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IMPLICATIONS OF NON-FINANCIAL PERFORMANCE MEASURES IN INDIAN BANKS

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The inadequacies of conventional management accounting (MA) information point out a need for management to locate correct measuring gear for budding non-financial performance (NFP) in the exceedingly aggressive financial services, as well as in the manufacturing industry. Thus, the conduct of MA in measuring the performances of budding NFP has been in receipt of augmented emphasis in the increasingly important service industries. Bearing in mind the shortcoming of the conventional MA information system, predominantly the measurement of novel emerging NFPs, this empirical research is an effort in the direction of investigating the role of MA in non-financial as well as financial performance measurement (PM) in chosen banks and financial institutions (BFIs) in India. The study demonstrates that the function of MA in non-financial PM is not important. However; management is paying more notice to its measurement. This study identifies three different aspects of NFP: profit-driven NFP; NFP for long-term spirited advantage; and independent NFP (those not linked with the profitability of an organization).

Key Words: Service Industries; Performance Measurement; Management Accounting; Banking.

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INTRODUCTION

The shortcomings of conventional management accounting (MA) information, and the need for further study of its practical role in both manufacturing and services, have been talked and researched by many well-known scholars (Scapens, 1990; Kaplan, 1984 among others). A call for multi-dimensional performance measurement (PM) has been established as a result of several studies by contemporary MA scholars (Kaplan and Norton, 1992, 1996; Fitzgerald *et al*., 1991; Nanni *et al*., 1990; Govindarajan and Shank, 1992; Otley, 1999).

In recent years, non-financial PM has received substantial consideration from MA scholars, and there have been quite a few studies with the intention to deal with NFP measures. Prominent among these studies have been those of Scapens (1997), Simons (1990), Hoque and James (2000), Abernethy and Lillis (1995), Ittner *et al*. (1997), Armitage and Atkinson (1990), Ezzamel (1992), and Turney (1991). A lot of of these researchers talked about the subject of performance measures in manufacturing industries, but a small number of studies have been dedicated to service industries. Distinguished exceptions include Smith (1998), Fitzgerald *et al*. (1991), Ballantine *et al*. (1998), Brignall (1997), Evans *et al*. (1997), and Silvestro *et al*. (1992).

Fitzgerald *et al*. (1991) have argued that PM is an input issue in ensuring the winning completion of a company's strategies and techniques in chase of its goals, and in ensuring the achievement of a business organization in both the short term and the long term. In the short term, financial performance measures unswervingly connected to profitability (such as return on investment and earning per share). However, in terms of long-term profitability, the intangibles that guide to profit over time assume better importance – counting such non-financial factors as customer approval quality, and so on. In lots of cases, such factors might be measured "non-financial" in the short term, but are taken to be "financial" in the longer term. From the normative point of view, it might be said that they are "non-financial", but if so-called "non-financial" performance factors are scrutinized absolutely over a dissimilar time horizon, by way of few exceptions they are seen to be important in overall long-term profitability.

Kaplan and Norton (1996) recognized this realism by giving an example:One organization now considers its scorecard measures to contact the collision of each possible investment. A relative weighting is recognized for the measures, giving important stress to financial measures, such as return-on-capital and profitability, but also to the drivers of future financial performance, such as quality, service, and customer retention. They exposed an entire succession of linkage in overall financial performance. For example, employee morale increases customer satisfaction and this, in turn, leads to elevated return on capital because such employees produce pleased and loyal customers, and having such customers, in turn, drives financial performance. In this case, the elements in the service profit chain can thus be articulated. To appreciate the position of MA in measuring NFP, it is essential to recognize and classify NFP according to the wider objectives, strategies, and techniques of a business organization. Management must believe performance measurement in terms of long-term competitive advantages (LTCA) and not necessarily in terms of the short-term profitability of the organization.

