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Organizational Culture and Performance: Evidence From Microfinance Institutions in Kenya

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Abstract

The study aimed at determining the influence of organizational culture on the performance of microfinance institutions in Kenya. A descriptive cross-sectional survey design was adopted. Secondary data were collected from annual reports by the Association of Microfinance Institutions in Kenya and the Microfinance Rating Africa. Primary data were collected using structured questionnaire targeting the chief executive officer, human resource manager, and marketing manager. Data were analyzed using factor analysis and hierarchical regression. Our analysis identifies clan and hierarchy as the dominant cultural typologies in the microfinance industry. The results obtained demonstrate that organizational culture has a significant influence on non market performance. In addition, market culture is inversely associated with debt/equity ratio. We conclude that organizational culture is a major source of sustainable competitive advantage in the microfinance industry. Furthermore, we conclude that market culture promotes financial independence and sustainability in the long term.

Keywords

organizational culture, performance, competing values framework, debt/equity ratio, microfinance

Introduction

Business firms operating in competitive markets are consistently under pressure to monitor and improve their performance with the goal of meeting the ever-increasing expectations of investors, employees, and customers. Microfinance institutions (MFIs) operate in competitive financial sector characterized by dominant and resource-endowed commercial banks and the member supported savings and credit cooperative societies that enjoy a large number of loyal clientele. Unlike their competitors, majority of MFIs rely on debt from established lenders to provide credit services to their customers. However, developing countries where majority of the MFIs are domiciled have stringent depositor protection regulations that constrain the bulk of nondeposit taking MFIs to mobilize funds from the public. Therefore, exceptional management of organizational resources to compete in the market is essential for the performance of MFIs. Performance relates to the results and outcomes the top management of the firm plans to achieve (Thompson, Strickland, & Gamble, 2008). The upper echelons of firms based in unpredictable and competitive industries spend most of their time and effort in search of answers to performance enhancement questions. The performance management challenge has equally attracted attention of researchers in management. Over the years, studies have attempted to explain how organizational performance can be managed by finding a strategic fit between the firm's diverse range of resources and changes in the external environment. Organizational culture has been identified as an important intangible resource and a barrier to imitation with powerful effects on performance. Schein (1985) proposed that organizational culture serves the dual roles of adaptation to changes in the environment external to the firm and enabling internal integration. Colyer (2000) suggest that performance can be understood better by analyzing organizational culture as firms respond to changing circumstances based on their established culture.

In the wider ethnographic sense, culture relates to the complex whole encompassing knowledge, beliefs, art, ethical habits, and customs acquired by human beings through implicit education and socialization in the society (Geertz, 1973). Although several definitions of organizational culture have been proposed by researchers (Harris, 1998; Hofstede, 1980; Sathe, 1985; Schein, 1999), the basic underlying

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assumptions adopted by the majority of the organizational members are at the core of culture. Whereas assumptions are not directly observable, they are the cerebral level of culture and are inferred from organizational values and artifacts. Assumptions are the mental models used by managers and employees to make sense of the environment (Harris, 1998). Values are the socially constructed principles that guide behavior and are reflected through the spoken and audible goals, philosophies, and strategies. Artifacts are the visual and tangible layer of culture and consist of signage, branding, and physical settings of the establishment.

Cultural values and assumptions build the mental frame for reasoning and responding to stimulus from the business environment. The values and assumptions determine organizational members' perception of time, nature of human activities, and horizontal as well as vertical relationships at the various levels within the organization. The study of organizational culture has attracted a plethora of epistemological perspectives over the years. The current study adopts the competing values framework (CVF) to describe and measure organizational culture in the microfinance industry. The CVF assumes that organizations exhibit two dimensions, namely, environmental focus and internal organization as the central attention (Cameron & Quinn, 1999). The competing values theory assumes that organizational complexity breeds different types of culture (Westrum, 2004) and a single type of culture cannot distinguish an organization (Choi, Seo, Scott, & Martin, 2010; Deshpande, 1993). Therefore, in balancing the requirements of different stakeholders, firms make overt and implicit choices in the degree to which their cultures exhibit values and norms that are representative of four different cultural orientations comprising clan, adhocracy, market, and hierarchy (Choi et al., 2010; Morgan & Vorhies, 2018).

