital for the branch, depending on the risk level, called internal transfer rate. This rate is an element that influences the intermediation margin.

The internal transfer rate is determined by correcting the base interest rate (cost of capital – fixed by the Bank) with the level of risk; for example we can consider the following figures.

Exhibit 6 –Internal transfer rate calculation.

Amount of invested capital	100
Insolvency probability	10%
Prospective loss in case of insolvency	20%
Expected loss	= 10% x 20% = 2% 2% x 100 = 20
Interest Rate applied on loan	8%
Base Interest Rate	5%
Interest Rate corrected by risk (internal transfer rate)	5% + 2% = 7%
Spread	8% - 7% = 1%
Actual contribution to profit	1% x 100 = 10

Source: personal elaboration

Using the internal transfer rate, as cost of capital, the result of the branch is affected by the decision made by branch's director.

If branches' directors are evaluated on the branch result, in this way, they will be led to grant loan to solvent customer.

Another important consequence of the use of internal transfer rate is that the directors will have a parameter to charge the right interest rate to customer (for example, if we consider the exhibit 6, higher than 8%).

Regarding the type of indicators included into the KPIs of branch, there are few qualitative and long-term indicators.

In the Exhibit 7, we list the KPIs proposed in order to outdo the limitations outlined.

Another limit connected to the KPIs of the branches is that the directors often don't understand the importance of the indicators themselves in respect of the Bank goals.

The action proposed is, in addition to the implementation of the MBO system¹¹, a plan of monthly meeting with the members of the Strategic Planning Staff to spread the meaning of the comprehensive control system designed for the branches.

Exhibit 7 – Proposed Branch's KPI's.

PROPOSED BRANCH's KPIs
Intermediation margin (calculated using internal transfer rate as cost of capital) Average Riskness of the invested capital Prospective losses / Invested capital Total volumes managed per employee Cross selling measures Intermediation margin per employee N° customer per employee Operating costs / Intermediation margin

Source: personal elaboration

6 – Conclusion and limits¹²

This analysis aims at studying the implementation of a management control system in a Piedmont Cooperative Bank with reference to the Balanced Scorecard model (BSC) suggested by Kaplan and Norton (1996, 2001).

The banks are now facing radical changes in market's system, especially due to globalization, innovation of financial products and European rules imposed by Basel 2 Accord.

In this framework, it occurs a comprehensive measure system to control success key factors; the system must reflect directly from company's strategy and must consider the crucial problem of the alignment of the different organizational units.

In order to formalize the strategic process of the Bank A, the first step is represented by the design of the strategic map of the Bank, in which all success key factors are included and linked by cause – effect relations.

Starting from the strategic map it's possible to trace the indicators to measure performances. This passage is very important, because Bank A was used to find out the indicators without a precise reference to the strategic map.

¹¹ The Management by Objectives is a process of agreeing upon objectives within an organization. MBO substitutes for good intentions a process that requires rather precise written description of objectives (for the period ahead) and timelines for their monitoring and achievement. The process requires that the managers and the employee agree to what the employee will attempt to achieve in the period ahead, that the employee accept and agree to the objectives, otherwise commitment will be lacking.

¹² This paragraph is by Paola Vola.

The risk of this way of proceeding is to miss the link between the success key factors and the indicators. In other words, the strategy wouldn't be effective.

This work contains, firstly, the strategic map of the Bank A, then the set of indicators – the Balanced Scorecard for the Corporate.

Considering the problem of alignment of the organizational units, the branches in our case, we have considered the performance indicators existing within the control system.

The aim of the control system of the branches should be to encourage the decisions of the branches' directors in order to affect Bank A's goals.

Considering that it's important to involve them into the general goals of the Bank, in the map we have proposed the alignment of the individual goals of these directors with the general goals of the Bank.

The implementation of the involvement of directors can be reached through the introduction of a reward system, such as management by objectives system for the branches' directors, based on the economic and financial performance of the branches.

So the set of indicators of the branches is fundamental for the implementation of the global strategy.

As far as regard this point, we have designed the Balanced Scorecard for the branches introducing some indicators to try to exceed the limits of the existing set of indicators (limits in the calculation of the branch economic –financial result and restricted type of indicators).

The proposed Balanced Scorecard takes into account the costs connected to the riskiness of the loans granted and the prospective losses on loans in the calculation of the result of the branch and qualitative and long-term indicators.

The aim of the paper is to show, through a case study, that a logical model in strategic process is necessary (firstly the design of the strategic map, then the formalization of the Balanced Scorecard), in addition to the need of alignment of the organizational units.

The alignment of the organizational units can be reach through the involvement of the directors of the units – branches' directors; it means that measures based on unit's economic-financial results and MBO systems can be useful to obtain the alignment needed.

The main limitation of this study consists in the unique case investigated; the use of Balanced Scorecard, as management control system, within the cooperative credit in Italy is not wide spread.

With reference to this aspect, we have planned further researches focused on the way other co-operative banks use Balanced Scorecard model in Italy.

These studies will be essential to enrich and complete the evidences on comprehensive measurement control systems within cooperative credit sector in Italy.

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