



Beyond Budgeting
Institute

Case Report

Handelsbanken: Consistency at Its Best

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About Beyond Budgeting Institute and BBRT

The Beyond Budgeting Institute is at the heart of a movement that is searching for ways to build lean, adaptive and ethical enterprises that can sustain superior competitive performance. We promote a set of principles that lead to more dynamic processes and front-line accountability. Organizations that follow this approach transform their management model in line with these principles.

Our ideas are spread through the Beyond Budgeting Round Table (BBRT); a shared learning network of member organizations with a common interest in transforming their performance management models to enable sustained, superior performance. We help organizations learn from worldwide best practice studies and encourage them to share information and experiences to move beyond command and control.

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Handelsbanken: Consistency at its Best

Based on Handelsbanken's unique management model, which was introduced in the early 1970s, the bank has continuously delivered very impressive results. These have been achieved by putting customers first and without the use of traditional management tools such as budgets and forecasts.

Handelsbanken was founded in 1871 and is today one of the largest Nordic banks with 782 branches in 24 countries. The bank has been a listed company since 1873. This makes Handelsbanken the oldest company on the stock exchange in Stockholm and it now has approximately 100,000 shareholders. The second largest shareholder with 10.3 % of shares is The Oktogonen Foundation - a trust that manages the company's employee profit sharing scheme.

Through its branches the bank offers a full range of products and services. Unlike in many other banks the branch network is not merely a distribution channel for its products. In Handelsbanken's case it is the branch that decides which products to offer its customers. The branch is the bank.

Since Dr Jan Wallander, the bank's then new CEO, introduced a new visionary management model in the early 1970s the bank has achieved truly remarkable results: For 41 years in a row - and still counting - the bank has delivered on its goal, which is to achieve a better profitability than the average of comparable banks in its home markets.

Handelsbanken's idea of how to run a successful universal bank is essentially based on trust and respect for the individual - both customers and employees. The model is predicated on the belief that the only sustainable competitive advantage available to a firm in a fast changing world (especially in a service business) lies with its people - especially their creativity, insights and judgment¹. Handelsbanken's model has focus on management through a radically decentralized people-based model. This is in stark contrast to the centralized numbers-driven alternative so prevalent elsewhere.

The author met recently with Frank Vang-Jensen, Handelsbanken's managing director in Denmark and with head of communications Anette Haaning for a talk about the bank's unique management model and how it is working in 2013. In addition to this interview, this case story is based on annual reports and other material published by Handelsbanken, a series of published articles, and on reports made by the Beyond Budgeting research team.

1) This is one of the key messages in Gary Hamel's: The Future of Management, Harvard Business School Press, 2007.

Handelsbanken today

Handelsbanken is a full-service bank with a nationwide branch network in Sweden, the UK, Denmark, Finland, Norway, and the Netherlands. The bank regards these six countries as its home markets. Handelsbanken was founded in 1871 and currently has just over 11,000 employees working in a total of 24 countries.

Since the early 1970s, Handelsbanken's organization has been strongly decentralized and operations are always based on the customer's requirements. This means that all business

decisions regarding individual customers' relationships with the bank are taken close to the customer.

Handelsbanken has more satisfied customers than peer banks, is one of the most cost-effective listed full-service banks in Europe, and every year during the past 41 years has had higher return on equity than the average of peer banks.

The bank grows internationally by establishing its business model on selected markets.



Frank Vang-Jensen, Managing Director. Handelsbanken Denmark

Impressive results without budgets

With the bank's own words, they "got rid of the budgets and liberated their employees". Absolute targets, budgets and detailed forecasts no longer exist in the bank. These have been replaced by a few relative targets. Changing strategy statements from top management are also long gone; instead the business responsibility now lies with the branches that are close to the bank's customers. And the results speak for themselves:

- For 41 years in a row, the bank has lived up to its financial target which is to achieve a shareholder return that is higher than the average of its peers.
- In the Nordic countries, the bank is number one in customer satisfaction ratings.
- In Europe, Handelsbanken is the most cost effective bank, and it has the lowest CDS level and can, therefore, borrow money at the lowest cost on the funding market.
- As opposed to its peers, Handelsbanken did not require any financial support during the recent financial crisis.
- Over the latest five years the bank has delivered a total positive return to its shareholders of 45 %. This is approx. three times higher than the second most successful bank in Europe. The average return of European banks in this period was negative with 68 %.