Clan culture focus on human relations (O'Reilly, Chatman, & Caldwell, 1991) demonstrated through internal cohesiveness, employee welfare, loyalty, and employee commitment to the organization. Cameron (2004) describes clan culture as homely and family like working environment. Tseng (2010) observes that employees in clan culture value participatory engagement, teamwork, and consensus building. Adhocracy culture is innovation driven and exhibits flexibility and value creating change. The culture type is characterized by creativity, growth, and variety seeking. Market culture concentrates on productivity, goal attainment, and performance geared toward financial success. Hierarchy culture is depicted by internal efficiency, stability, coordination, and control. Organizations exhibiting this type of culture emphasize security of tenure, predictability, and compliance to rules and regulations. Within the competing values perspective, strong culture with a balanced composition of the four culture types are valuable in enabling managers to deal with conflicting stakeholder demands. Strong cultures are viewed as powerful mediums for signaling employees regarding desirable behaviors and organizational outcomes. Therefore, organizational culture is conceived to determine better deployment of the firm's resources that lead to desirable performance outcome.

Performance outcomes indicate the degree of success in addressing the competing interests of key stakeholders consisting of customers, employees, and shareholders. Literature suggests that business firms assess their performance using both financial indicators and market measures. Financial indicators of performance vary ranging from operating ratios, return on asset (ROA), return on equity, and return on investment. More recently, increased attention has been given to non financial measures of performance with marketing indicators considered alongside financial measures. Organizations that are heavily dependent on debt financing would be expected to broaden the scope of financial indicators of performance to include debt/equity ratio. MFIs draw their capital from debt financing by large, and low interest financial institutions. Therefore, good performance encompasses indicators of self-reliance reflected through debt/equity ratio. Smaller debt/equity ratio signals higher self–reliance, whereas larger ratio indicates debt-trapped MFI. We operationally define performance of MFIs using two dimensions that entail market performance (product development, market share, customer satisfaction, corporate reputation, long-term focus) and financial performance (debt/equity ratio).

MFIs operate in competitive lending market where survival is pegged on abilities by the firm to balance the competing interests of different internal and external stakeholders. Therefore, in balancing the divergent stakeholder interests, MFIs exhibit different values and practices that define their cultural orientations. Despite the common knowledge that majority of MFIs source capital from credit facilities by low-cost large lenders, financial measures of performance have ignored the importance of leverage ratios as indicators of self-reliance. Instead, majority of the studies assessing performance of MFIs rely on ROA. Our study proposes an alternative financial performance measure using debt/equity ratio. Organizational culture plays important roles in internal integration and external adaptation, which together are valuable ingredients for performance outcomes. Although organizational culture provides a relatively stable and frugal pathway to improving performance of the firm, it has received little research attention particularly in emerging industries such as microfinance. Nonetheless, context-specific performance outcomes arising from the influence of organizational culture in industries such as manufacturing and insurance have been established (Kim, Lee, & Yu, 2004). Although previous studies have tested the influence of organizational culture types on performance, the findings are conflicting and inconclusive. Whereas majority of the studies (Morgan & Vorhies, 2018; Yesil & Kaya, 2013) demonstrate that outward looking culture orientations are inclined to impact on performance positively, other scholars (Chatman, Caldwell, O'Reilly, & Doerr, 2014; Fekete & Bocskei, 2011) found positive influence of internally focused

cultures on financial performance. Therefore, the empirical evidence adduced in literature linking organizational culture with performance does not unequivocally rule out context-dependence results. With the hanging clouds of inconsistencies, it is difficult, without multiple evidences across different contexts and over time to conclusively affirm the nature and strength of influence organizational culture has on performance. Our study addresses the question: How do different types of organizational culture influence market performance and financial leverage in the microfinance industry?

To answer the research question, we test the influence of market, adhocracy, clan, and hierarchy organizational cultures on performance. Based on the CVF and extant literature on the subject, we argue that market and adhocracy cultures are sensitive to changes in the external environment that facilitate the firm's adaptation to the developments in the market. Hence, we expect market and adhocracy cultures to have positive relationship with performance of MFIs. We hold the view that because clan culture is people-centered, it has the motivating power on employees; it sustains teamwork and creates synergy leading to higher performance outcomes. In contrast, hierarchy culture breeds structural rigidities making it difficult for the organization to quickly adjust internally and respond fast to changes in the external environment. Therefore, we expect hierarchy culture to be negatively associated with performance of MFIs.

