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## Devising a Balanced Scorecard to Measure HDFC Banks' Performance: A Case Study.

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### Abstract

*Performance evolution process acts a significant role in measuring the strategic achievement of commercial banks. It is absolutely essential to develop a performance evaluation system in a organization, if the organization aims at the long term survival, growth and development. This paper makes a study about how to use the Balanced Scorecard (BSC) as a tool, of performance management system of Indian commercial banks. It also point out that, BSC makes a way into the flaw of conventional sole implementation of financial indicators which measures performance. BSC is a performance management evaluation system not only based upon financial views, also also on non-financial aspects like customer indicators, internal business processes, and employee learning & growth. This is done by constructing the Balanced Scorecard for the banks, and then evaluating the performance the banks through this BSC approach. Panel data spread over five years from 2009 to 2013 and 22 indicators of the bank is used for this purpose. The initial discussion relating to the result of Balance Scorecard as a technique for performance measurement also established. It is found that being a part of the service sector, long-term strategic planning in a banks need to concentrate on such performance measurement system. However the implementing this technique becomes complicated due to the difficulties in measurement of intangible assets, existence of the interrelations among these indicators, different in significance assigned to various indicators within the organization and trouble in setting the linkage between the employees performance and reward mechanism.*

**Keywords:** *Balanced Scorecard, Performance measurement in Banks, Commercial Banks and performance.*

### Introduction

In the competitive business era the only thing that really matters is organization's performance. The introductions of performance management of commercial banks get into gain as a crucial significance to the world and investors abroad after 1991 reforms. Now, banking sector has been commenced to adopting holistic performance measurement systems named Balanced Score Card (BSC) to exhibit the stakeholders that this sector is turning to take advantage of financial and non-financial measures to offer investors with performance information. Banks Executives should understand that traditional financial measurement like return on investment, profitability and earnings per share can give misleading signals for continuous improvement and innovation in competitive word. Also financial performance measurement indicators are criticised in respect of being short term oriented, considering past performance, being non consistent with current business's environment, lack of predictive power and being irrelevant for all levels in the organizations.<sup>1</sup> Therefore, it is quite essential to develop a performance measurement system in an organisation, if an organization aims at the long term survival, growth and development. Balanced Scorecard is not only an appraisal indicator, also a strategic tool. The use of the Balanced Scorecard is abolishing the traditional single-use financial indicators methods to measure the organisational performance. The vital idea of behind the adopting balance score card is to set organisational strategy through finance, customer, internal processes and learning and development indicators in four are to show a relationship between the organization's strategic track to achieve performance appraisal, performance improvement, as well as the implementation of the strategy.

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<sup>1</sup>Singh, M., & Kumar, S. (2007), "Balanced Scorecard Implementations Global and Indian Experiences".

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In the contemporary economic environment, factors like customer knowledge, satisfaction of customer, relationship with customer, culture innovation and changes defines the success for banking industries. This research paper attempts to address this issue from the perspective of HDFC and ICICI bank performance management, and tries to assess the performance of these two banks by employing Balanced Scorecard as a tool to improving performance management system.

### **Performance measurement and Balanced Scorecard**

Literature from the various resources exhibit that, performance measurement ordinarily designed around financial, operational and management control system. Prior to 1980's, organizations used financial indicators like, return on equity, net profit and return on investment to measure their performance, however it is very well known that financial indicators are well in very short term. To achieve a competitive edge, and to retain customers; organizations should be innovative to fulfil the ever changing needs of their customers. Given below is the explanation of the BSC perspectives based on Kaplan and Norton (1992; 1996; 2001):

**Financial:** This indicator measures the profitability, risk, growth and liquidity position of organisation from the perspective of stakeholders. Kaplan and Norton had given importance to the requirement for traditional financial data for the measurement of: Return on Investment, Return on Equity, Fund Flow, Cash Flow, Net Operating Income, Revenue Growth, Overall Risk and Return etc of organisation.

**Customer:** This strategy helps to create value addition and differentiation of product from the view of customer as, ultimate aim of any organisation is to satisfy and retain their customer. Under this measure: customer satisfaction, resolve customer complaints, provide value addition to customer, customer lost/won, sales from new product, etc.

