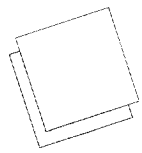
An executive summary for managers and executive readers can be found at the end of this article



Enhancing organizational performance in banks: a systematic approach

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Abstract *To enhance their organizational performance, banks can benefit from the experiences of manufacturing firms and gainfully employ quality and process improvement philosophies with proven track records in manufacturing industries. This article presents a framework, which integrates root cause analysis with benchmarking, process reengineering and continuous improvement. A case study is employed to illustrate the application of the framework and to demonstrate how it can benefit a bank in lowering costs, enhancing productivity, responding to customer demands, reducing complaints and improving customer satisfaction.*

Introduction

A fundamental business challenge

The banking industry now more than at any other time in its history is confronted with a fundamental business challenge – survival and success in a turbulent environment. As they face further deregulation, increasing competition from other financial institutions and continuously evolving customer demands, for success and survival, banks have to adopt proactive approaches (Avkiran, 1999; Shemwell and Yavas, 1998; Yavas and Shemwell, 1997a). At a time when change is the only constant, this is not only desirable, but also a necessity – even if it means navigating uncharted operational and strategic waters.

The premise of this article is that to enhance their organizational performance, banks can benefit from the experiences of manufacturing firms and gainfully employ such quality and process improvement philosophies and related tools as root cause analysis (RCA), benchmarking (BM), process reengineering (PR) and continuous improvement (CI). With this in mind, in this article we offer a practical framework which is capable of assisting bank executives in addressing today's multifaceted challenges.

In the reminder of the article, following a discussion of the operational environment of a bank and the interrelatedness of the back-stage and front-stage operations for success in banking, we present the framework which integrates RCA with BM, PR and CI and capitalizes on their synergies. We then illustrate the application of the framework by a case study and demonstrate its benefits.

Background

A bank's operational environment consists of two stages – back-stage and front-stage. Back-stage where the focus is on efficiency entails operations

that are not directly observable by customers (e.g. check sorting, programming ATM machines, internal audit/control, statement generation). Front-stage operations on the other hand, with an effectiveness focus, include all those tasks and activities that take place at the "moments of truth" or when customers interact directly with customer-contact personnel. Typically, back-stage operations are technology-oriented and front-stage operations are people-oriented. It should, however, be recognized that the two stages are highly interrelated. For instance, a customer request for a fund transfer is considered a front-stage activity. Yet, the mechanism or "know-how" of a fund transfer is within the domain of the back-stage operations. The key is that banking is a service business delivered partly through technology but ultimately through people (Sheshunoff, 1987). As such, investments in back-stage operations (e.g. buying advanced computer systems) by themselves will not result in satisfied customers unless the staff using the system are thoroughly familiar with the system and/or services are provided in a courteous, friendly and competent manner by front-stage personnel (Combs and Bourne, 1995).

Interrelatedness and cohesion

This interrelatedness and cohesion among the activities at the two stages are critical for success in the banking industry (cf. Chen 1999). In contrast, the gaps between the back and front-stage operations are common sources of complaints and dissatisfaction among bank customers (Coskun and Frohlich, 1992; Shemwell and Yavas, 1999) and can be quite detrimental. How effectively a bank can coordinate the two stages affects both functional quality (i.e. service delivery process – how service is delivered) and technical quality (i.e. the outcome of the service – what is delivered) (Grönroos, 1984). These in turn determine the overall organizational performance or the strategic effectiveness of a bank as an operational system. By applying the four managerial and operational philosophies and tools (RCA, BM, PR and CI) in a synergistic and systematic manner, banks can lower costs, reduce customer complaints, enhance productivity, deliver high quality service consistently, improve customer satisfaction and, in sum, reach higher levels of organizational performance.

The framework

Procactive operational and strategic actions

The framework (see Figure 1) stresses that to respond to today's realities effectively, banks need to take a series of proactive operational and strategic actions pertaining to their front and back-stage operations. For instance, they should investigate problems, evaluate solutions, make necessary changes and continuously strive for excellence. In accomplishing these tasks, RCA can be used to investigate and determine the root or real causes of a problem. Internal, competitive or external BM can be employed to identify and determine the best solutions to the problem. PR can be utilized to enact the necessary changes and implement the solution. Finally, CI can be employed to verify and enhance the effectiveness of the reengineered process on an ongoing basis.

In this context, the framework presents a roadmap toward organizational effectiveness. It entails a complete managerial approach which decision-makers can rely on in managing their banks operationally and strategically to attain efficiency, effectiveness, and desired customer and competitive outcomes. The four philosophies and tools which serve as the cornerstones of the framework are briefly discussed next.

