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THE RELATIONSHIP BETWEEN ORGANIZATIONAL CULTURE, RISK MANAGEMENT AND ORGANIZATIONAL PERFORMANCE

Review
Article

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Performance management;
Bank culture;
Risk management;
Denison model (2006);
Matis model (2013)*

JEL Classification

Z10, D23, G21, G32

Abstract

This article critically aims to demonstrate the relationship between three variables: organizational culture, risk management and organizational performance. The main factor is organizational culture and how it impacts on the risk management and performance of the organization. The research also focuses on the influence of organizational culture on performance and risk management in the bank sector. This paper is based on secondary literature which reviews analytical research of multifaceted data, such as peer-reviewed journal articles, university textbooks, internet resources, etc. Organizational culture represents one of the key variables impacting organizational performance. Organizational culture develops when the culture and principles of the employees are compatible with the culture and principles of the institution and it reflects high performance and efficiency. Moreover, the perception of risk and risk management influence the organizational culture. This is then reflected in the strategic management and performance as the combination of efficiency and effectiveness. This study also emphasizes the importance for banks and other organizations to create or apply an efficient framework, for the risk events identification, analysis and monitoring.

INTRODUCTION

Culture can be a very complex issue hard to measure as it involves behaviors and attitudes (Crémer, 1993). The Financial Stability Board stressed the importance of the great effort the institutions and managers had to make in order to understand an institution's culture and how this affects its safety, and to accordingly develop their performance in an efficient way (Dudley, 2014). Managerial and organizational behavior (OB) concept of organizational culture is easy neither to depict nor to analyze. Many business researchers have measured the impact of culture on economic behavior. Volumes of research work have focused on the concept of culture which is generally defined as "the customary viewpoints and ideas that ethnic, religious and social groups transmit comparatively equally across generations (Williams, 1983; Steinmetz, 1999). This research paper views organizational culture as a consequence of economic activity, and not as its mere generator. The literature in the field presents several conceptualizations of organizational culture, and this paper addresses the competing values framework (CVF).

The objective of this study can be summarized along these three strands:

- I. The first objective is to define organizational culture and the way culture has been regarded at the group level.
- II. The second goal is to introduce a framework to diagnose the attributes of organizational culture and organizational performance and effectiveness by reviewing previous studies on the topic and also by explaining Denison's Models of Culture and Effectiveness.
- III. The final objective centres on the relationship between Bank Culture, Risk Management and Performance in Banking Sector and examines practical ways and models in which a bank can undertake a change from the current to the preferred culture.

As mentioned, this article was based on reviewing ideas and models from previous studies on organizational culture.

METHODOLOGY

What distinguishes scientific research is that it allows us to know other views and the efforts and research knowledge of the past are important for any new study which starts from these findings and recommendations. The models in scientific approaches use the qualitative, descriptive or explanatory methods. The secondary literature reviews of analytical research from journal articles, books and internet resources will be used in order to achieve the objectives of this study.

LITERATURE REVIEW

The culture at the group level

Organizational culture is defined as a set of common beliefs and values that influence how employees think, feel, and act in the workplace (Schein, 2011).

The culture at the group point refers to the quadrant with elevated elasticity and an inner centre of attention. Dynamics at the group level of analysis are fairly important since a group's membership relates to a firmly held significance. The cultures at this organizational level also place importance on cohesiveness, joint decision-making and selfless support among co-workers. Managers support and influence these principles by utilizing methods, such as empowerment, mentoring, and support of teamwork (Gregory et al., 2009). In general, we can say that culture can be defined in different dimensions. Liker & Hoseus (2008) defined culture according to the population as can be seen in Figure 1, which demonstrates the impact of both national and industry cultures on organizational culture. First, national culture affects people's perception of the world it represents as a mental schema that nationals usually have in common. There can be many subcultures in the same organization. Thus, Schein (1984) holds that an organization may contain multiple cultures. Subcultures may stem from the occupational background which can affect the culture in the organization: a marketing culture, financing culture, engineering culture etc.

The significant relation between organizational culture and organizational performance

One of the most popular definitions of performance management states that the organization must focus on improving the employees' self-performance, the capabilities of teamwork and the contribution of individuals to maintaining the continued success and effective performance of the organization as a whole" (Armstrong and Baron, 1998).

In Table No. 1 we will review some of the previous studies on the important relationship between organizational culture and performance from 1982 to 2010.

Culture represents a multifaceted phenomenon stemming from basic viewpoints and assumptions to observable building blocks and practices. A large dose of positive uncertainty also prevails in determining whether organizational culture can be "assessed through a prism of relative wisdom. Primary investigation connecting organizational culture and effectiveness tends to be fairly restricted by lack of agreement on the most suitable measures of effectiveness (Denison et al., 2004). See Figures 2 and 3.

Denison's model in Figure 2 identifies four main dimensions of effective organizational culture: adaptability, mission, involvement and consistency. Adaptability and mission are two quadrants representing external aspects while involvement and consistency are internally focused quadrants. Employee involvement is considered a flexible element of internal focus, while adaptability is an element of external focus. Consistency represents the stable internal element and mission is the stable building block of external focus (Denison et al., 2004).