The structure of the article is as follows: We open by describing the topic under investigation, position the topic within relevant theoretical discourse. Next, we review relevant literature on organizational culture and performance relationship. We then proceed to explain the research methodology employed followed by a report on results of the data analysis. We then discuss our findings, draw conclusions, and explore theoretical and practical implications. Finally, we examine limitations of the study and suggest areas identified for further research.

Literature Review and Hypotheses

In the following section, we provide a review of literature covering the link between organizational culture and performance. We make an attempt to present evidence from empirical literature to explain how the different types of organizational culture affect performance. We then consider research hypotheses for testing guided by the CVF and empirical literature.

Organizational Culture and Performance

Culture shared by the majority of organizational members determines how the firm relates with its internal and external environment in the search for solutions to organization's concerns such as performance and survival. Fellows and Liu (2013) argue that culture conditions behavior and in turn, behavior modifies culture thereby, promoting learning by members of the organization and hence, the generation of new answers to performance-oriented questions faced by the firm. Using the positivist paradigm, the current study encapsulates culture as the complex web of basic assumptions, values, and artifacts that describe the identity of an organization. The culture of an organization is portrayed by the dominant leadership styles, communication, organizational processes, structures, systems, and the unique definition of success in the views of particular organizations. Values and beliefs determine structures and systems that are created within an organization and how people behave towards each other. On the contrary, structures and systems affect the attitude of organizational members.

Organizational culture plays a primary function in modeling the behavior and performance of the firm through the collective efforts of individual members of the organization. According to Deal and Kennedy (1982), performance management is the responsibility of top management. Consequently, managers make deliberate efforts toward developing performance-driven organizational culture. To underscore the importance of organizational culture, Bennett, Fadil, and Greenwood (1994) explain that the success of an organization depends on effective alignment between strategy, structure, and culture. Further evidence in support of the influence of organizational culture on performance is reported by Cooper, Cartwright, and Earley (2001) who argue that culture acts as a stabilizer of individual behavior. In addition, Giberson et al. (2009) emphasize that organizational culture is an integrating force that pulls organizational behavior in the direction desired by management.

From a functional perspective, organizational culture is viewed as a means of social control by which behavior and beliefs are shaped and determined (O'Reilly & Chatman, 1996). Despite the trigger role played by organizational culture to influence performance, several studies have reported inconclusive results on the role played by organizational culture in performance management. Empirical evidence positively linking organizational culture with firm performance has been reported by Peters and Waterman (1982), Deal and Kennedy (1982), and Denison and Mishra (1995). Scholars arguing in support of the affirmative link between organizational culture and performance maintain that strong culture is necessary for superior performance because it enhances consistency in organizational performance efforts. On the contrary, Ott (1989) observes that the influence of organizational culture on performance is contingent on other organizational factors and therefore, its relevance may not be universal across organizations. He clarifies that culture is only relevant as a performance-enhancing variable when it is strong and aligned to strategy.

C. M. Byles and Keating (1989) observe that underdeveloped culture may have minimal effect on performance. Therefore, the power of organizational culture to improve performance is presumably determined by organizational culture's potency. However, strong culture may not necessarily

translate to improved performance especially where culture is inconsistent with critical success factors (M. C. Byles, Aupperle, & Arogyaswamy, 1991). Moreover, Quinn and Cameron (1983) raise concerns about culture strength noting that unbalanced strength of different types of culture can be dysfunctional, with the resultant negative organizational performance. Consequently, organizational culture's influence on performance is influenced by its alignment with strategy, structure, and other supportive organizational resources. Culture is considered strong where majority of organizational members share common values and beliefs promoted by leaders of the organization (Deal & Kennedy, 1982). On the contrary, a weak culture occurs where majority of organizational members fail to adopt values and behaviors transmitted by top management. Whereas mixed findings have been reported in literature, we advance the argument that organizational culture supports the implementation of strategy and creates a defense against competitive imitation thereby leading to superior performance outcome.

Studies focused on assessing the influence of the different types of organizational culture on performance have reported mixed findings. Tseng (2010) reported significant positive influence of adhocracy and hierarchical cultures on performance. Similar results were obtained by Calciolari, Prenestini, and Lega (2018). However, Fekete and Bocskei (2011) established that clan and adhocracy cultures were significant positive predictors of performance. They demonstrate that hierarchical culture has negative influence on financial performance. Zhang and Zhu (2012) found contrary evidence with regard to hierarchical culture, but reported significant positive impact of both adhocracy and market cultures on performance. Morgan and Vorhies (2018) support the indirect positive link between market culture and market performance through customer satisfaction. However, they explain that market culture has direct positive effect on financial performance and indirect influence through innovation. In consistent with Choi et al. (2010), who argue that all types of culture are important predictors of performance, Chatman et al. (2014) conclude that all the four types of organizational culture based on CVF has significant positive influence on performance.