OBJECTIVES

Performance measurement is in receipt of a higher emphasis in service organizations as well as in manufacturing organizations. Though a great deal has been written about the requirement for correct performance measures, and there have been quite a few studies dealing with NFP measures, reasonably little is known about the role of MA in the measurement of NFP in practice. Against that background, this paper investigated the role of MA in measuring NFP in the competitive Indian financial market. In this study of how MA systems are used to measure performance in the financial sector, answers to the following questions were investigated:

- What methods or systems of MA are used to calculate financial and non-financial performances in banks and financial institutions (BFIs)?
- Whether BFIs are in fact measuring non-financial factors and indicators, and if so, to what level is this being done?
- Which factors of NFP are being measured, and which methods or apparatus of MA are useful in measuring them?
- What are the difficulties being practiced by management, what are the causes of these difficulties, and how they might be conquered using the existing MA performance measures?

RESEARCH AND METHODOLOGY

This study involved the collection of data from primary and secondary (annual reports, booklets, and special publications on related issues) sources and literature survey. Data was collected by semi-structured interviews with chief executive officers (CEOs) of four BFIs during the year 2013-2014. The questions covered an introduction to the institution, MA practices in the institutions, and performance measures – both financial and non-financial.

The present study was able to make a meaningful comparison of the role of MA in different types of financial institutions. The purpose of the study was not to contrast like with like, but to study the role of MA in non-financial PM in dissimilar types of financial institutions. Even though the study attempts to draw some comprehensive conclusions, the authors are aware that generalizing from only four BFIs must be treated with care. For practical reasons it was not likely to expand the study population. The secondary sources of information were useful for comparing the objectives of CEOs with actual MA practice.

Management accounting in performance measurement in BFIs

Based on the analysis of the data collected, this part discusses performance measurement in banks and financial institutions.

Bank A

Bank A is the largest commercial bank, and has branches throughout. Its crest management emphasizes the measurement of performance as being "very important", and financial performance of every section in the bank is often measured. The methods and models that are taken to measure performance are activity-based cost management (ABCM), benchmarking, and performance pyramid. Bank management reports no difficulties with measuring performance by means of the present methods, apart from deference with risk-adjustment matters. The call for correct risk-analysis and customer and product profitability is very important for the chief executive. Customer and product profitability are also vital factors in which management feels a need to develop its present practice of PM. The views of Bank A on the subject of PM are presented in Table 1.

Although the CEO accorded only some significance to NFP, the bank does measure NFP regularly. In doing so, Bank A uses the same models and methods for measuring NFP as it does for measuring financial performance. The management of bank A is well content with the present methods, and would like to carry on the present practice in future, assuming no considerable change in the bank's internal and external circumstances.

The executives of A recognize the worth and importance of MA systems in PM, but measurement of NFP is moderately less emphasized than that of financial performance. This is reflected in the planning of MA systems and the measurement process itself. Declining production costs, control of profit centers, and financial planning are all significant in the view of top management, and are relatively more important than certain non-financial aspects (such as environmental issues). The CEO pays a lot of concentration to the measurement of a variety of risks and to the profitability of customers and products, and less attention to the measurement of non-financial indicators. Nevertheless, several important aspects of NFP are measured – including customer satisfaction, quality, on-time service, promise to customers, and so on. Of these, on-time delivery of services and commitment to customers may be considered a part of the attempt to make sure customer satisfaction.

The business procedure has already been re-engineered, and ABCM and life cycle are used to measure performance (as well as for other aspects, such as costing). Though, in view of the chaos in the banking sector, management feels a need to utilize life-cycle theory – which seems to be a useful and timely approach as long as economic conditions remain uncertain, total quality management (TQM) is progressively being implemented, and management feels that TQM is also likely to be supportive in measuring both financial and NFP accurately. However, since non-financial PM is not receiving a high priority from management, it is likely that TQM will be used to drive the financial performance.

In this case, the CEOs are not so much worried about whether the cost-accounting system is modern or not. Rather, they are paying more attention in seeing that MA systems help to reduce service costs. They are also keen to make correct decisions in civilizing the allocation mechanism of indirect costs. Whatever the rights and wrongs of this report, there is no significant problem in this bank with accumulating data on costs, and the cost-accounting system do fit with the actuality of the business.

