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ORGANIZATIONAL CULTURE,
DIVERSITY OF PERFORMANCE
MEASURES AND ORGANIZATIONAL
PERFORMANCE

BY

FAZLIN ALI

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ORGANIZATIONAL CULTURE, DIVERSITY
OF PERFORMANCE MEASURES AND
ORGANIZATIONAL PERFORMANCE

BY

FAZLIN ALI

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ABSTRACT

This study aims to examine the relationship between the three variables namely, organizational culture, diversity of performance measures used and organizational performance. A total list (2122) of firms registered with the Federation of Malaysian Manufacturers Directory in the year 2006 was used as the sample for this study. Out of this list, 230 questionnaires were received back, that is equal to 10.8% of the targeted respondents. A survey was done using questionnaires to gather data from the respondents. The respondents were chief executive officers, chief financial controllers, managers or executives. The study proposed that there will be a direct relationship between organizational culture and diversity of performance measures used, between organizational culture and organizational performance; and an indirect relationship between organizational culture and organizational performance acting through diversity of performance measures used by organizations. Between the two types of organizational culture values i.e. flexibility culture values and control culture values; it was expected that flexibility culture values gave a dominant influence on the diversity of performance measures used and organizational performance rather than control culture values. The results of direct and indirect effects from this study indicated that there is a relationship between all the three variables. However, the results suggested that in Malaysia, having control culture values as dominant culture of an organization, supplemented by flexibility culture values gave higher contribution to the diversity of performance measures used and organizational performance. Diverse performance measures used that included financial and non financial measures were also found to have a relationship with better organizational performance. This study contributed by adding to the performance measurement system literature on the effect of organizational culture on diversity of performance measures and organizational performance in the context of developing countries.

ملخص البحث

تهدف هذه الدراسة إلى دراسة العلاقة بين ثلاث متغيرات وهي بيئة المنظمات وتنوع مقاييس الأداء المستخدمة و أداء المؤسسات. وقد استخدم قائمة تشمل ٢١٢٢ شركة مسجلة في دليل اتحاد المصنعين الماليزيين لعام ٢٠٠٦ كعينة لهذه الدراسة. وقد تم استقبال ٢٣٠ استبياناً من هذه الشركات أي ١٠,٨% من مجموع الاستبيانات المرسله لغرض إجراء الاحصاء الذي شمل المدراء التنفيذيين أو المدراء الماليين أو المدراء أو الموظفين. وقد عرضت الدراسة وجود علاقة مباشرة بين بيئة المنظمات وتنوع مقاييس الأداء المستخدمة، وبين بيئة المنظمات وأداء المنظمات، وعلاقة غير مباشرة بين بيئة المنظمات وأداء المنظمات عبر تنوع مقاييس الأداء المستخدمة من قبل المنظمات. وتوقعت الدراسة، عند مقارنة نوعي قيم بيئة المنظمات المرنة والصارمة، أن للأولى تأثيراً سائداً على تنوع مقاييس الأداء المستخدمة وأداء المنظمات. وأظهرت النتائج المباشرة وغير المباشرة لهذه الدراسة وجود علاقة بين المتغيرات الثلاثة. وقد وجدت الدراسة أن القيم الصارمة مدعومة من القيم المرنة تعطي دفعاً أكبر تنوع مقاييس الأداء المستخدمة ولأداء المنظمات. وقد استخدمت معايير مالية وغير مالية لتجد بينها علاقة مع أداء المنظمات، وتكمن أهمية الدراسة في إثراء لأنظمة قياس الأداء وأثر بيئة المنظمات على تنوع مقاييس أداء المستخدم وأداء المنظمات في البلدان النامية.

APPROVAL PAGE

I certify that I have supervised and read this study and that in my opinion; it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Accounting.

.....
Dr. Muslim Har Sani Mohamad
Supervisor

I certify that I have read this study and that in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Accounting.

.....
Dr. Nik Nazli Nik Ahmad
Examiner

This dissertation was submitted to the Department of Accounting and is accepted as a partial fulfillment of the requirements for the degree of Master of Accounting.