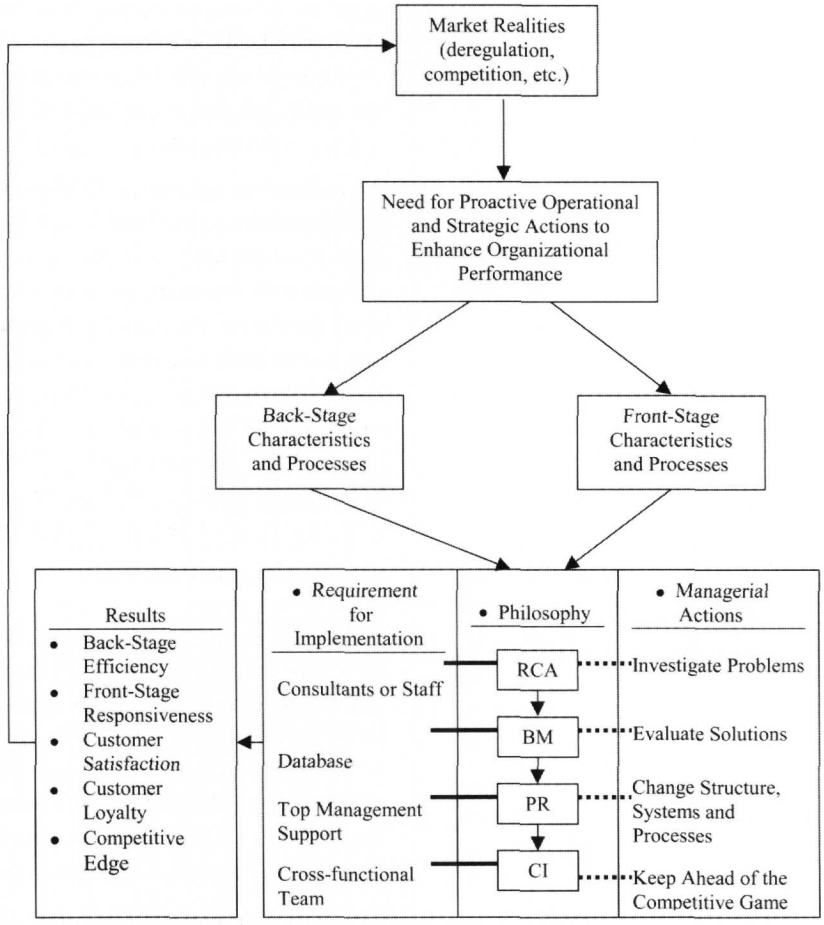

Figure 1. A conceptual framework for enchancing organizational performance

Root cause philosophy

RCA

RCA refers to both a philosophy and a set of specific techniques aimed at discovering the basic reason(s) for the occurrence of unwanted situations, problems, or accidents. The root cause philosophy provides the proper mindset for a customer-focused approach to doing business. It considers satisfaction of customer wants and needs as an end to the organizational processes or means (Dorsch *et al.*, 1997). Furthermore, the actual techniques furnish work teams and managers with both structured and unstructured approaches to problem isolation and rectification and point the way toward potential solutions. In services settings, as is the case in manufacturing, the need to apply RCA may be triggered by customer complaints, failures in responding to customer demands or overall operational deficiencies in delivery systems. In applying the RCA to problem solving and process improvement, it is imperative to draw distinctions among symptoms, apparent causes and actual root causes. Symptoms refer to the tangible indication(s) of a problem. Apparent causes are the actions that create a problem. The root cause, on the other hand, is the least common organizational, personal, or activity denominator of a problem (Wilson *et al.*, 1993).

To delineate the differences among symptoms, apparent causes and root causes at times may be quite difficult. Yet, this differentiation constitutes the essence of the RCA and necessitates a thorough, systematic and detailed analysis of the internal processes and systems. As an example, consider an electronics manufacturer which receives customer complaints due to failing components in an equipment that it produces. A symptomatic fix to the

problem would be simply to exchange the failed components with new components. However, this strategy of mere placation of dissatisfied customers is a superficial solution at best. It does not guarantee that future deliveries of like units will be free of defects since the root cause of the failure is unknown.

Likewise, the treatment of apparent causes can also provide only a shortsighted and inadequate solution to the problem, since the apparent cause may not necessarily be the root cause. Suppose that an initial investigation reveals that the manufacturer's testing and inspection methods/procedures are inadequate and the equipment with failure-prone components easily passes the tests and inspection prior to delivery to the customers. Thereafter, the company would take corrective action to enhance the final testing and inspection phase of the manufacturing and delivery processes. While this may appear to correct the problem from the customers' perspective by preempting future deliveries of faulty components, it does not address the root cause (i.e. what is causing the components to fail in the first place).