Therefore, we hypothesize as follows:

Hypothesis 1a: There is a significant positive relationship between adhocracy culture and market performance of MFIs.

Hypothesis 1b: There is a significant negative relationship between adhocracy culture and debt/equity ratio in the microfinance industry.

Hypothesis 2a: There is a significant positive relationship between market culture and market performance of MFIs.

Hypothesis 2b: There is a significant negative relationship between market culture and debt/equity ratio in the microfinance industry.

Hypothesis 3a: There is a significant positive relationship between clan culture and market performance of MFIs.

Hypothesis 3b: There is a significant negative relationship between clan culture and debt/equity ratio in the microfinance industry.

Hypothesis 4a: There is a significant negative relationship between hierarchy culture and market performance of MFIs.

Hypothesis 4b: There is a significant positive relationship between hierarchy culture and debt/equity ratio in the microfinance industry.

Method

The study adopted a cross-sectional survey aimed at describing the types of organizational culture exhibited by MFIs. The cross-sectional survey was preferred because it enables assessing relationships between variables and making comparisons across observed units. The population of the study encompassed members of the Association of Microfinance Institutions (AMFI) in Kenya. The population consisted of MFIs of different categories and scope of service delivery as follows: five commercial banks offering microfinance services, five wholesale microfinance lenders, 16 deposit-taking microfinance (DTM) institutions, and 29 retail microfinance lenders. Organizational culture indicator (OCI) comprising more than 10 question items on a 5-point rating scale with anchors *not at all* = 1 to *strongly agree* = 5 was used to measure culture. The items included in the scale for example were as follows: "our CEO emphasizes focus on customers and competitors across all departments," "our departmental heads work toward delivering superior value to customers," "management tolerates reasonable degree of error," and "our employees work through teamwork." Financial performance was measured using debt/equity ratio.

Secondary data were extracted from published annual industry performance reports from the AMFI and the Microfinance Rating Africa. Secondary data were used to extract debt/equity ratio. Primary data were obtained using a questionnaire circulated to chief executive officer, human resources manager, and marketing manager in each organization. Average standardized scores for each question and MFI were used to reduce common source bias. The questionnaire was pretested on deposit-taking cooperative societies within Nairobi. A revision of the questionnaire was undertaken after the pretest, and a final draft was prepared for the collection of data. The questionnaire was emailed to all respondents followed by personal visits to respondent organizations by the research assistants.

The Cronbach's alpha coefficient was used to test the reliability of the research instrument. Organizational culture questions collectively returned a reliability coefficient score of .819. On the other hand, the reliability score for performance was .896. The results of Cronbach's alpha coefficient

Table 1. Rotated Factor Matrix.

Organizational culture items	Rescaled			
	Market	Hierarchical	Clan	Adhocracy
Emphasis on customers and competitors by CEO across departments	0.697			
Departmental heads strive to deliver superior customer value	0.582			
Customer satisfaction is the basis of employee rewards	0.761			
Structural adjustments are carried out to adapt to changes in the market		0.768		
Existence of established effective systems, policies, and guidelines		0.702		
Risks are avoided in business practices		0.742		
Employees embrace teamwork			0.775	
Management creates bonding sessions at least once a year			0.826	
Inputs of every employee is considered in management decision			0.8	
Investment in research and innovation				0.809
Focus on external environment takes priority over internal orientation				0.613
Strategies reviewed from time to time to effectively respond to environmental changes				0.62

were above the cut-off limit of .7. Therefore, we confirmed the reliability of our research instrument. Validity concerns were dealt within the current study through pilot testing and adopting established scales that are consistent with CVF. Exploratory factor analysis was used to examine data structure and to test construct validity. The absence of significant cross loadings was used to establish discriminant validity and construct unidimensionality. The extracted average variance for both organizational culture and performance was greater than zero indicating the presence of convergent validity. Normality of the distribution of data was visually inspected through Q-Q plots. Outliers were removed to reduce measurement error.