.....
Dr. Nazli Anum Mohd Ghazali
Head, Department of Accounting

This dissertation was submitted to the Kulliyyah of Economics and Management Sciences and is accepted as a partial fulfillment of the requirement for the degree of Master of Science in Accounting.

.....
Dato' Dr. Jamil Osman
Dean Kulliyyah of Economics and
Management Sciences

DECLARATION

I hereby declare that this dissertation is the result of my own investigations, except where other wise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at IIUM or other institutions.

Fazlin Ali

Signature

Date

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LIST OF ABBREVIATIONNS

BSC	Balance Scorecard
e.g.	for example
i.e.	that is
ibid	(ibidem): in the same place
IIUM	International Islamic University Malaysia
OC	Organizational Culture
PMS	Performance Measurement System
SME	Small Medium Enterprise
UK	United Kingdom
US	United State of America
vs.	versus, against

CHAPTER ONE

INTRODUCTION

1.0 INTRODUCTION

This chapter starts with discussion on the background of the study followed by the research questions. Section 1.3 discusses the motivations and contributions while section 1.4 outlines the organization of the study by chapters.

1.1 BACKGROUND OF THE STUDY

Performance measurement systems have evolved from the 1980's where performance measures that were based on cost accounting measures and other financial measures began to be used (Otley, 2003). Overtime, with the changes in the business environment; focusing on financial measures alone was not adequate for the survival of organizations. This gave rise to the development of performance measurement system which has balance measures with financial and non financial dimensions such as the SMART performance pyramid, result and determinant model and balance scorecard (Kaplan and Norton, 1992; Cross and Lynch, 1992; Fitzgerald, Johnston, Brignall, Silvestro and Voss, 1991).

Findings from several studies have shown that the contemporary performance measurement system has a positive link with performance such as on effectiveness, efficiency and profitability of organizations (Braam and Nijssen, 2004; Evans, 2004). Despite its established link to performance, the implementation of contemporary performance measurement system is still very low such as evidenced in Germany, India, UK and Canada (Kald and Nilsson, 1999; Specbacher, Bischof and Pfeiffer, 2003;

Joshi, 2001; Hudson, Smart and Bourne, 2001; Gosselin, 2005). The case is the same in Malaysia where it is found that there is a low adoption of contemporary performance measurement system (Maliah, Nik Nazli and Norhayati, 2004; Rozhan, 2006)

Studies in Malaysia show that there is a heavy reliance on traditional methods of performance measurement system. Maliah, Nik Nazli and Norhayati (2005) in their study found that 82% of the respondents perceived that the most important function of standard costing is for cost control and performance evaluation. Norma, Ibrahim Kamal and Suzana (2004) in their review of literature of Malaysia, found that studies have proven that Malaysian firms widely utilize traditional management accounting practices for their performance measurement purposes.

Studies on contemporary performance measurement tools that have been implemented in Malaysia reveal that although the firms claim to implement the tools, the concept is not implemented in whole and the model is also underdeveloped (Rozhan, 2006). Partial implementation of the tools result in the creation of several problems including development of unconnected performance measures (Rozhan et al, 2006).

Beside the extend of Performance Measurement System implementation, Performance Measurement System studies also examine the impact of several contingent factors on Performance Measurement System implementation and its impact on the organizational performance (Hoque & James, 2000, Davis & Albright, 2004). Examples of the variables (contingent factors) are firm sizes, market factor, market competitions, perceived environmental uncertainty and organizational cultures (Hoque & James, 2000; Hoque et. al, 2001; Ruzita et. al, 2004; Henri, 2006).

One of the variables used to explain adoption of PMS is organizational culture. Organizational culture is a powerful tool for interpreting organizational life and activities (Allaire & Firsirotu, 1984). It has been argued that organizational culture has

an important impact on shaping the organization and explain the differences in management practices (Fontaine & Richardson, 2003). Therefore, organizational culture can be the basis for understanding the differences that may exist in PMS implementation between organizations.