Actual root cause of the problem

To find the actual root cause of the problem, there is a need to trace events back to the origin or the least common organizational, personal and/or activity denominator. An inspection of the electronics components may, for instance, reveal that another electronic component, a voltage regulator, may not be operating within the specified parameters, and is thus causing the other components to fail. The root causes, therefore, may be attributed to deficiencies in design and manufacturing procedures. After all, these inadequacies allowed a nonconforming voltage regulator to be installed in the first place. The corrective action then might be as simple as a change in the procedures related to adjustment of voltage regulators.

This example clearly illustrates how RCA can be used to improve quality, productivity and customer satisfaction. A correction of the voltage regulator problem will result in fewer failures of the other components. This in turn will yield savings in the labor and materials used to replace those components. Customer satisfaction will also increase due to fewer failures after delivery. The electronics manufacturer may even be able to attract additional business through an increase in corporate goodwill that stems from the provision of high quality products to customers. Thus, process and system modifications and improvements that are induced as a result of the utilization of RCA may have implications for both the operational efficiency and the strategic effectiveness of the organization.

BM

Systematic process

BM is a systematic process of identifying operational and strategic gaps in an organization and searching for best practices that would eliminate such gaps (Czuchry *et al.*, 1995; Dorsch and Yasin 1998; Spendolini, 1992). There are three basic types of BM – internal, competitive and functional (generic). The BM process itself is essentially the same for each type. The difference lies with what is to be benchmarked and with whom.

In internal BM comparisons are made between an organization's internal activities and processes. This is the typical starting point for the overall BM process since an organization must understand its own activities, or work processes before they can be compared to those of another organization. While best practices may not always be found internally, the main objective of this activity is to uncover practices within the organization. One of the major advantages of internal BM is accessibility to data. Furthermore, there is usually little difficulty in translating the objectives and goals across

departments and functions than with the other BM endeavors. In addition, the results from internal BM are likely to have a more immediate impact due to the shorter process cycle required to conduct the investigation and subsequently incorporate the results, if applicable.

External activity

Competitive BM is an external activity that involves comparisons to a direct competitor's products, services and/or processes, thereby providing keen insights into an organization's position compared with market or industry practices. A primary benefit of competitive BM stems from the fact that organizations in like industries typically utilize similar work processes in delivering products and services. When superior practices are uncovered, this built-in compatibility allows the BM organization to integrate best practices into its internal operations. In fact, many organizations which have already performed internal BM studies are eager to trade information because of this process compatibility.

Logically, competitive BM must follow internal BM, since the internal data must be documented and analyzed before it can be compared to external information. According to experts, organizations that fail in BM efforts do so because they embark on competitive BM before fully understanding their internal work processes. It should, however, be noted that the data required to conduct competitive BM may not be readily available due to the reluctance of competitors to share what may be sensitive or proprietary information. In order to avoid the one-to-one interaction between possible market rivals, many organizations hire third-party consultants to contact competitors and conduct BM on a confidential basis.

Locate best practices

In functional BM, the objective is to locate best practices regardless of their source (e.g. a totally unrelated industry). This type of BM can be especially useful when comparing generic activities such as accounting or marketing that are common to most if not all organizations. In many instances, technologies and practices proven elsewhere can be incorporated into the BM organization's operations with little or no modification. Furthermore, since the partner organizations are not direct competitors, the willingness to cooperate is usually much greater than with competitive BM.

PR

Once the best practices are identified, the next step is PR. While commentators differ in their definitions (see, for example, Davenport and Short, 1990; Hammer and Champy, 1993; Lowenthal, 1994; Petrozzo and Stepper, 1994), the essence of reengineering is to redesign content, scope, flow and structure of tasks and subtasks within an organization to enhance operational and customer-related performance outcomes such as cost, productivity, quality, service, satisfaction and speed. The process typically encompasses fundamental and dramatic shifts in thinking and necessitates cultural as well as technical changes in the organization. While PR has been widely used in manufacturing operations, it lends itself to service operations as demonstrated by Czuchry *et al.* (2000) in a mental healthcare institution.

CI

CI is a philosophy which promotes organizational change based on an ongoing pattern of planning, execution and evaluation of results related to all operations of an organization for the purpose of forever improvement (National Institute of Standards and Technology, 1995). An essential tenet of the CI philosophy is that once operational problems are rectified, the organization must maintain an open-mind for further improvement.