To identify the types of organizational culture in the microfinance industry, factor analysis was carried out. Before the analysis was done, tests of sampling adequacy comprising Kaiser–Meyer–Olkin (KMO) and Bartlett's test of sphericity were undertaken. Hierarchical linear regression analysis was performed to test the relationship between the four types of culture and performance. Although F statistics was used to test the significance of the regression model, the statistical significance of our hypothesized relationships was tested by examining the p value, standardized beta coefficients and the coefficient of determination. Change in the coefficient of determination (ΔR^2) was used to examine the additional change in the variation of performance attributed to applicable culture type in the relevant models.

Results

Of the 55 MFIs, one could not be located. Therefore, questionnaire was sent out to 54 organizations, but one declined to participate in the study. Fifty-three organizations completed the questionnaire translating to a response rate of 96%. The distribution of firms by age was as follows: 30.2% below 5 years; 30.2% between 5 years and 9 years; 18.9% ranging between 10 years and 14 years; and 20.8% aged 15 years and above. More than half (59%) of MFIs in Kenya had less than 10 branches. Seventeen percent of the firms had between 10 and 19 branches. The results further indicate that 34% of the MFIs offered their services in at least 20 branches across the country. MFIs were in three tiers, where small firms (54.7%) had at most 50 employees, medium firms (20.8%) employed between 51 and 150 people, whereas large firms (24.5%) had more than 150 employees on their payroll.

Types of Organizational Culture

The measurement scale for organizational culture comprised 12 question items measured using a monotonic 5-point rating scale with lower limit of 1 and upper limit of 5; where 1 represented *not at all* and 5 signified *very large extent*. Respondents were asked to rate the extent to which each statement matched cultural traits in their organizations. Table 1 presents the results of factor analysis for organizational culture.

Tests of sampling adequacy were positive with KMO statistic of .781 and a significance of .000 for Bartlett's test of sphericity. In consistent with the CVF, the results in Table 1 demonstrate that four types of organizational culture, namely, market, hierarchical, clan, and adhocracy were present in the microfinance industry albeit at varying levels across the institutions. Strong elements of clan culture were evidently pronounced followed by hierarchy culture and market culture. Moderate presence of adhocracy culture was observed. The results indicate that MFIs in Kenya were largely internally oriented with more focus placed on employee commitment, teamwork, and participatory engagement of employees at the place of work. Teamwork was enhanced through regular bonding sessions and interpersonal interactions. The relative strong presence of hierarchy culture suggests that MFIs

Table 2. Regression Results for Organizational Culture and Market Performance Relationship.

Model	*R*	R^2	Adjusted R^2	*F*	*SE* of the estimate	Change statistics					Durbin-Watson
						R^2 change	*F* change	*df*1	*df*2	Significant *F* change	
1	.582[a]	.338	.325	26.071	.49509	.338	26.071	1	51	.000	
2	.586[b]	.343	.317	13.076	.49806	.005	0.392	1	50	.534	
3	.640[c]	.410	.373	11.330	.47711	.066	5.489	1	49	.023	
4	.708[d]	.502	.460	12.078	.44288	.092	8.866	1	48	.005	2.293

Regression coefficients model		*SE*	Standardized coefficients β	*t*	Significance
1	(Constant)	.370		4.599	.000
	Market culture	.018	.582	5.106	.000
2	(Constant)	.459		4.077	.000
	Market culture	.025	.648	4.143	.000
	Clan culture	.030	–.098	–.626	.534
3	(Constant)	.470		3.150	.003
	Market culture	.025	.561	3.633	.001
	Clan culture	.031	–.236	–1.466	.149
	Hierarchical culture	.026	.331	2.343	.023
4	(Constant)	.458		2.338	.024
	Market culture	.025	.404	2.648	.011
	Clan culture	.029	–.188	–1.253	.216
	Hierarchical culture	.025	.231	1.713	.093
	Adhocracy culture	.021	.360	2.978	.005

preferred order, stability, and predictability. The moderate presence of market and adhocracy cultures illustrate that the firms attempted to balance internal integration with external orientation and adaptation to the environment. MFIs emphasized research and innovation as a way of adapting to the business environment and remaining relevant in the market. The delivery of superior value to customers by employees was prioritized and rewarded by majority of the MFIs.

Relationship Between Organizational Culture and Market Performance

Market performance was measured using a 5-point rating scale based on parameters such as long-term focus, efficiency, customer satisfaction, corporate goal achievement, corporate reputation, outreach and product development among others. Respondents rated the performance of their organizations relative to competitors. Composite scores for each variable were computed through summation of standardized scores in each case. The composite scores were used in the regression analysis. The results of linear regression assessing the association between organizational culture and market performance are displayed in Table 2.

