

Enhancing the Performance of Regional Development Banks

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Abstract—The roles of Regional Development Banks (BPD) in Indonesia are as financial intermediaries and as drivers of the respective regional economy. These roles can be performed optimally if there are synergies undertaken by all stakeholders. This study is expected to contribute to BPD stakeholders in optimizing performance. This research used mixed methods which started with a quantitative process to analyze questionnaire data and secondary data of 26 BPDs. The qualitative process is carried out by in-depth confirmation through interviews of BPD leaders, employees, and customers. In addition to the confirmation, Focus Group Discussions (FGDs) are conducted with BPD officers, the Association of Regional Banks (Asbanda) and the Financial Service Authority (OJK) using the Balanced Scorecard (BSC). The important finding in this research is the performance of an internal process which gives a high perceived value of customer and determined the success of BPDs.

Index Terms—regional development bank, banking performance, balance score card

I. INTRODUCTION

Data of the Financial Service Authority (OJK) at the end of December 2015 indicates that more than half of the total banking capital and market shares of bank intermediation in the form of collection and distribution of banking funds is controlled by the top 10 bank asset ratings. Less than half of the shares are spread over 108 other banks. One of the groups of the remaining 108 banks belongs to the Regional Development Bank (BPD) group. Until March 24, 2017, there are 26 BPDs scattered throughout the territory of Indonesia.

Based on the analysis as a strategic group in which 26 BPDs are combined and considered as an integrated business entity, the total assets of BPDs nationally by the end of December 2015 was recorded at IDR 475 trillion. The asset figures of all BPDs are in the fifth rank of commercial banks nationally under Bank BRI, Bank Mandiri, Bank BCA, and Bank BNI. This figure is equivalent to 7.7% of total assets of all commercial banks nationwide. Based on data as of December 31, 2015, the total average assets of BPDs was recorded as IDR 18.26 trillion, with the highest total asset of IDR 83.03 trillion owned by Bank BJB and the lowest was Rp 4.01 trillion, which is owned by Central Sulawesi Bank. Meanwhile the total average credit of BPDs was recorded at IDR 12.17 trillion, with the highest total credit of IDR 55.31 trillion was owned by Bank BJB and the lowest was IDR 2.53 trillion, which is owned by Central Sulawesi Bank. Total third-party funds (DPK) of BPDs was recorded at IDR 13.28 trillion,

with the highest position of IDR 62.75 trillion was owned by Bank BJB, and the lowest at IDR 2.26 trillion was owned by Central Sulawesi Bank. While the total average equity of BPDs was recorded at IDR 2.29 trillion, the highest was owned by Bank BJB of IDR 7.70 trillion and the lowest of IDR 0.59 trillion was owned by Central Sulawesi Bank. In comparison with the overall average performance of banks in Indonesia, total assets were recorded at IDR 51.10 trillion; total credit of IDR 34.10 trillion; total DPK of IDR 41.35 trillion; and total equity of IDR 6.76 trillion. Based on these facts, it is known that the performance of BPDs nationally was below average.

The banking actors of BPDs realize that the performance is stagnant, but there is an opportunity to become great in their respective regions. BPDs throughout Indonesia with the support of Bank Indonesia together with the Association of Regional Development Banks (Asbanda) completed the Regional Bank Champion (BRC) program. BRC's vision is "to be the region's leading bank through competitive products and services with a professionally managed network in order to foster regional economic growth". After an evaluation of BRC implementation in early 2015, several fundamental problems that needs to be addressed structurally was found: (1) contribution of BPDs to regional development is still low where the share of productive loans only reached 26%; (2) inadequate governance, human resources, risk management and infrastructure that triggered an increase in non-performing loans in the productive segment; and (3) the competitiveness of BPDs is still low because the product and service quality are not adequate. The idea came from OJK and Asbanda that BPDs need to transform to improve structural weakness and strengthen the organizational foundation to be able to grow and compete so that it will play a role in the regional economy in the future. This program is called the BPD Transformation Program, and was inaugurated on May 26, 2015.