Handelsbanken's management model

The bank's strategy is clear: It wants to become the best and most profitable universal bank in its home markets. Within this broad statement each region and branch is free to develop its own strategy and marketing plans. Which products to promote and which customers to serve are decisions taken by the branch manager. As a consequence, the bank does not perform any central marketing campaigns. The branch has the best knowledge of the local customers and, consequently, marketing activities are decided locally.



As Frank Vang-Jensen explains: “Our model is founded on the positive view that people can and will perform when given the room to do so.” This is completely in line with the message from the Beyond Budgeting network whose purpose it is to help: “Build empowered and adaptive organizations without losing control”. This is exactly what Handelsbanken has achieved so brilliantly.

In the following we review some of the key elements that make up the bank’s unique management model.

Target setting

Handelsbanken’s goal is to have higher profitability than the average of comparable banks in its home markets. The goal is mainly to be achieved by having more satisfied customers and lower costs than those of its competitors.

When Jan Wallander arrived at the bank in 1970 its policy was to be the largest bank in Sweden. One of his first decisions was to replace this objective with one that read “the best and most profitable bank in Sweden”. Strategic plans and detailed forecasts based on assumptions of size and scale were dismantled. Focus changed from size to profitability.

The wording of the goal has changed marginally during these many years but it continues to be both relevant and ambitious. The beauty of how the bank expresses its goal is that it is simple, ambitious yet not unrealistic, relative to competition, and independent of changing market conditions.

Other than this overall goal, the bank does not operate with centrally controlled targets or budgets. If a branch so wishes it is free to set its own targets informally and they can be shared with the regional manager. One of the reasons is that the business focus is always on profitability and never on volumes. Another key element is a strong belief that absolute targets are not worth the paper they are written on.

To drive performance the bank relies heavily on its culture of continuous improvement. In the words of Jan Wallander: “Managers should not sit down once a year and leave it at that. They should constantly observe how the company is doing and discuss and formulate plans for action as the performance of the company changes or changes in the economic conditions give an indication that something should be done.” Not only managers but informal teams of employees and branches are continuously working together, sharing information and learning from each other in order to do things better all the time.

Radical decentralization

Decentralization is a key element of the bank’s concept. It goes back to the principle of running the bank based on trust and respect for individuals. This approach leads to better and faster decisions close to customers, and it creates commitment and the opportunity for employees to make an impact and do an even better job. This in turn helps the bank to gain more satisfied customers. The high degree of trust is based on a belief in people’s willingness and ability to constantly become more skilled in their work and in their efforts to seek and overcome new challenges.

The organization and work methods are based on the branches’ responsibility for individual customers and not on central units’ responsibility for product areas or market segments. Handelsbanken’s organization is aimed at promoting the interplay between strong branches, highly-trained specialists and efficient support functions.



Figure 1

Handelsbanken's organization is simple and it is focused on the customer (see figure 1).

The model is opposite to most other companies: In Handelsbanken the CEO and the head office groups are there to support the regions and branches.

Today, Handelsbanken has six home markets: Denmark, Sweden, Norway, Finland, the Netherlands and the UK. Each country consists of its own country organization and one or more regional banks.

For every 50-75 branches there is one regional head office. Denmark, for example, with 55 branches represents one of Handelsbankens 14 regional banks. Each branch manager reports directly to the regional head. All the regional heads are part of the group's senior management team. With so many branches to look after, the regional manager has little time for micro-management.

The bank's top management has clearly stated that the degree of decentralization and its long-term success could not have been achieved without abandoning the top down planning and budgeting process. This is regarded as the turning point in this success story.

Customer focus

Handelsbanken aims to achieve its profitability by having more satisfied customers than its competitors. The quality and service level of all customer interactions must therefore live up to - or preferably exceed - customer expectations.

Availability is important for customers so, contrary to many other banks, Handelsbanken is opening new branches at an impressive speed. In the UK for example, the bank opened a new branch every second week in 2012. In addition, the bank has a manned 24 hour service that is open to customers 365 days a year.