The results presented in Table 2 show that market culture has a statistically significant and positive effect on market performance with a coefficient of determination (R^2) of 0.325. This implies that market culture explains 32.5% of the variation in market performance. The *F* statistics was significant at 0.000 indicating that the regression model was fit for estimating the relationship between market culture and market performance. The standardized beta coefficient of .582 indicates that for every 1% change in organizational culture, there is a corresponding 0.582% change in market performance. Our results support the hypothesis linking market culture with market performance. The results reveal that clan culture does not have significant influence on market performance of MFIs ($\Delta R^2 = .005$, $\Delta F = 0.392$, $p \geq .05$). The results do not support our hypothesis linking clan culture with positive influence on performance. When we control for hierarchical culture in Model 3, the results show significant positive influence on market performance ($\Delta R^2 = .066$, $\Delta F = 5.489$, $p \leq .05$). Contrary to our prediction, we report that hierarchical culture has significant positive influence on performance. In addition, the test of direct influence of hierarchical culture on performance reveals that it explains 24.7% of the variations in market performance ($R^2 = .247$). When we control for adhocracy culture in Model 4, we establish a positive influence on performance ($\Delta R^2 = .092$, $\Delta F = 8.866$, $p \leq .05$). Therefore, our hypothesis linking adhocracy with positive influence on performance is supported. When we

Table 3. Regression Results for Organizational Culture and Debt/Equity Ratio Relationship.

Model summary[a]

Model	*R*	R^2	Adjusted R^2	*F*	*SE* of the estimate	Change statistics					Durbin-Watson
						R^2 change	*F* change	*df*1	*df*2	Significant *F* change	
1	.634[b]	.402	.371	12.773	3.11035	.402	12.773	1	19	.002	
2	.697[c]	.486	.429	8.525	2.96142	.084	2.959	1	18	.103	
3	.717[d]	.514	.429	6.002	2.96319	.028	0.978	1	17	.336	
4	.721[e]	.519	.399	4.320	3.03904	.005	0.162	1	16	.693	2.890

Coefficients[b]

Model		Unstandardized coefficients		Standardized coefficients		
		B	*SE*	β	*t*	Significance
1	(Constant)	14.340	3.427		4.185	.001
	Market culture	–0.607	0.170	–0.634	–3.574	.002
2	(Constant)	8.646	4.648		1.860	.079
	Market culture	–0.836	0.209	–0.873	–3.992	.001
	Clan culture	0.511	0.297	0.376	1.720	.103
3	(Constant)	7.277	4.852		1.500	.152
	Market culture	–0.955	0.241	–0.997	–3.954	.001
	Clan culture	0.398	0.318	0.293	1.252	.227
	Hierarchical culture	0.292	0.295	0.251	0.989	.336
4	(Constant)	6.407	5.426		1.181	.255
	Market culture	–1.013	0.287	–1.057	–3.533	.003
	Clan culture	0.418	0.330	0.308	1.268	.223
	Hierarchical culture	0.290	0.303	0.250	0.958	.352
	Adhocracy culture	0.096	0.239	0.088	0.402	.693

[a]Dependent variable: debt/equity ratio.

test for the direct relationship between adhocracy culture and performance, we establish that the culture explains 35.9% of the variations in organizational performance ($R^2 = .359$). Overall, the results suggest that organizational culture explains 46% of the variations in market performance (adjusted $R^2 = .46$, $F = 12.078$, $p \leq .05$). The results demonstrate that adhocracy culture has better predictive power on market performance than market culture. However, market culture explains variations in market performance better than hierarchical culture.

Relationship Between Organizational Culture and Debt/Equity Ratio

Theoretical postulations in literature point at inconsistencies about the link between organizational culture and financial performance. Although several scholars (Daft, 2007; Kotter & Heskett, 1992; Kriemadis, Pelagdis, & Kartakoullis, 2012) present supporting evidence on the link between organizational culture and performance, the researchers measured the latter construct using subjective indicators. On the contrary, critics (C. M. Byles & Keating, 1989; Ott, 1989) argue that organizational culture do not have significant influence on financial performance. Strong views on organizational culture–performance relationship have been expressed by Kandula (2006) who maintains that culture differentiates performance among various organizations in the same industry. Persuaded by the inconsistencies in literature, the current study sought to empirically determine the significance of the link between organizational culture and financial performance.