Based on the problems exposed, the performance of BPDs in Indonesia is still low compared to the performance of the national commercial banks. While the role of BPDs is very important in order to support development in the region, it should have support from the regional government, including implicit and explicit support for the development of BPR. Implicit support can be provided in the form of funding and funding allocations from the local government. Explicit support can be in the form of regulations that favor the

development of BPRs. Besides those, the closeness with the regional community has not been optimally worked on by the BPR.

The solution to the difference in actual performance, which is still weak, with the strong performance expected in BPD is the goal to be found through this research. This study aims to analyze the performance of BPDs by measuring company performance based on four perspectives namely financial, customer, internal process, and growth as introduced by Norton and Kaplan since 1992, known as the Balanced Scorecard–BSC (2010).

The unit of analysis in this study is the banks incorporated in the category of BPDs in Indonesia. The unit of observation shall be the management of each bank, in this case, the President Director or any party authorized to represent the President Director. In order to obtain relevant, strong and useful results, this study uses complementary data sourced from OJK secondary financial data, FGDs with OJK and Asbanda officials, as well as direct interviews and observations of employees and customers of BPDs.

This research lies in the sphere of strategic management. The results of this study are expected to be useful for use as a consideration for management in the industry of BPDs. Besides that, this research is expected to give thoughtful contribution for OJK and Local Governments as policymakers to determine the direction of BPDs.

II. LITERATURE REVIEW

Performance measurement in the banking sector has been conducted by researchers using various approaches in the literature. Al-Najjar and Kalaf stated that the use of BSC is still relevant in measuring bank performance [1].

According to Kaplan (2010), BSC in measuring performance is done through financial aspects, customers, internal business processes, and learning and growth. The financial perspective is measured by receivables, return on capital employed, and operational costs. Customer perspective is measured by customer satisfaction. Internal business process perspective is measured by rework. Learning and growth perspective is measured by employee's morale and employee's suggestion.

The concepts of the definition of company performance are proposed by many experts. David (2013) stated that financial ratios are used to evaluate strategy. Hahn and Powers stated that banking performance is measured by Return on Asset (ROA) [2]. Deev argued that banks are judged on the basis of three approaches: asset-based approach, market approach, and income approach [3]. Donghun and Madhavan (2010) stated that there are two streams in measuring performance: (1) using accounting measures such as ROA, return on sales (ROS), and Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) in which most studies in management fall within this stream; and (2) using market-based performance measures, particularly assessing divestment performance in terms of stock market reaction (Cumulative Abnormal Return/CAR) in which this approach is the norm in research on

financial topics. Bridoux, Smith, and Grimm stated that the company's performance is measured by operating profits that are measures of profitability insensitive to accounting policies and depreciation, and non-recurring income and expenses related to assets [4]. Garcia-Castro, Ariño, and Canela stated that Market Value Added (MVA) presents several advantages over traditional company performance measures [5].

Based on the above description, there are several dimensions of enterprise performance variables that several previous researchers have found (David (2013); [2]–[5]). For the purpose of this research, the Kaplan and Norton (2010) approach is used because the dimensions they propose are suitable for the purpose and description of this research. These dimensions are: Finance, Customer, Internal Process, and Learning and Growth (Kaplan and Norton(2010)). The development of concept definition for company performance variables in this research is arranged into a construct of company activities to evaluate executed strategy from the financial perspective, customer perspective, internal business process perspective, and learning and growth perspective. The determination of the indicator construct of the dimensions of the firm's performance variables is adjusted to the conditions faced by BPD, which faces problems related to these aspects.

On the Financial Perspectives, the indicators that would determine the performances of BPD are Minimum Capital Requirement (MCR), Non-performing earning assets and non-earning assets towards total earning assets and non-earning assets, Non-performing earning assets to total earning assets, Loan-loss provisioning of financial assets against earning assets, Non-Performing Loan (NPL), ROA, Return on Equity (ROE), Net Interest Margin (NIM), Operational Cost of Operating Income, and Loan to Funding Ratio (LFR).

On the Customer Perspective, the indicators that would determine the performances of BPD are leader quality, whether the service provider is valuable, implementation of expertise and support, and product's level of innovation and quality.