**Internal Business Process:** This strategy deals with producing goods and services is most efficient and effective way so that products can be produce in less cost without impairing the quality. Most commonly measure used under this prospective are: cost of products, quality of products, time saving of services and process innovation.

**Learning and Growth:** This is the strategy for creating congenial climate which could support organisational change, innovation and growth and improve work relationship. The most common measures are used under this indicator: employee's empowerment, employee's motivation, employee's development and information system capabilities.

### **Literature Review**

Since the appearance of the balanced scorecard (BSC) in 1992, developed by Kaplan and Norton, it has gained widespread acceptance as a effective tool for performance measurement and strategic management in various business sectors including the banking sector.

Pandy (2005) reported the results of a simulated exercise where a group of senior managers (attending an educational program) of a large bank developed a BSC made for their bank. Guided by the author, this experiment demonstrated that the achievement of strategic objectives is highly driven by the internal process improvement and that the non-financial variables surpassed the financial variables. Harold (2006) applied the BSC to develop a comprehensive performance measurement and a management tool for the IT in the banking sector in India. The author clarified how a cascade of balanced scoreboards can be useful in the technology effectiveness of commercial banks in India to guarantee better performance management. Ahmed *et al.* (2011) conducted a study in which they surveyed a sample of 27 banks in Pakistan to identify the measures that are used by the sample banks to evaluate their performance according to the four perspectives of the BSC. The authors reported that all the banks surveyed used measures that correspond to the BSC approach to evaluate their performance, however, the significance of the measures varied among the sample studied. Zhang and Li (2009) in their study examined commercial banks in China and they proposed the BSC as a tool to improve the performance of commercial banks in China. They suggested a method and a strategy for application along with restrictions of the BSC. Kollberg and Elg (2010) attempted to recognize the key characteristics of the

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BSC application in health care organizations in Sweden. The researcher used a case study approach where they paid attention to diverse managerial levels in a hierarchical branch in three health care organizations that applied the BSC. The examination discovered that the BSC is used as an instrument for increasing internal capabilities and organizational development.

### Research Problem

The literature states a strong relevance to appraising banks' performance through the BSC approach. However, BSC as a performance management tool did not find its importance in Indian banking sector. In addition, the performance measurement used in the HDFC bank is still based on financial measures, and monthly or annual reports. Therefore this study shall deal with the problem of developing a BSC model to measure the performance of the HDFC bank. The performance results can benefit the bank studied, the stakeholders, and the financial sector analysts.

### Objective of Study

The present paper is aimed to examine the performance of HDFC bank by using balanced scorecard approach. Following are the main objectives of study:

1. To analyze the Financial, Customer, Internal Business Process and Learning & Growth performance indicators of HDFC Bank.
2. Increasing understanding about how the balanced scorecard may be developed and applied within the context of new private banking sector in India.

### Research Methodology

The study is based on secondary data, relevant data is collected from the published annual reports of the selected banks taken from their websites, magazines and journals on finance, RBI official site, have also been used a sources of data. To analyze the performance of sample unit data for the period of five years (2009-2013) has been used. This study covers one of top ranking bank among new private banks "Housing Development Financial Corporation" (HDFC).

### Data Analysis and BSC Development

The following steps were used to develop the BSC for the HDFC:

**First:** Based on the concept of strategic map, the author's effort was to determine the characteristic of bank's administrative activities so as to develop a cause-effect relationship to relate the bank's objectives to its strategic goals in an attempt to choose the measures relating to each one of the four BSC perspectives. Followings measures were selected for every perspective, they are: (a) Financial perspective: Cash deposit ratio, Credit deposit ratio, Interest income to total assets ratio, NPA to net advances, Net Interest income to total assets, Investment- Deposit ratio, Return on assets, Return on equity, Capital adequacy ratio. (b) Customer Perspective: Priority sector advances to total advances ratio, Ratio of deposits to total liabilities, Ratio of term loans to total advances, Ratio of secured advances to total advances. (c) Internal Business Processes Perspective: Business per employee (in Rupees million), Profit per employee (in Rupees Million), Wage bills to total expenses ratio, Wage bills to total income ratio, Wage bills to intermediation cost ratio. (d) Learning and Growth: No of offices, No of employees (in thousands), No of Debit Cards (in lacs), No of Credit Cards (in lacs).

