



**Ain Shams University**  
**Faculty of Commerce**  
**Accounting & Auditing Department**

# **The Impact of Adopting BSC on Earnings Quality**

**(An Applied study on the Egyptian Banking Sector)**

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*Thesis*

*Submitted in Fulfillment of the Requirements of  
Master Degree in Accounting*

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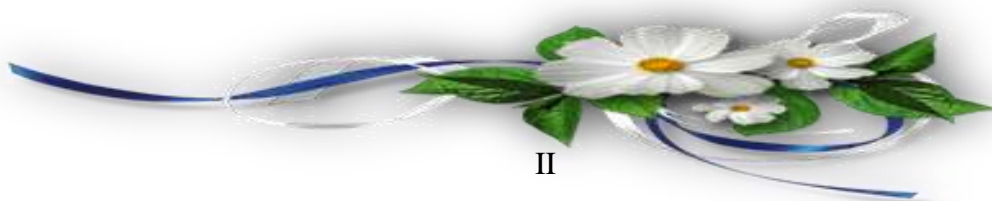
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# **Abstract**

**Shaimaa Sayed Mohamed El-Mehy**

## **The Impact of Adopting BSC on Earnings Quality**

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Nowadays, Banks are facing severe competition and challenges to cope with speedily development in bank's markets. So, banks have to adopt a comprehensive performance management system like balanced scorecard (BSC) to be able to compete and survive. Banks have to not focus merely on financial indicators only. It is essential to give more attention to non-financial measures as well in order to be satisfied with the banks performance and to increase earnings quality of the bank.

This research examined the impact of adopting balanced scorecard on earnings quality. In order to achieve the research objectives a questionnaire was used for non-financial data collection and distributed randomly among the employees working in the Egyptian banking sector, with a total sample size of 290 questionnaires, data were collected and analyzed using the SPSS, while the financial data were collected directly from the financial statements of banks from the time period 2009 to 2016. Four banks were chosen; two of them were publicly held banks; two privately owned bank. The researcher used the statistical program EVIEWS VR. (9) for analyzing the financial data collected from the financial statement.

The most important research result, that there is a significant relationship between using both financial and non-financial measures and increasing banks' earnings quality. Accordingly this will help top level managers to give more attention to areas that need improvement most in order to increase the earnings quality.

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**Keywords:** Balanced scorecard (BSC), Strategy Map, Earnings quality, Egyptian Banking sector.

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# **The General Framework of the Research**

## **1/1 Introduction:**

Banking system in Egypt is a cornerstone of its financial architecture and evidently plays a crucial role in overall economic development and growth. The safety and soundness of banking system is important not only because it prevents economic downturns related to financial panics, but also because it avoids adverse budgetary consequences for governments, which often bear a significant part of the costs of the bailout.

The modern complex economic system cannot function without banks. Banking system is facilitating the personal transactions, such as deposits, remittance of money, lending and borrowing of money. It becomes easier to develop agriculture, industry and trade. At the same time, it helps to accelerate the pace of economic development. Banks help in mobilizing and allocating scarce resources, which are essential for economic development.

Banking sector is an integral part of the broader financial system and constitutes a key provider of finance to business. In general, a healthy, robust and stable banking sector plays a crucial role in supporting economic activity, promoting economic growth, and ensuring financial stability.

Bank's role is essential for each country's economy, since no growth can be achieved unless savings are efficiently channeled into

investment. Therefore, reforming the banking sector and creating a new culture of trust and confidence has been a crucial task in the process of transition to a market economy.

Managers have focused on financial ratios to measure the performance. Moreover, banks need to reevaluate their performance measures to achieve more effective performance.

Traditional methods of measuring banking performance by financial indices alone have virtually disappeared from large organizations. Currently, non-financial measures are at the core of describing strategy and of developing a unique set of performance measures that clearly communicate business strategy. Banks are looking for a strategic performance management tool that links performance to strategy using a multi-dimensional set of financial and non-financial performance measures. <sup>(1)</sup>

It is essential for banking sector to enhance a performance evaluation system that encompasses all aspects of the banking sector, In order to achieve a long term survival, growth and development. Such a system should be able to bring out strengths and weaknesses of the banking sector for the purpose of improvement.