Bank B

Bank B is a financing house under the sunshade of a large commercial bank. Its growth rate in the past five years has been about 10 per cent per annum, with a 15 per cent average rate of return. The management of Bank B does not accord much importance to measuring performance. Indeed, Bank B measures performance only in terms of the activities of the sales and promotion departments. In spite of this apparent unresponsiveness to general performance measurement, it is interesting to note that management does utilize balanced scorecard (BSC).

The CEO expects that target-costing and BSC, taken together, can resolve their problems in this regard. It is obvious that the organisation does not have a clear conception of how this might be achieved, but the firm believes that the two methods can be merged to make a practical tool for accurate measurement of performance. The role of PM in Bank B is presented in Table 2.

The top management of Bank B believes strongly in the importance of non-financial PM in the organization, but they practice it only “sometimes”. The targeted aspects of non-financial PM are customer pleasure, quality, quick response, and one-time service. These are measured using the idea of process-type theory and benchmarking. In this look management is “somewhat” content with the accuracy of present NFP measures, and they are bearing in mind the development of a completely new model of NFP measures. According to an executive, none of the obtainable models of performance measures is suitable for measuring NFP in the organization. This executive believes that the traditional approach of sending a questionnaire to customers does not give a realistic picture of customer anticipation. He notes that since Bank B works under the patronage of a large bank, it receives direct support (and sometimes also pressure) to measure overall activity properly. Bank B has few products and a limited number of customers, and management therefore focuses its efforts on assisting these customers as they are "the future" of this organization. Concerning the ability to reduce service costs to make the organisation more competitive, he is rather doubtful. He is concerned about the need to do "more" to decrease service costs.

Top management says that when they feel the need to measure customer satisfaction they do so by using questionnaires, after which customer satisfaction is benchmarked against some other financial institutions. However, benchmarking does not have an effective role because of the narrowly defined range. Moreover, since Bank B's products are few and distinctive, their service-process type of theory is also not effective – because, as Fitzgerald *et al*. (1991) have noted, process-type theory emphasizes the individuality of a service shop.

Bank B has re-engineered its business process, but this has not helped in establishing non-financial PM in the organisation. Total costing (TC) is used for costing purposes, and is even helpful for financial performance measures, but is apparently not deemed to be useful in measuring NFP. A top manager is of the opinion that the methods used to measure financial performance are hard to put into practice in this organization. It is observed that, in practice, when management considers activity-based costing (ABC) and TC, they rather think of making them helpful for financial performance measures and not the measurement of NFP. They do not even regard that there is any need to measure NFP in the organization.

A CEO advises that BSC be practiced in Bank B. However, internal performance (such as employee performance) is not measured. Bank B measures the financial performance of only two departments – sales and production. Therefore, it can be said that Bank B incompletely practices so-called BSC.

Bank C

Bank C is one of the largest co-operative banks, with an average growth rate in the past five years of about 1 per cent. The top management of Bank C does not attach much significance to measuring performance, although management does measure the performance of every section of the organisation. Their major concern is now to make the organisation profitable in the chaos of the banking sector in Finland. The methods and models that are used to measure performance in the organisation are benchmarking and customer survey. When asked whether there was any problem in measuring performance in the organisation, management referred to "some problem". However, management believes that by using some other model the problem can be solved. In this regard, the CEO told of his efforts to use balanced scorecard. Table 3 summarizes the vision of Bank C.

Management is not content with the methods currently being practiced and is therefore thinking of a modification of benchmarking and customer survey, which they believe would be a better way to measure NFP. It is known that benchmarking should be a comparison with the best-practicing organisation if the benefits of benchmarking are to be achieved (Govindarajan and Shank, 1992). However, it was observed that managements in different cooperative banks compare their performance with each other. In practice, they do not compare different financial and non-financial performance measures among other financial institutions (such as commercial or savings banks), and thus the competence and competitive position is under question.