The framework in action

Utility of the framework

To illustrate the application and the utility of the framework, an example is in order. Consider the following case that the authors are familiar with. In an attempt to enhance the efficiency of its back-stage operations, a bank invested in an advanced computerized transactional processing information system. The system would improve the accuracy of the processing and reporting of traditional account-related transactions (e.g. withdrawals, deposits, transfers) and speed up the generation of scheduled statements. Equally important from the customers' perspective, the new system would reduce the waiting time in queues, an endemic source of customer complaints received by front-stage personnel in the bank. Yet after the system became operational, complaints, not only about waiting time, but also about inaccuracies in transactions, started to mount. This apparent failure in back-stage operations, on the one hand, further fueled loss of customer goodwill. On the other hand, it caused moral problems among the frustrated front-stage employees who often became targets of customer wrath.

Realizing that the new transactional processing information system was not working as intended, the bank performed a RCA to figure out what was wrong. The apparent cause of the problem was attributed to the lack of staff familiarity with the operations of the new system. Feeling that the employees, especially the two recently hired tellers, were not brought up to speed on the new system, the bank management initiated a training program. However, the training program did not solve the problem – customer complaints did not subside.

"Parallel conversion strategy"

A more detailed RCA revealed that the root cause of the problem was the utilization of the new system and the old system at the same time. To allow employees time to learn the new system and reduce resistance to change, management had decided to install the new system while the old system was still in operation. Thus, the so-called "parallel conversion strategy" which has its advantages, in this case, had backfired. The new and the old systems maintained two separate databases which were not designed to be updated simultaneously. They lacked the needed interfaces and mechanisms to ensure the compatibility of data in the two databases leading to frequent inaccuracies. Since the two systems and their databases operated under different procedures, the time required to complete a transaction depended on the system used, at times resulting in long waits in line.

Internal BM based on the experiences of another department in the bank which had gone through system upgrade three years earlier proved to be very useful in identifying the best practice to rectify the system conversion problem. At that time, the fund transfer department had changed its system to make it more responsive to customer needs. The objective of the new system was to reduce the actual transfer time, the time required to verify the transfer and the notification of the completion of the transfer to the customer. In that case, a "cutover conversion strategy" which entails doing away with the old system completely and solely relying on the new system had resulted in a very smooth transition. The effectiveness of the cutover conversion strategy was further confirmed by the experiences of one of the system analysts who was involved in a similar case when he was employed with a major insurance company. Thus, "external BM" lended support to the findings from the internal BM effort. Given these, the bank management sought the solution to the current problem in a cutover conversion strategy.

Consequently, the bank initiated a comprehensive PR encompassing all processes, operations and procedures to support the new system. For

instance, the two databases were consolidated and the old database was taken off-line only to be used as a backup for the new database. Additionally, the capabilities of the new transactional processing system was enhanced by enabling customers to have access to their accounts via the Internet.

These changes resulted in several benefits. According to periodic customer satisfaction surveys conducted by the management, overall customer satisfaction with the bank increased from 71 percent to 94 percent. A comparison of customer complaints before and after the implementation of the new system revealed a reduction of 35 percent. Furthermore, in the survey conducted before the implementation of the changes, 68 percent of the customers had indicated that they would recommend the bank to their friends and colleagues. To the delight of management that figure had risen to 89 percent. While the bank did not track waiting time, from their own observations and more importantly from the virtual disappearance of customer complaints, they knew that the waiting time in queue had substantially gone down.

CI team

According to management, all of these improvements were remarkable and, in their view, significantly enhanced the bank's competitive standing and customer goodwill. As one manager put it: "Due to the intangible nature of our business, you can't always assign numbers to improvements. But you know things are better because your customers do not lie to you". Yet realizing that there is always room for improvement and that there is no reason for complacency, management formed a CI team. Consisting of bank managers, staff, customers and outside consultants the objective of the team was to monitor the system and identify and propose plans of action for further improvement.

Concluding remarks

With the challenges they face today, banks have to adopt a proactive approach to the way they do business. The framework offered in this article enables bankers to address and deal with issues pertaining to their back-stage and front-stage operations systematically. It should be noted that the RC, BM, PR and CI philosophies discussed here are not new and they have time-honored traditions in the manufacturing industries. However, their integration in a systematic and coherent manner – the way we propose in our framework – represents a novel approach. Besides the specific benefits discussed above, banks can derive several other benefits from the implementation of the framework.