Kaplan and Norton (1992) <sup>(2)</sup> proposed the concept of the balanced scorecard (BSC) to overcome the problems that result from

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(1) Tariq H. Ismail (2007), "Performance evaluation measures in the private sector: Egyptian practice", **Managerial Auditing Journal**, (Vol. 22, No. 5), pp. 503-513.

(2) Robert S. Kaplan & David P. Norton (1992), "The balanced scorecard measures that derive performance", **Harvard Business Review**, (Vol. 70, Iss.1), pp.71–79.

the sole reliance on financial measures while evaluating the business performance. The BSC has been widely adopted in the evaluation of organizational performance from four perspectives: finance, customer, internal business process, and learning and growth. These perspectives are associated with four functions of accounting and finance, marketing, value chains, and human resources, respectively. Each perspective helped top level managers to answer a basic performance question: How does each level of top manager look to shareholders? How do customers see the banking sector? What must top level managers excel at? What top level managers can do to improve and create value? However, studies of how to analyze causal relationship between evaluation criteria, distinguish influential factors, and create an effective mechanism for the establishments of a strategic implementation of evaluation criteria are scarce. Consequently, managers are challenged by the delineation of strategies that can both analytically and organizationally link together performance indicators and performance drivers, while allowing for the implementation of the BSC process.

The balanced scorecard has focused mainly on performance measures without taking into consideration the casual relationship between performance indicators. To enhance performance, balanced scorecard should be incorporated into performance measurement model through constructing feasible strategy map.

Many executives just give their employee limited information about what they should do. That could lead to a quick failure. Because how the employee should achieve a plan that they do not fully understand. Organizations need tools for easily communicating

both their strategy and processes that will help employee implement their strategy.

Strategy map provide such a tool by introduced three principles that link an organization's BSC to its strategy: (1) cause / effect relationships, (2) performance drivers, and (3) linkage to financial goals. Organizations give employees clear and overall lines into how their jobs are linked to the overall objectives of the organization. To make the employees work in a coordinated and collaborative way toward achieving desired goals.<sup>(1)</sup>

The performance measurement scorecard makes a balance between leading and lagging indicators, short and long-term objectives, and external and internal performance perspectives. It also forced management to concentrate on drivers of future performance and not just on past performance. These operational drivers and measures complemented the traditional financial measures, providing a more comprehensive picture of the company's performance.<sup>(2)</sup>

## **1/2 Statement of the Problem**

Because of the intangible nature of the products and services provided by banking institutions, one cannot easily measure the efficiency and competitiveness of banking products and services. Most available researches have focused on measuring the

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(1) Hung-Yi Wu (2012), "Constructing a strategy map for banking institutions with key performance indicators of the balanced scorecard", **Evaluation and Program Planning**, (vol.35, Iss.3), pp.303–320.

(2) Lynn Bible, Stephen Kerr, and Michael Zanini (2007), "The Balanced Scorecard: Here and Back", **Management Accounting Quarterly**, (Vol. 7, No. 4), pp.18-23.

productivity and efficiency of the banking industry by measuring outputs, costs, and performance. Moreover, many of the studies only use financial ratios to evaluate banking performance. Most of the traditional performance measures in banking focus on external financial reporting. However, focusing solely on these external reports has kept banks from long-term planning, growing, innovating, and learning. Furthermore, banks need to completely reassess their performance measurement in order to meet customer needs and requirements. To achieve more effective performance, banks must align their goals with those of their clients' services. <sup>(1)</sup>

In the Banking sector, the survival of the banking sector depends on its ability to both evaluate current performance and identify strategies to improve the quality of planning and control decisions. To help them doing this, banks' managers have used a variety of measurements techniques and performance evaluation tools. Many researchers have tried to examine management accounting practices and performance evaluation measures in developed countries, along with individual benchmarking dimensions. However, there is a lack of empirical researches examining Egyptian banking sector practices of using performance evaluation measures and analyzing factors that may affect the selection of those measures. <sup>(2)</sup>

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(1) Hung-Yi Wu (2012), **op.cit.** , pp. 303–320.

(2) Tariq H. Ismail (2007), **op.cit.** , pp. 503-513.