Management does feel the need for one more model to be developed. Management's opinion of ABC and BSC is not very positive because they believe that ABC is good for cost accounting purpose and not for measuring general business performance. According to management, however, it is not possible to achieve everything at the same time as Kaplan and Norton (1996) prescribed. The CEO believes that benchmarking is less useful for measuring NFP. As a result, customer survey is the only method that management prefers to practise. The CEO acknowledges the present system as being "very problematic" in fitting with the reality. The reasons given for not implementing other systems were the reluctance of personnel to change to new systems and the costs of accumulating data. The key behavior and activity drivers were not a problem to find, it is because of the dimension of a self-governing unit and the line of products that Bank C produced.

Though, management does feel the need to modify and improve the present practice of PM, it does not consider the ABC system to be a useful method to measure NFP because it is "very problematic" to implement and from time to time creates misinterpretation and displeasure among personnel. Since the want for FPM is not great, BSC can correctly be used. However, as mentioned earlier, management thinks that "it is not possible to attain the whole thing at the same time".

Bank D

Bank D is a cooperative bank, and its operating function is quite alike to that of a commercial bank. Its top management gives far above the ground precedence to measuring financial performance, and this is measured in every section of the organization. CEO said that he does not have much idea about the integrated PM model, but that he had been informed through an additional source that bank management is using an integrated PM model to measure financial performance. However, benchmarking practice does exist in the organisation. Some troubles are reported with the present PM and top management feels the need for an alternative model of performance measures. Table 4 indicates the perception of Bank D.

Top management of Bank D measure NFP regularly and it is "very important" to them. Many aspects like customer satisfaction and excellence of services are a higher priority. Obligation to customers and on-time service are also significant factors to top management. Being a co-operative bank, social well-being receives a high priority from management, and the welfare of stakeholders is especially important to top management. The management used to measure NFP by using an integrated PM model (mixture of business strategy and performance measures in diverse levels of the organization) and benchmark NFP with similar organizations. They are somewhat satisfied with the accuracy of this present non-financial PM method. The use of an integrated PM model is meant to integrate the strategic objectives into the operation, and therefore, from a normative point of view, but the model is not adept the same way as Nanni *et al*. (1990) suggested. It should chiefly be pointed out that many of Bank D's units are independent and in many cases they are entitled to decide the cost and MA systems for their own betterment and competence.

FINDINGS AND CONCLUSION

Management Accounting(MA) systems have had a function in measuring performances in diverse banks, but their function in measuring NFP is not as much of significance. The financial PM is a regular and a vital practice but in many BFIs, non-financial performance measures (PM)is less significant and not proficient on a regular basis. From the normative point of view, there is need for precise measurement of different performances and contemporary management accounting scholars are promoting a number of MA methods and techniques to measure performance. Though, in practice, MA performance measurement is dominated by traditional MA techniques (Bromwich and Bhimani,1989).

We observed that benchmarking is the most extensively used PM technique in banks. Two of the four BFIs measured both financial and NFP by benchmarking against other similar kinds of organizations. The idea of benchmarking with top practice organization is not found, but management is somewhat aware of judging their organization's performance at least with like kind of organizations' performance that is not best but better than others. BFIs are rather concerned about their domestic market. Therefore, they do not see the need for benchmarking their performance against non-Indian banks.

Customer satisfaction is the most significant feature of non-financial PM in the BFIs studied. Many of them find that customer approval has a direct impact on improving financial performance, and they are therefore very much conscious about it. The second most vital aspect is quality service in BFIs. Three banks consider quality aspects to be vital, but in one bank quality service is considered as part of the customer satisfaction agenda. Obligation to clients and stakeholders and on-time service is the third most important aspect of non-financial PM in BFIs. In this case, two other banks believe in on-time service and commitment as part of customer satisfaction efforts. Cooperative banks try to maintain commitment with clients and, therefore, they rather consider commitment as an independent aspect rather than part of customer satisfaction.