First, at a time when the banking industry witnesses fierce competitive pressures and faces an increasingly discerning clientele, it allows a bank to differentiate itself strategically from its competitors by improving service quality, enhancing accessibility and responding to customer demands. Second, it can help reduce high costs associated with rectifying problems by anticipating problems before they actually occur and ensuring that the service delivered to the customers is of high quality in the first place. Third, in addition to reducing real costs incurred because of poor service, it can also reduce the hidden costs associated with lost business (e.g. customers' switching banks) due to poor quality service. Finally, it can result in not only improved customer satisfaction, but also employee satisfaction since front-stage personnel will have to deal with fewer consumer complaints. On a closing note, it should be underscored that the illustrative case in this article comes from banking. However, customer complaints emanating from poor service quality and gaps between front and back-stage operations are certainly not limited to banking (Yavas and Shemwell, 1997b). The

framework can easily be adapted for application in other service settings and help these organizations achieve substantial gains in operational efficiency, service quality, customer satisfaction and competitive edge.

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This summary has been provided to allow managers and executives a rapid appreciation of the content of this article. Those with a particular interest in the topic covered may then read the article* in toto *to take advantage of the more comprehensive description of the research undertaken and its results to get the full benefit of the material present

Executive summary and implications for managers and executives

Service industries can benefit from the experience of manufacturing
Service industries can profitably employ quality and process improvement techniques, which have a proven track record in manufacturing industries, to lower costs, enhance productivity, improve responsiveness to customer demands, reduce complaints, deliver high quality service consistently and boost customer satisfaction.

Yavas and Yasin argue that root-cause analysis can be used to investigate and determine the real causes of a problem, benchmarking can be employed to identify the best solutions, process re-engineering can be utilized to enact the necessary changes and continuous improvement can be employed to check and improve the effectiveness of the re-engineered process on an ongoing basis.

Root cause analysis
Root cause analysis is both a philosophy and set of specific techniques to discover the basic reasons for unwanted situations, problems or accidents. Root cause analysis helps organizations to distinguish between symptoms (the tangible indications of a problem), apparent causes (the actions that create a problem) and actual root causes.

Benchmarking
Benchmarking helps organizations to identify gaps in their operations and search for best practices that would eliminate such gaps. Internal benchmarking involves comparisons between an organization's internal activities and processes. It is the usual starting point for benchmarking because an organization must understand its own activities or work processes before it can compare them to those of another organization. Competitive benchmarking involves comparisons with a direct competitor's products, services and processes. One problem with competitive benchmarking is that direct competitors may be unwilling to co-operate. In order to avoid one-to-one interaction between possible rivals, many organizations hire third-party consultants to contact competitors and conduct benchmarking on a confidential basis. The objective of functional benchmarking, meanwhile, is to locate best practices regardless of their source. They could, for example, come from a totally unrelated industry. Functional benchmarking is especially useful when comparing generic activities such as accounting or marketing.

Process re-engineering
Process re-engineering involves redesigning the content, scope, flow and structure of tasks within an organization to reduce costs and increase productivity, quality, service, satisfaction and speed. Process re-engineering typically involves dramatic shifts in thinking and necessitates technical and cultural changes in the organization.

Continuous improvement
Once operational problems are rectified, the organization must maintain an open mind for further improvement. This is a central tenet of continuous improvement.

The framework in action
A bank invested in an advanced computerized system to improve the processing of withdrawals, deposits and transfers, speed up the generation of

statements and reduce queuing. But it led to longer queues and more inaccuracies. The apparent cause was the staff's lack of familiarity with the new system. But training did not solve the problems. A more detailed root cause analysis revealed that the difficulties resulted from using the old and new systems concurrently. The new and old systems maintained two separate databases which were not designed to be updated simultaneously. Internal benchmarking, based on the experiences of another department in the bank which had gone through a similar upgrade three years earlier, helped to identify the best practice to rectify the problem. A system analyst who had been involved in a similar case when employed by an insurance company lent support to the findings of the internal benchmarking. The bank initiated a comprehensive process re-engineering encompassing all processes, operations and procedures to support the new system. A continuous improvement team was set up.

Overall customer satisfaction with the bank increased from 71 percent to 94 percent, customer complaints dropped by 35 percent, waiting time fell and more customers indicated that they would be willing to recommend the bank to friends and colleagues.

Benefits of the techniques

The techniques can help to reduce the high costs associated with rectifying problems by anticipating problems before they occur and ensuring that customers receive high quality service in the first place. The techniques can also reduce the hidden costs associated with lost business because of poor quality service. Finally, the techniques can improve employee satisfaction because staff will have to deal with fewer customer complaints.

(A précis of the article "Enhancing organizational performance in banks: a systematic approach". Supplied by Marketing Consultants for MCB University Press.)