Besides, Simon (1995 as quoted by Henri, 2006, p77) mentioned that “*the essence of management control system is to manage the tension between creative innovations and predictable goal achievement and to balance the basic organizational dilemma between control and flexibility*”. With high competition due to globalization and fast movement within the business environment nowadays, organizations need to be more flexible in their operation and require diverse performance measures to encourage innovation and creativity. However, Malaysia has a control and more bureaucratic type of culture (Hofstede, 1990) which also proved to use more rigid preset measures i.e. focus on financial measures to achieve predictable preset goals of top management (Henri, 2006). These 2 competing values (i.e. control vs. flexibility) represent the attributes of organizational culture (Quinn, 1988). Therefore, it is interesting to investigate the performance measurement system from the organizational culture perspective because the need of the industry and the local culture is represented in the extremes of the competing value dimension.

Studies on the impact of organizational culture on management control practice and performance found that there is a relationship between them (Henri, 2006; Gosselin, 2005; Balzarova, Castka, Bamber and Sharp, 2006; Denison and Mishra, 1995; Lee and Yu, 2004; Despande, Farley and Webster, 1993; Md Zabid, 2004). Study on adoption of contemporary management accounting tools (Maliah et. al., 2004) also suggests investigating organizational culture to explain the low adoption of contemporary management accounting tools in countries in Asia. These show that

organizational culture may be one of the factors that can explain the scenario of low adoption of contemporary performance measurement system. Therefore, the objective of this study is to **investigate the link between organizational culture, the practice of performance measurement system and organizational performance in Malaysia.**

1.2 RESEARCH QUESTIONS

This study attempts to answer the following research questions about the relationship between organizational culture, practice of performance measurement system and performance in Malaysia:

- (a) Is there any relationship between **organizational culture** and **diversity of performance measures used**?*
- (b) Is there any relationship between **organizational culture** and **organizational performance**?*
- (c) Is there any relationship between **diversity of performance measures used** and **organizational performance**?*
- (d) Is there any indirect relationship between **organizational culture** acting through **diversity of performance measures used** and **organizational performance**?*

1.3 MOTIVATION AND CONTRIBUTION OF THE STUDY

Studies on performance measurement system show that comprehensive performance measurement system that includes financial and non financial measures are needed to guarantee the survival and competitiveness of the firm in the market (Neely, Gregory and Platts, 2005; Yenyurt, 2003; Tangen, 2004; Kaplan and Norton, 1996).

Organizations need to change and adopt the comprehensive performance measurement system. However, Malaysian organizations' show low rates of adoption of this type of performance measurement system (Nik Nazli Nik Ahmad et al, 2003; Maliah Sulaiman et al, 2004, 2005; Norma Omar et al, 2004). Therefore it is interesting to study this phenomenon. Since organizational culture explains organizational life and activities (Allaire and Firsirotu, 1984), it may also hopefully explain the scenario of heavy reliance on traditional performance measurement system in Malaysia and may contribute to this debate.

Further, Kamal Naser, Yusuf Karbhari and Mohammad Zulkifli, (2004) mentioned that in developing countries, very few studies were undertaken to identify factors that influence corporate performance. This study is expected to add to the body of literature on corporate performance, specifically in the context of Malaysia as a developing country.

Both organizational culture and performance measurement system were found to have connections with performance in previous studies (Lee and Yu, 2004; Denison and Mishra, 1995; Hoque and James, 2000; Davis and Albright, 2004; Evans, 2004). However, previous studies examined the role of organizational culture and performance measurement system towards organizational performance separately. This gives the motivation to study the relationship between all the three variables namely organizational culture, practice of performance measurement system and organizational performance together.