**Second:** With the help of the data available about the HDFC performance from 2009-2013, the authors were able to identify the BSC's objectives, measures and targets for the four perspectives as they appear in Table (I, II, III, and IV)

**Third:** A performance scale was identified for each measure, and 50 score points were divided on the elements of each scale. The total scores in the BSC developed are therefore 1100 (22 measures x 50 points).

## Findings

The analysis reveals that the HDFC performance measured by the BSC was 980, 960, 1000, 1000 and 980 for the years 2009-2013 respectively. Converting these scores on a 100% scale yields: 89%, 87%, 91%, 91% and 89% for the same years (Table V). It seems evident that the HDFC performance was declined during the first two years of the study, but in the next two years the performance improving. In general the annual average score achieved by the bank was 984, which indicates an average performance. With respect to performance on individual perspectives, observed from Table (I, II, III, and IV) that the scores achieved on the financial perspective was highest in 2012 (400 score) and in 2013 score was declined as compare to 2009. This finding coincides with the bank's concentration on the financial performance as a measure of performance. However, there was a decrease in Cash Deposit ratio this means that banks Liquidity ratio is low in last 2 years. There has been a decrease in NPA to net advances due to good credit management policies adopted by bank in last couple of years. There is also a increase in return on assets ratio from 2 years this is due to efficient utilisation of funds and profitable investment made by bank. In last five Capital Adequacy ratio was scored at same level this indicates that bank have less risky weighted assets or indicates high assets quality.

**Table I : Financial Perspective Score Assignment**

	SCORE ON SCALE					SCORE ASSIGNMENT				
	10	20	30	40	50	2013	2012	2011	2010	2009
<b>FINANCIAL</b>										
Cash-deposit ratio	0-2.5	2.51-5	5.01-7.5	7.51-10	10.1-12.5	20	30	50	40	40
Credit-deposit ratio	0-16	17-32	33-48	49-64	65-80	50	50	50	50	50
Interest income to total assets	0-2	3-4	5-6	7-8	9-10	50	50	40	40	50
NPA to net advances	0-0.12	0.13-0.25	0.26-0.38	0.39-0.50	0.51-0.63	20	20	20	30	50
Net interest income to total assets	0-0.86	0.87-1.7	1.8-2.6	2.7-3.4	3.5-4.3	50	50	50	50	50
Investment - Deposit Ratio	0-9	10-18	19-27	28-36	37-45	50	50	40	40	50
Return on assets	0-0.40	0.41-0.80	0.81-1.20	1.21-1.60	1.61-2	50	50	40	40	40
Return on equity	0-4	5-8	9-12	13-16	17-20	50	50	50	40	50
Capital adequacy ratio	0-3.5	3.51-7	7.1-10.5	10.51-14	14.1-17.5	50	50	50	50	50
						<b>390</b>	<b>400</b>	<b>390</b>	<b>380</b>	<b>430</b>

The HDFC scores on the customer perspective were consistent in last five years. The Priority sector advances to total advances ratio, Ratio of deposits to total liabilities scored fifty for last five years. At the same Ratio of secured advances to total advances scored fifty in last five year, this conclude that most of loans sanctioned by

bank were secured in last five years. This shows that the customer's were confident about the performance of HDFC in India.

**Table II : Customer Perspective Score Assignment**

	SCORE ON SCALE					SCORE ASSIGNMENT				
	10	20	30	40	50	2013	2012	2011	2010	2009
<b>CUSTOMER</b>										
Priority sector advances to total advances ratio	0-7%	8-14%	5-21%	22-28%	29-35%	50	50	50	50	50
Ratio of deposits to total liabilities	0-16	17-32	33-48	49-64	65-80	50	50	50	50	50
Ratio of term loans to total advances	0-16	17-32	33-48	49-64	65-80	40	40	50	50	50
Ratio of secured advances to total advances	0-16	17-32	33-48	49-64	65-80	50	50	50	50	50
						<b>190</b>	<b>190</b>	<b>200</b>	<b>200</b>	<b>200</b>

The internal processes perspective does not reveal significant improvements; the average score is 220. In the year of 2013 total score achieved (200 score) in internal business process was lower than average score. There was also poor performance in respect of profit per employees in last two years. Total cost of employees to total expenses is almost same in last 5 years.