On the Internal Process Perspective, the indicators that would determine the performances of BPD are value chain effectivity and efficiency, operational process application, customer benefits optimization, channel and market expansion, establishing and maintaining a relationship with customers, technology and product development, lifecycle management, and future market identification.

On the Learning and Growth Perspective, the indicators that would determine the performances of BPD are skills, capabilities, and expertise development, sustainable learning climate, and building a leadership and culture of courage.

Based on the recapitulation of the concept definitions on improving the performance of companies from several experts and constructs of variables built for this study, a typology of bank performance improvement as a measure of the achievement of competitive advantage is proposed.

From the Financial Perspective, the source of its performance is business growth and sales over cost growth. The way to increase its performance is by increasing the financial ratios of the BPD. By enhancing the performance, the company

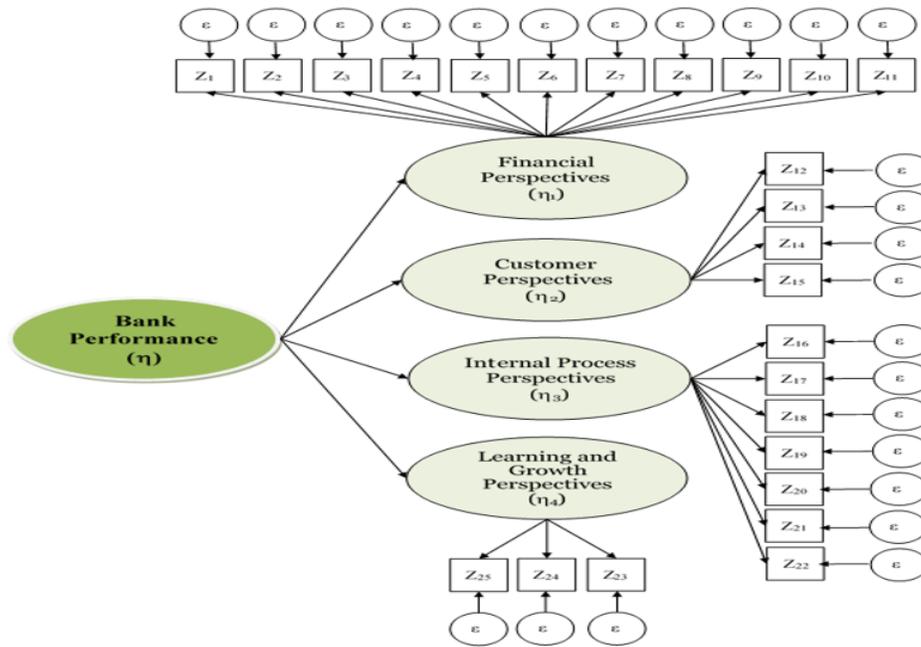


Fig. 1. Hypothesis testing design.

will increase its tangible asset strength. From the Customer Perspective, the source of its performance is customer satisfaction. The way to increase its performance is by increasing and maintaining the relationship with the customer. By enhancing the performance, the company will increase its reputation among existing and new customers.

From the Internal Process Perspective, the source of its performance is effective and efficient operations. The way to increase its performance is by giving the best result at the lowest risk possible. By enhancing the performance, the company will be more capable internally. From the Learning and Growth Perspective, the source of its performance is by organizational learning. The way to increase its performance is by learning new skills and knowledge that would benefit the organization. By enhancing the performance, the company will increase its intangible asset strength.

Based on the description above, a model based on the explanation of the hypothesis is proposed. Below is the model that is proposed for this research.

III. RESEARCH METHODOLOGY

This study aims to obtain a description or describe the studied variables using conclusive research design. According to Malhotra (2010), conclusive research is a study that tests the specific hypotheses as well as testing the specific relationship. Conclusive research design consists of descriptive research and/or causality research [6].

Given the type of research is descriptive and conclusive, the research is conducted through data collection in the field by using survey research methods including descriptive survey, explanatory survey, and observation using a time horizon of cross section/one shot was done at one particular time.