Financial performance was measured through debt/equity ratio as the indicator of financial sustainability in the context of MFIs. As culture tends to have a long-term effect on performance, debt/equity ratio was considered a good indicator of financial sustainability in the long term. In addition, debt/equity ratio was treated as an indicator of financial performance from the capitation cost perspective in the microfinance industry. Table 3 presents the results of regression analysis assessing the significance of the relationship between organizational culture and debt/equity ratio.

The results in Table 3 demonstrate that market culture has a statistically significant influence on debt/equity ratio ($R^2 = .371$, $p = .002$, $F = 12.773$). The results indicate that

37.1% of the variation in debt/equity ratio is explained by market culture. *F* statistics was significant at 0.002, which indicates fitness of the model. The negative beta coefficient (standard $\beta = -.634$) means that market culture is inversely related to debt/equity ratio. The results show that for every 1% change in market culture, debt/equity ratio would reduce by 0.634%. The results in Model 2 are not statistically significant (p-value > 0.05); an indication that clan culture is not associated with debt/equity ratio. Hence, our hypothesis is not supported. The results in Models 3 and 4 demonstrate that both hierarchical culture and adhocracy do not have significant influence on debt/equity ratio (p-value > 0.05). Hence, our hypotheses are not supported. Generally, organizational culture explains 39.9% of the variation in debt/equity ratio.

Discussion

Organizational culture and firm performance has attracted significant research attention. Theoretically, organizational culture has been associated with performance through the former's influence on employee attitude and behavior. Literature suggests that the strength of organizational culture and its alignment to strategy and structure are important in explaining the performance of the firm. Firms that are successful in aligning their strategy and structure to organizational culture create competitive advantage that consequently leads to long-term performance. Ogbonna and Harris (2000) uphold the view that the congruence between organizational culture and strategy creates superior performance. Empirical evidence presented in previous studies (Denison & Mishra, 1995; Kotter & Heskett, 1992) demonstrates that organizational culture is associated with long-term performance of the firm.

In the current study, it was established that organizational culture significantly ($R^2 = .46$, $p \leq .05$) explained market performance. The finding is consistent with previous findings obtained by Peters and Waterman (1982), Denison and Mishra (1995), and Ortiz and Arnborg (2005). However, our results run contrary to findings reported by Ott (1989) and C. M. Byles and Keating (1989) who call attention to the negative relationship between culture and performance. Nevertheless, organizational culture tends to influence performance in the long term rather than in the short term. This is accentuated by the fact that the development of cultural values shared by the majority of organizational members takes time. Schein (1990) observes that the development of cultural values stems from a learning process wherein the organization attempts to cope with the complex problem of integrating the internal environment to proactively respond and adapt to the business environment. In the process, the success and mistakes made over time generate further lessons that either reinforce or change the existing cultural values. Hence, organizational culture holds an important role in enabling the firm to uniquely adapt to the market in ways that generate sustainable competitive advantage and eventually deliver superior performance. Once developed, culture tends to be stable in the long run unless a major disruption occurs in the environment. Therefore, organizational culture is unlikely to deliver short-term performance gains particularly at the formative stages of the development of corporate values. In addition, a major change in the environment may require internal organizational readjustment including modifying employee behavior by developing and promoting new cultural values capable of coping with the disruption. Consequently, readjustment of the internal environment whenever necessary and realigning organizational culture and strategy may delay short-term performance gains. Hence, it may be premature to expect a weak or unstable culture to affect performance positively.

Adhocracy, market, and hierarchical culture were found to have significant positive influence on performance. Our findings support earlier results reported by Chatman and colleagues (2014), but differ on the generalization made by them on the influence of all types of culture on performance. We did not find support for clan culture. Therefore, we argue that externally oriented culture are better predictors of market performance, but are supported by internal integration of the firm through hierarchical culture. Our findings are consistent with Morgan and Vorhies (2018), but improve on their results by clarifying the critical role played by adhocracy in boosting performance outcome. Like market culture, adhocracy supports speedy adjustment by the organization to external environment, hence influencing performance. Market culture is linked to performance through market-oriented posture and responding to customer needs through value-creating strategies that lead to customer loyalty. Craig (2010) argues that market-oriented organizational culture instills better treatment of employees to enable them continue creating customer value. Hence, market culture strikes a balance between external orientation and internal focus. The degree to which the firm adopts market culture could affect its market performance. Organizational culture is essential for setting employee's mind frame in the formulation and appropriate implementation of market-driven strategies. Organizational culture sets the stage for matching organizational capabilities with opportunities in the market. However, the relevance of organizational culture in driving better performance outcome holds on condition that it responds at the right time and in a competitive manner to changes in the business environment.