Employees in Handelsbanken do not have any variable compensation so they have no incentive to

Creating shareholder value			
Key figures (SEK m)	2012	2009	
Total income	35,062	32,335	Nordic banks, the corresponding figure was on average - 17 %. Handelsbanken was the only large Swedish bank to provide its shareholders with a positive return during these five years. To illustrate the stability and robustness of Handelsbanken we have compared some key figures for 2012 and 2009. In these two years the bank recorded its highest and lowest, respectively, profit for the year since before the financial crises.
Cost/income ratio	46.3 %	47.1 %	
Profit for the year	14,548	10,244	
Total assets	2,387,858	2,122,843	
Return on equity	14.7 %	12.6 %	
Number of employees	11,192	10,821	
During the past five-year period, the Handelsbanken share has generated total return amounting to 45 %. For the other major			



convince the customer that a certain service or product is better. The bank's advice focuses on what is right for the individual customer, not on what is most profitable for the bank in the short run.

The bank's customer focus is very much linked to the before mentioned decentralization. It is the employees in the branches that face the customers and they are responsible for ensuring the high quality through personal assistance and advice. Customers prefer to meet someone who knows them and who lives in their community; and they want to meet someone who can make decisions. This is why the bank provides the branches with such high degree of autonomy. Decisions should be taken as close as possible to the customer.

This again leads to satisfied employees and to better decisions. The latter is seen in the much lower loan losses than the average of peer banks.

The bank closely monitors customer satisfaction. Several times per year every branch is subject to reviews performed by external and independent consultants. Every year, Swedish Quality Index and EPSI carry out independent surveys of customer satisfaction based on a European standard. The results for 2012 showed that Handelsbanken had the most satisfied customers in Sweden. In the other Nordic countries and in the UK, the bank also had top positions among both private and corporate customers.

Cost efficiency

Being cost effective is another strong element of the bank's unique culture. All branches are measured on their cost to income ratio and the results are very impressive: At the aggregate level the bank's cost to income ratio for continued operations was 46.3 % in 2012. The corresponding figure for the average of other Nordic banks was 53.0 %. As in previous years, Handelsbanken had the highest cost effectiveness of the major listed Nordic banks.

A part of the explanation lies in the bank's simple organizational structure and its much leaner central support functions than their peers. The bank spends much less on management and advertising costs are, for example, almost non-existing.

All central functions must justify their cost and service levels towards the branches which are charged for the use and availability of central services. This provides a healthy internal debate with a common purpose: To remain more cost effective than its peers.

Also at branch level there is a strong cost conscious culture. Costs are - by definition - always too high, so employees are constantly doing what they can to reduce costs. Branches are often located at less than prime locations to keep costs down, and they are always looking for better and more effective ways of serving the customers.

Reporting and follow-up

The need for follow-up and control increases with the degree of decentralization. Consequently, the bank's business control system is centralized and monitors profitability and business activity at individual branch office level. Regional banks and other business segments are evaluated on return on equity. Branches are monitored on the cost to income ratio, including risk-weighted cost of capital, the true funding cost and actual loan losses.



Because of the flat hierarchy and fast, open information system, there is no hiding if a problem or a performance blip occurs.

The bank focuses on very few key measures that are deeply embedded in the organization. The same simple measures apply at managerial level and define the bank's competitive position. This is very different from many other companies that use a massive amount of KPI's which sometimes creates more confusion than clarity.

Two key elements of the bank's financial reporting are transparency and benchmarking; elements that go well together. Transparency ensures that the branches know how well they are doing, and benchmarking ensures meaningful comparison when measuring performance. In combination, these elements stimulate learning and continuous improvement.

One very interesting element of the bank's internal reporting is its league table which makes up the first page of its monthly reports. In the table all branches are ranked based on their latest cost to income ratio. This creates an internal peer pressure as all aspire to have a nice standing in the table. This is one good example of creating pressure for performance in a simple way without spending time on setting budget targets and subsequently spending time explaining variances between actual and budget performance.

No bonuses - but profit sharing for all

Another very interesting part of the bank's successful business model is that it has a staff profit sharing scheme instead of bonus programs like almost all other major corporations. Frank Vang-Jensen explains: "We believe that bonuses should be avoided in risk taking operations, mainly because they risk providing the wrong incentives." Consequently, the bank has no bonus program for any members of the board, senior management or for any staff in the branch office operations, who all work on flat salaries. This applies to all employees in the group except for a very limited number of staff in the investment banking operations.