This research utilizes an explanatory design with a two-phase mixed method. The first step is collecting and analyzing the quantitative data, then in the second phase, qualitative data collection and analysis are done to strengthen the result of the quantitative research [7]. The explanatory design includes Mixed Methods Research (MMR) with the philosophical assumption of the inquiry method.

This study was begun with a quantitative (QUAN) phase, beginning with data collection process of BPD's top management opinion through a questionnaire about BPDs on Bank performance. In the QUAN process, the result was the identification of variables from the most dominant level of measure up to the least dominant to get the QUAN conclusion supported by the findings of the previous process.

In the process to identify the result for follow-up, an evaluation of the relevant quantitative findings was followed up in the qualitative phase. Output process identifying the result for follow-up included the formulation of a qualitative (QUAL) problem, list of banking experts as informant candidates for the interview and FGD, questionnaire for each interview and FGD, and a list of development model literature commonly used by the banking industry in Indonesia.

The process of QUAL collection data was done to confirm the QUAN findings by conducting interviews on specific employees emphasized on the perspective of internal processes and growth and learning perspectives. In addition, interviews were also conducted on customers to confirm customer perspectives. FGD banking experts were interviewed to get input on what, how, and why happened as a result of the findings in quantitative.

The solution technique used to be the tool analysis process

TABLE I
MEASUREMENT MODEL OF BANK PERFORMANCE

Dimension	Manifest Variables	Standardized Loadings	R^2	Variance Error
Financial Perspectives	$\eta_{3.1}$	0.159	0.025	0.975
Customer Perspectives	$\eta_{3.2}$	0.912	0.831	0.169
Internal Process Perspectives	$\eta_{3.3}$	0.943	0.890	0.110
Learning and Growth Perspectives	$\eta_{3.4}$	0.797	0.636	0.364
Composite Reliability (CR)				0.830
Average Variance Extracted (AVE)				0.595

Source: Research quantitative result

of QUAN in this research is PLS-SEM. Important considerations when determining to implement PLS-SEM are rooted in the characteristics of the method. According to Hair, et al., there are four important reasons relevant to the application of PLS-SEM [8]: (1) data, (2) model properties, (3) PLS-SEM algorithms, and (4) model evaluation problems.

The data used in this study consists of primary and secondary data. Primary data is data obtained directly from each BPD through questionnaires and interviews. In addition, the primary data was also obtained from interviews with employees and customers, and FGDs with officials from Central Bank of Indonesia (BI), OJK, and Asbanda. Secondary data was obtained from BI, OJK and Asbanda regarding official performance profile of BPDs reported to BI, OJK, and Asbanda, as well as government regulations and policies related to the variables, studied in this study.

Based on secondary data obtained from BI, OJK, and Asbanda, the population of all BPDs in Indonesia until March 24, 2017, was 26 BPD. Given the small population, the unit of analysis in this study is population data of all 26 BPDs in Indonesia. The domain of this research relies on the realm of the middle theory of strategic management that emphasizes the observation of top management behavior in managing the organization.

Recognizing that this study has a small population size and the potential consequences that the predictive validity of the study is lower, the solutions to strengthen the research findings is mixed method research which are: (1) The data collection method was conducted by census to 26 BPDs, and (2) interviews and FGDs were conducted intensively to produce a thick description in the discussion of research findings. Thus in this research, mixed method is very relevant to be implemented.

IV. RESULTS

Based on the result of measurement model with Confirmatory Factor Analysis (CFA), it is found that the dimension of the financial perspective has a much lower loading factor than other dimensions. These results illustrate that quantitative data of: 1) non-performing earning assets and non-earning assets against total earning assets and non-earning assets; 2) non-performing earning assets to total earning assets; 3) CKPN; 4) Gross NPL; 5) NPL Net; and 6) BOPO do not have a close correlation with customer perspective dimensions, internal processes, and learning and growth perspectives. In

line with Henseler, the dimension of the financial perspective will be maintained in measuring financial performance [9]. Considerations to maintain this dimension are: (1) the indicators contained in the dimensions of the financial perspective have positive factor loading, (2) the overall value of CR and AVE is still greater than the minimum.