The results demonstrating a significant relationship between market culture and debt/equity ratio are consistent with the findings obtained by Kotter and Heskett (1992), Fekete & Bocskei (2011) who empirically established a positive link between organizational culture and financial outcomes. Kotter and Heskett (1992) specifically established that organizations with strong culture had more revenues, higher share price, and improved net income as compared with their counterparts with weaker cultures. Although views are split on whether organizational culture has direct

or indirect influence on financial performance, Peters and Waterman (1982) identified a direct link. More evidence was provided by the causal study by Denison (1990) stretching over 15 years that directly linked organizational culture with profitability. In contrast, Ogbonna and Harris (2000) found mixed support depending on cultural orientation. They report that only externally oriented organizational culture was linked to performance. The inverse relationship between organizational culture and debt/equity ratio in the current study implies an inverse relationship where organizational culture in the microfinance industry supports the generation of funds from within. This implies that the prevailing dominant organizational culture instills the values of financial independence and discourages borrowing as an alternative to managing capitation. Although organizations may face financial constraints that necessitate seeking external financing, organizational culture shapes leadership attitude toward risks and the extent to which the organization relies on external lenders to provide financial solutions to the firm. Therefore, organizational culture guides managers in making decisions regarding trade-off between debt and equity.

Conclusion

The study set out to determine the influence of different types of organizational culture on market and financial performance. A descriptive survey was undertaken, and primary data were collected using structured questionnaire. Secondary data were extracted from annual reports by the AMFI in Kenya. Data were analyzed through factor analysis and linear regression. Our study identified clan culture as the dominant type of organizational culture in the microfinance industry. On the basis of factor analysis, we conclude that MFIs in Kenya are characterized by the four types of cultures suggested by the CVF. However, the inward looking and stability-preferring cultures are more established than the outward-oriented cultures of market and adhocracy. Our results demonstrate that market culture is a good statistical predictor of both market performance and financial leverage. As culture is unique to each organization, it can neither be mimicked nor destroyed by competitors. Culture delivers a differentiating advantage that forms a foundation for building competitive advantage. Therefore, we conclude that strong culture aligned to organizational strategy and structure is a dominant source of sustainable competitive advantage. The results linking market culture with debt/equity ratio is a good indicator of financial sustainability. Firms that reduce the ratio of their debt to equity in the management of financial resources tend to grow at a slower rate, but more sustainably. Consequently, we conclude that strong market culture provides internally generated financial solutions, reduces dependence on lenders, and increases long-term financial sustainability of the organization.

Implications of the Study

Our results have implications to both theory and practice. With regard to theory, our findings support the postulations of the CVF and maintain that a balanced organizational culture comprising market, adhocracy, hierarchy and clan cultures is essential for superior performance. However, our findings suggest that market orientation is the most important culture for managing financial sustainability of the firm. We view hierarchy as an important culture in setting ideal internal conditions that support market and adhocracy cultures to manage organizational adaptation to the environment. Whereas, a high correlation was noted between clan culture and market culture, we hold the opinion that clan culture do not have direct link to performance, but potentially creates competitive advantage upon which externally oriented cultures mount market response strategies. Pertaining to practice, we demonstrate that culture management could be a significant game changer in performance management. MFIs in Kenya appear to be emphasizing internally oriented culture than promoting externally focused culture. Considering the role of market and adhocracy culture, our findings suggest that promotion of market culture could improve internal generation of funds and create more sustainable institutions.

Limitations and Suggestions for Future Research

Our study is not without limitations. First, we relied on cross-sectional research design that lacks the ability to test causality. Therefore, our findings must be interpreted with caution, as we do not imply cause effect relationship between organizational culture types and performance. Second, whereas we have contributed to performance measurement by testing the link between culture and debt/equity ratio, we have used a single indicator of financial measure. A broad-based indicator would yield more reliable findings. Third, our study was based on MFIs in Kenya. Therefore, our results suffer limited generalization. The nonsignificant result for clan culture opens a window for further investigation. We recommend that future researchers need to investigate further the role of clan culture on performance. In addition, we urge future researchers to investigate the impact of adhocracy culture on financial performance. Finally, we recommend triangulation of methods by future researchers interested in organizational culture studies.

Declaration of Conflicting Interests

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