Based on the motivations to conduct this study as mentioned above, this study offers several contributions,

- This paper tries to add to the performance measurement system area of research by examining the impact of organizational culture to the

implementation of integrative performance measurement system (financial and non-financial). There are several frameworks used to measure culture such as Hofstede's six dimension of organizational culture (1990) and the solidarity and sociability dimensions of Goffee & Jones (1998). This study will be using the Competing Value Model to operationalize organizational culture. The Competing Value Model framework put the flexible and control dimensions as 2 competing values with characteristics of Hofstede's dimension but clearly differentiates the attributes of control and flexible culture. By using the competing value framework in measuring culture, this paper will provide some insight to the literature acknowledging the notion made by Henri (2004:114) that "to date, there is no published management accounting studies examined performance measurement system from the competing values perspective." (except to his study) and as far as the researcher is concerned there is no such study made in the context of Malaysia as yet.

- This paper attempts to give some insights on the Malaysian perspective i.e. an Asian country on the impact of organizational culture to the implementation of performance measurement system. Chow et al (1999) found evidence that culture influence the design of management control of a firm where they found that organizations owned by US modified their home-country controls to fit local (Taiwanese firms) preference more than the organizations owned by the Japanese. They argued that the findings were due to US culture being more different from Taiwanese culture compared to Japanese culture, so US firms had more to gain by modifying the control system than the Japanese firms. However, this study was based

on national culture instead of organizational culture. Therefore the present study is expected to contribute to give insight on the Malaysian perspective as an Asian country adding to the contribution by Henri (2006) who studied organizational culture in Canada and to test using organizational culture instead of national culture.

- Furthermore this paper will expand Henri's (2006) paper by investigating the possible relationship between the usage of diversity of performance measures to the firm's performance. This will also give some information to the literature on corporate culture and organizational performance as there is a limited study conducted on that matter (Lee and Yu (2004). As evidenced in the literature, implementation of diverse performance measures lead to better performance of an organization, while organizational culture influenced the implementation of diverse performance measures. Studies in Malaysia found that there is low implementation of diverse performance measures. Therefore, this study is important to see the link between the 3 variables and whether the right combination of organizational culture and performance measures implementation will lead to better organizational performance.
- By conducting this study, organizational culture and diversity of performance measures will be determined as factors impacting on Malaysian corporate performance. The result is expected to assist these companies in focusing on these factors to improve their performance by identifying the appropriate culture and appropriate level of diverse performance measures used that is found to suit Malaysian firms and lead to better performance.

- Finally, the use of questionnaire survey to collect the data across a range of manufacturing industries enabled findings to be generalized to a larger population, compared to the use of case study, which has been a focus of several prior studies in performance measurement system and especially organizational culture. Besides, manufacturing firms were used as sample to enable the findings of this study to be compared with the previous studies in Malaysia. This study hopes to further contribute to the studies that examined the level of performance measurement system implementation by providing insight of one of the factor that might influence the level of performance measurement system in Malaysia.

1.4 ORGANIZATION OF THE STUDY

The content of this study is organized into seven chapters. Chapter one provides a brief discussion on the background of the study. It also outlines the research objectives and research questions. Motivations and contributions in conducting this study were also discussed.

Chapter two provides the literature review on performance measurement system. It gives a comprehensive definition of performance measurement system and evolution that happens in the performance measurement system arena. Theoretical discussion and empirical findings on performance measurement system were also presented.

Chapter three provides insights on organizational culture. Both definition of culture and organizational culture were discussed. The competing value model that is used to operationalized organizational culture in this study is outlined in the third chapter. This is followed by discussions on the role of organizational culture on

performance measurement system and performance. Subsequently, Malaysian organizational culture is presented.

Chapter four presents the theoretical framework model proposed for this study. This is followed by discussions about the basis for hypotheses development.

Chapter five is on research methodology. It covers the sample selection and data collection procedures. The research instrument and the pilot testing procedures were presented in detail. Demographic profile of respondents and their companies were also described followed by data analysis tools and procedures.

Chapter six presents and discusses the findings of this study. First, descriptive statistics on the means, standard deviations and the range of variables is presented. This is followed by normality test for the variables. Subsequently, results obtained from the t-test which examine the differences among organizational groups are presented followed by correlation analysis. Finally, this chapter discusses the findings on the hypothesis testing using regression and path analysis.

The last chapter concludes the study by discussing the major findings and its implications. Limitation of the study and suggestions on further research were also discussed.