When the bank reaches its goal of a higher return than the average of its peers, a third of the excess is paid into the profit sharing fund which is administered by the Oktogonen Foundation. A remarkable element of the model is that every employee receives an equal allocated amount. "This creates a strong sense of belonging to the family", says Frank Vang-Jensen.

Disbursements can be made when the employee reaches 60 years of age. As the Oktogonen Foundation invests most of its funds in Handelsbanken shares, employees thus have a financial interest in the long-term performance of the bank.

Handelsbanken and the financial crisis

Quote from the CEO in the 2009 annual report: "At fairly regular intervals - every 15 years or so - the financial sector, often in an economic upswing, appears to misjudge the risks in its lending so badly that we talk of a financial crisis. A common denominator prior to these crises seems to be that the financial sector has attempted to grow more quickly than the real economy. Personally, I have always been skeptical about ideas that regard the financial industry as a separate business

sector, just like any other sector. My view is that banking is primarily a support function for the real economy. In other words, sound banking means moving in the same pace as the natural growth in households and companies."

Of all the Swedish listed banks, Handelsbanken is the only one which did not need to issue new shares during the period.



Credit policy

The bank's credit policy is centralized and non-negotiable. It is the same in all markets and it remains unchanged over the business cycle. Credit decisions are made based on the cash flow and repayment capacity of the customer. A weak or uncertain repayment capacity can never be offset by a high margin or by collateral.

Low risk tolerance

Handelsbanken has a low risk tolerance. It avoids high-risk transactions, even if the remuneration may look attractive ref. the credit policy above. The low risk tolerance is maintained through a strong risk culture that is sustainable in the long term and applies to all areas of the bank's activities.

The bank's business model focuses on taking credit risks in the branch office operations. All other risks are therefore minimized. Position-taking is only accepted in customer-driven transactions and only within strictly defined limits.

The bank also seeks to reduce all macro risks, in order to have a business model that is independent of fluctuations in the economy.

Frank Vang-Jensen makes a link to the strong culture of cost consciousness: "We ask every employee in the branch to save a penny wherever they can in their operations. How could management then ever face the organization and explain that the head office had incurred a significant loss due to involvement in high-risk transactions or in speculative position-taking? That would undermine our credibility and it could jeopardize our strong cost culture, which is crucial for the bank."

The combination of low tolerance to risk, a sound capitalization and strong liquidity makes the bank well equipped to cope with difficult and turbulent market conditions.

Consistency at its best

One of the most striking things about Handelsbanken is the consistency in its adherence to the management model and principles from the early 1970s; both in the way it is practiced and in the bank's communication.

When reading annual reports, research reports, case stories, articles, and other available material about the bank, it is remarkable how consistent the bank is in its approach. It is impossible to tell in

Handelsbanken and Beyond Budgeting

Handelsbanken introduced their revolutionary management practices in the early 1970s far ahead of their time. During the 1990s other Nordic companies started to experiment with new management models and outside Europe there are also examples of companies that - to some extent - have implemented principles similar to those of Handelsbanken.

Based on the work and experiences of these pioneers, Jeremy Hope and Robin Fraser wrote the now famous book "Beyond Budgeting" which led to the creation of the international Beyond Budgeting network which is an active and growing membership organization.

Based on the Beyond Budgeting Principles, the organization contributes to changing generally accepted corporate management models to create more flexible, adaptable, and ethical corporations that deliver sustained high performance. Handelsbanken and the Beyond Budgeting network have close ties and Handelsbanken stands as the best practice example of a truly empowered and adaptable organization.

For more information about joining the Beyond Budgeting network, please visit: www.bbtt.org.



which year the specific text was written... the messages, the goal, the principles, and the organization are all the same.

But make no mistake: The bank has a very strong performance culture and continuous improvement is taking place at all times; within the framework and principles from the early 1970s.

The bank's model is both stable and robust and it enables on-going adjustments to an increasingly dynamic and turbulent economy and a demanding competitive environment. Very impressive!