Based on Table I, it is found that the dimension with the largest loading factor value is the internal process perspective dimension. This dimension is closely related to the capabilities of banks in operational implementation in order to provide the best service for customers.

The following discussion of variables, dimensions, and indicators will describe the individual map so that it can be used in strategic planning. Performance variables are measures that become benchmarks for evaluation strategy used to compare the formulation of goals with the achievements produced by the company. Performance variables are also used to perform control strategies (Kaplan and Norton(2010)). Performance variables are used as a component in evaluating and controlling strategies.

These results indicate that internal processes are closely related to Bank Performance. The most important internal process perspective for the performance measure is the ability of BPDs to optimize benefits for customers. The benefits perceived by customers is the benefit for customers in doing business with BPD. The customer's perceived benefits are reflected in the continuous improvement of the business.

The most important customer perspective used as a performance measure is that the products and services offered have value (perceived value) for the customer. The most important learning and growth perspective used as a performance measure is the ability of management to develop skills and strategic capabilities in every line in BPDs to support performance improvement. Finally, the most important financial perspective used as a performance measure is Gross NPL. It is a comparison of the number of credits that are less current, doubtful, and loss with total credit disbursed.

V. DISCUSSION

Based on the main strategy mapping and complementary strategy mapping, the next strategy should be implemented in an efficient and effective manner. Increased bank performance in the banking industry, especially BPDs in Indonesia, is more likely to be in the perspective of internal processes. The internal process perspective that is supported by technological

adaptation will support all operational work processes performed by the bank so that it can run effectively and efficiently.

Currently, banks' operations require absolute management of information systems. The processes of planning, implementation, and evaluation require information technology. Technological sophistication and capability in the application of information technology in the work will give positive impact to operational performance that is executed. Currently, all BPDs in Indonesia are competing to keep updating the information technology owned. This is reflected in the value of technology spending carried out by BPDs that continues to grow. The relevant internal process perspective is the ability of BPDs to optimize benefits for customers through an effective and efficient internal process. An effective and efficient internal process occurs when the bank's operations are performed with the fastest time and the cheapest cost that minimizes the burden of the bank with the optimum benefits felt by the customer. Optimal benefits are reflected in customer satisfaction to always do business and improve business with the bank on an ongoing basis.

A. Prescription for Key Strategy of Bank Performance Improvement

To spur improvements in bank performance, the results of this study suggest referring to the internal process perspective. Suggestions are addressed for the corporate level, business level, functional level, shareholders and regulators as bank supervisors.

At the Corporate Level, all leaders and employees must be provided with directions that the main performance to be achieved in the long-term vision must be oriented to effective and efficient internal processes through the utilization of information technology. Effective and efficient internal processes range from work planning to customer perceived benefits. Effective and efficient internal processes are the basic attitudes that must be applied in the banking business and will lead to the improvement of other targeted performances.

At the Business Level, competitive and cooperative strategies can be suggested. Competitive Strategies through effective and efficient internal processes are the main weapons that can be offered and are the basis of customer choice to do business with the bank. Ownership of an effective and efficient internal process in serving each customer's transaction needs into competitive advantage must be demonstrated to the market. On the other hand, the cooperative strategy can be considered if the internal process has not been effective and efficient enough. Strategic partners to learn and adopt efficient and effective internal processes must be found so that banks can achieve effective and efficient service performance according to the customer and market needs.

The functional level can be described in four aspects: marketing, finance, operations and human resources (HR). Marketing is emphasized in the fast, effective and efficient internal process-based services that must be understood by marketers and delivered appropriately to meet customer transaction needs. Marketers must educate customers to switch to

full-fledged service quality banking that is the basis of long-term competitive advantage. Finance is emphasized on the allocation of funds for training and knowledge sharing so that employees work effectively and efficiently. This also includes allocation of funds for proper IT installations. Operations are emphasized on optimal operational performance capabilities by effectively utilizing information technology available, zero error target and fraudulent prevention. While the HR with possession of knowledge, skill, and attitude that supports the internal process effective and efficient. Knowledge starts from high standards in employee recruitment followed by education and training that are relevant in supporting the work. Skill is obtained from working hours and the apprenticeship process. Attitude is maintained with a thorough evaluation of the quantity and quality of work of the employees, the tour of duty to avoid dependence on key person and supervision inherent in line with the mandated authority.