**Table III : Internal Business Process Prospective Score Assignment**

	SCORE ON SCALE					SCORE ASSIGNMENT				
	10	20	30	40	50	2013	12	11	10	09
<b>INTERNAL BUSINESS PROCESS</b>										
Business per employee (in Rs million)	0-15	15.1.1-30	30.1.1-45	45.1.1-60	60.1-75	50	50	50	40	30
Profit per employee (in Rs Million)	0-1.50	1.51-3	3.1-4.5	4.51-6	6.1-7.5	10	10	50	40	30
Wage bills to total expenses ratio	0-3.5	3.51-7	7.1-10.5	10.51-14	14.1-17.5	50	50	50	50	50
Wage bills to total income ratio	0-2.5	2.51-5	5.01-7.5	7.51-10	10.1-12.5	40	50	50	50	50
Wage bills to intermediation cost ratio	0-8%	9-16%	17-24%	25-32%	33-40%	50	50	50	50	50
						<b>200</b>	<b>210</b>	<b>250</b>	<b>230</b>	<b>210</b>

Finally, the learning and growth perspective was not better than the customer perspective. The bank has scored almost 100% on No of offices, No of employees (in thousands), No of Debit Cards (in lacs), No of Credit Cards (in lacs) in the year of 2013. These findings show that the bank definitely values its stakeholder's, the employees. However, there has been a decrease in profit per employee, because the number of employees constantly increasing year by year in last five years. Debit and Credit card holder of bank was also increases at faster rate in last year's.

**Table IV : Learning and Growth Perspective Score Assignment**

	SCORE ON SCALE					SCORE ASSIGNMENT				
	10	20	30	40	50	2013	12	11	10	09
<b>LEARNING AND GROWTH</b>										
No of offices	0-600	601-1200	1201-1800	1801-2400	2401-3000	50	50	40	30	30
No of employees (in 000'S)	0-14	14.1-28	28.1-42	42.1-56	56.1-70	50	50	40	40	40
No of Debit Cards (in lacs)	0-32	32.1-64	64.1-96	96.1-128	128.1-160	50	50	40	40	30
No of Credit Cards (in lacs)	0-13	13.1-26	26.1-39	39.1-52	52.1-65	50	50	40	40	40
						<b>200</b>	<b>200</b>	<b>160</b>	<b>150</b>	<b>140</b>

### Conclusion

Designing a single BSC (balanced scorecard) for any organisation is very difficult task. Banks, being a financial service organisation, design and implement BSC model not only difficult but complicated also. Still, it emerges to be an efficient technique to measure the performance of banks. Balanced Scorecard approach helps in understanding the relation among various performance indicators, and make strategy designing & implementation process more efficient.

	SCORE ASSIGNMENT				
	2013	2012	2011	2010	2009
FINANCIAL	390	400	390	380	430
CUSTOMER	190	190	200	200	200
INTERNAL BUSINESS PROCESS	200	210	250	230	210
LEARNING AND GROWTH	200	200	160	150	140
<b>Total score achieved</b>	<b>980</b>	<b>1000</b>	<b>1000</b>	<b>960</b>	<b>980</b>
<b>Total score achieved out of total</b>	<b>1100</b>	<b>1100</b>	<b>1100</b>	<b>1100</b>	<b>1100</b>
<b>% of Score</b>	<b>89%</b>	<b>91%</b>	<b>91%</b>	<b>87%</b>	<b>89%</b>

In respect of HDFC bank, the performance of bank was declined during the first two years of the study, but in the next two years the performance improving. The paper concludes that that the HDFC performance measured by the BSC was 980, 960, 1000, 1000 and 980 for the years 2009-2013 respectively. Converting these scores on a 100% scale yields: 89%, 87%, 91%, 91% and 89% for the same years.

With the financial reforms in full swing, and influx of more private sector and multinational banks in to the economy, it is necessary for banks to adopt such a system of performance measurement it they have a aim to ensure better performance in future. The fact that the RBI has initiated the process to collect data pertaining to many different performance indicators over the past decade can be considered to be good progress in this direction.

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