According to the objectives and strategy of the business, the nature of NFP differs. This can also modify with different micro and macro environments. Under substantial scrutiny, the NFP and its measurement is to guarantee profit for competitive advantages. Most of the NFP measures that are emphasized and measured by management in BFIs are for profit, and we can call them "profit-driven NFP measures". However, efforts are being made by the management of some BFIs to ensure profit in the longer term. These gains can be characterized as "long-term competitive advantages (LTCA)". However, a few activities and performances of BFIs, which are not linked to improving profitability such as work for society, environmental consciousness, and so on, can be called "independent" NFP. The remainder of the efforts is aimed at making profit in the longer term and the achievement of competitive advantage in future markets.

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ANNEXURES

Table 1: Performance measurement in Bank A

Description	Financial PM	Non-financial PM
Importance	Very important	Somewhat
Application of MA systems	Every section	Regularly
Model/method	ABCM, benchmarking, performance pyramid	ABCM, benchmarking, performance pyramid
Problem/contentment	No problem	Well contented
Opinion/suggestion for improvement	Implement raw-rock model	Present systems and methods are OK

Table 2 Measuring performance in Bank B

Description	Financial PM	Non-financial PM
Importance	Somewhat important	Very important
Application	Sales and production sections	Very seldom
Model/method	BSC	Process-type theory, benchmarking
Problem/contentment with	Somewhat problematic	Somewhat contented
Opinion/suggestion for improvement	Target costing and BSC should be incorporated	Need to develop a completely new model

Table 3 Measuring performance in Bank C

Description	Financial PM	Non-financial PM
Importance	Somewhat important	Very important
Application	Every section	Seldom
Model/method	Benchmarking; customer survey (CS)	Customer survey (CS)
Problem/contentment with	Somewhat problematic	Somewhat contented
Opinion/suggestion for improvement	Use some other model	Method to be modified based on benchmarking and CS

Table 4 Measuring performance in Bank D

Description	Financial PM	Non-financial PM
Planning process with MA systems	Process easy, but plans unsuccessful	No plan at all
Usefulness/importance of existing MA systems (benchmarking, integrated PM model)	Somewhat useful and important	Somewhat useful/very important
Fulfillment of the objectives set of using/implementing MA systems	Somehow fulfilled	Fully fulfilled
Difficulties with using MA systems	No difficulty	No difficulty

Table 5 Summary of MA systems in Indian banks and other financial institutions

	Bank A	Bank B	Bank C	Bank D
Description	(commercial bank)	(investment bank)	(co-operative bank)	(co-operative bank)
Number of employees	12000	102	700	1700
Average growth rate in last five years (%)	Information is not delivered	8	2	4
Importance of measuring performance	Very important	Somewhat important	Somewhat important	Very important
Practices of PM in the organization	Every section	Partly (sales and production)	Every section	Every section
Models/methods to measure performance in the organization	ABCM, benchmarking, performance pyramid	Balanced scorecard	Benchmarking, customer survey	Benchmarking, integrated PM model
Problems with PM	Not at all	Somehow problematic	Somehow problematic	Somehow problematic
Ways to overcome the problems with PM	Implement "raw-rock" model	TC and BSC should be incorporated	Use other model	Alternative models be found
Importance of measuring NFP	Somehow	Very important	Very important	Very important
Practice of	Regularly	Very seldom	Seldom	Regularly

measuring NFP	measured			
Targeted aspects of NFP in organization	Customer satisfaction, quality, commitment, on-time service, etc.	Customer satisfaction, quality, quick response, on-time service	Customer satisfaction, quality, commitment	Customer satisfaction, quality, commitment, social well-being, on-time service
Models/methods to measure NFP	ABCM, benchmarking, performance pyramid	Process type theory and benchmarking	Customer survey	Benchmarking, integrated PM model
Contentment with the accuracy of measuring NFP	Well contented	Somehow contented	Somehow contented	Well contented
Opinion/suggestion on improving non-financial PM method	Present methods are OK to practice	Need to develop a complete new method/model	Model to be modified, based on customer survey and benchmarking	New model should be developed (preferably with software)