Shareholders need to provide support to management to set high standards for service quality based on effective and efficient internal processes. In addition to providing recognition of easily accessible and objective financial performance, shareholders should pay greater attention and appreciation to the achievements of increased customer base, market share width, low customer complaints and anything else related to real reputation in the field and have implications long-term.

Regulators need to play a role in providing greater impetus to banks to deliver effective and efficient internal process-based services through bank rules, circulars, and supervisory processes. Regulators should encourage and create a competitive climate of quality-based bank services. Fast service quality, meticulousness, and high accountability, in the long run, will increase public confidence in the banking system in Indonesia which in turn can reduce the potential of systemic risk.

B. Prescription for Strategy Supplementary Improvement of Bank Performance

In addition to the internal process perspective dimension, the bank's performance variables based on ratings consist of customer perspective, learning and growth perspective, and financial perspective. The customer perspective with the highest indicator is that the products and services offered have value in the customer's perception. The learning and growth perspective with the highest indicator is the ability of management to develop expertise and strategic capability in every line in BPDs to support performance improvement. While the financial perspective which has the highest indicator is NPL Gross—a comparison of the amount of credit status is substandard, doubtful, and stuck with the total credit disbursed.

Based on the above dimensions and indicators, the following prescriptions of complementary strategies are presented to improve bank performance.

The customer perspective with the indicator of the products and services offered which has value in the perceived value of the customer. Banks need to take the hearts of customers to be satisfied with the products and services available with

customer loyalty. The bank's ability to develop products and services available with the appropriate feature attributes needs to be improved. The fact that not all the products and services of the bank owned excel is a necessity. However, most importantly is that the bank must be able to minimize the shortcomings and maximize the owned slaughter. The goal is that customers feel their needs are fulfilled of products and services offered by the bank.

Learning and growth perspective with an indicator of the ability of management must develop skill and strategic capability in every line in BPDs to support performance improvement. Banks should develop knowledge management. Any knowledge and expertise possessed by an individual must belong to the company. Then, the knowledge owned by company is disseminated to other employees related to the needs of knowledge and skills. Banks must regularly undertake a tour of duty. The goal is that the knowledge and skills possessed do not belong to the individual. In addition, the "tour of duty" can be useful in preventing the earliest possible fraudulent occurrence. Financial perspective with the indicator NPL Gross represents the ratio of the number of credits that are substandard, doubtful, and lost with total credit disbursed. Gross NPLs must be compressed with sound credit principles that are profitable from the business side and safe from the side of default risk. Banks need to improve marketers' ability to identify and initiate a preliminary analysis of the proposed credit. Banks must have risk management capable of properly identifying, measuring, monitoring, and controlling risk in every opinion that marketers need as a front end. The bank must also have a competent credit analyst with integrity in conducting a creditworthiness assessment. Finally, banks need to encourage audits to be able to conduct objective investigations to protect the interests of banks to avoid problem loans.

VI. CONCLUSION

Based on the findings of this study, it can be concluded that BPDs have the potential to develop. All stakeholders should have common views to advance BPDs and long-term views. Bank performance can be enhanced as much as possible through an internal process. The perspective of BPD's ability to optimize customer benefits is reflected by customer satisfaction to always and continuously improve business.

Improving bank performance through customer perspective is done by providing products and services that have value (perceived value) for the customer. Learning and growth perspective is done by increasing management's ability to develop strategic skills and capabilities in every line in BPDs to support performance improvement. Financial perspective is done by pressing NPL as low as possible to fit regulatory standards.

For future research, there are several dimensions that could be implemented on other banks and financial institutes which might not have been implemented in other research. Future researchers could use those dimensions as a reference for future research on other samples.

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