While according to Denison & Spreitzer (1991), McDermott & Stock (1999), Škerlavaj et al. (2007), cultures tend to be situated on a two-dimensional (X-Y) grid, this model is based on four main axes. Internal and external focus cover both ends of a horizontal continuum, with the group and hierarchical culture on the internal focus and developmental and rational on the external focus. Vertical (Y) axis depicts control and flexibility levels whereas hierarchical and rational cultures have the highest control levels as opposed to the group and developmental with the highest flexibility levels (Figure 3).

The relationship between culture, risk management and the performance of banks

As for the bank culture, it must support the bank's objectives and strategies which are centered on growth and profits. Where culture affects all aspects of decision-making. Culture in bank sectors goes beyond values and beliefs; it extends to its all operational parts, starts from hiring employees, salaries all HR processes, to profitability and resources allocation, managing risks and opportunities (Fiordelisi & Martelli, 2011). Therefore, it is very important for financial institutions and all their managers and supervisors to understand the culture of the institution so that envisaged investments improve their performance, profitability and integrity.

Stulz (2016) mentioned bank supervisors' focus on risk management and risk awareness as one of the key factors of the bank's strong culture. Risk management should be an integral part of banking management and their institutional culture and practices (Song & Thakor, 2018). "Risk management should be an integral part of management, embedded in the culture and practices, and tailored to the business processes of the organization (ISO 31000, 2009)" (Purdy, 2010). The necessity to connect modern risk management practices with organizational culture was emphasized by Douglas et al. (2012). However, more discussions and understandings are still required to establish and identify the link between organization cultural values and risk management practices. Moreover, the alignment of risk management with the organizational culture and its

values represents a fundamental change in that organization which can be rejected if there is any inconsistency in cultural values. According to that, the risk management system must contain the constantly monitored and adjustable processes of : strategy determination, techniques and methods of risk measurements, and corporatist organizational culture (Matis, 2013; Popa, 2013; Dyck et al., 2005).

There are several research models that have attempted to explain the concept of organizational culture. In this article, two main models have been taken into consideration: Denison et al. (2006), who discussed the impact of organizational culture on all performance elements; the second model, the Matis model (2013), about the relationship of Organizational Culture, Risk management and Bank's Performance.

The main reasons for choosing the Denison model for organizational culture can be summarized in the following points:

- It analyzes how organizational culture affects performance.
- It represents the culture of many institutions and organizations, including financial institutions and banks.
- It is a reliable model and has been confirmed by many researchers.
- It studies the culture effects on performance at all levels of the organization. As it is shown in Figure 4.

This model was divided into two main categories:

- **Objective measures** which reflect the four dimensions of organizational culture: Adaptability, Mission, Consistency and Involvement.

- **Subjective measures** of organizational performance consist of 9 elements that reflect respondents' perception of Objective measures.

This model is one of the most specific models that explains the impact of organizational culture on all elements of performance that deal with the organization from inside (eg leadership, strategy, products, services...) and outside (eg, people, society etc.). They believe that each of the organizational culture elements can affect subjective enablers and influence the results criteria of organizational performance components.

Banking literature has lately been focusing on risk management development and their relation to performance. It especially emphasizes the importance of bank risk management under crisis conditions. There is a direct relationship between bank performance with both parties, the components of organizational culture and risk management strategies and methods. This is clearly shown in Figure 5 by the second model proposed by Matis (2013). It is important to note that bank culture must have prepared policies and procedures (P&P) to maintain and develop their performance. A bank culture must consider a risk management

system to be able to quickly assess all significant risk sources, their different types of interdependencies and changes in risk type(s) and exposure(s) over time. The financial crises of 2000-2001 and 2008-2009 revealed serious flaws in risk management approaches applicable to the biggest banks in the world. This model is closely related to:

- i. bank culture,
- ii. strategic management (preparation of senior/top management)
- iii. its performance.

CONCLUSIONS

The literature on organizational culture and performance revealed that banks and institutions that know how to develop their cultures effectively, must support advanced productivity and promote better quality of work life among employees.

It is important for banks and organizations to create or apply an efficient approach for risk events identification, analysis and monitoring. This was clearly stated in both Thakor's (2016) and Stulz's (2016) studies, where they emphasized that one of the key factors for strong bank culture is bank supervisors' focus on the risk management process and strategy.

Risk and risk management influences organizational culture, which is reflected in the strategic management and performance as the combination of efficiency and effectiveness. However, the alignment of risk management, organizational culture and its values is a fundamental change in that organization because it can be rejected if there is any inconsistency in cultural values. In the end, more discussions and in-depth analyses are still required to establish and identify the link between organization cultural values and risk management practices.

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APPENDICES

Table 1. Previous literary studies of organizational culture and performance

Researcher	Year	Results
Peters and Waterman	1982	High productive organizations are in relationship with strong culture
Murphy and Cleveland	1995	Research on culture will contribute to the understanding of performance management
Chung and Haddad	2001	The results confirm a positive relation between culture, performance and marginal industry effect between banks and hotels
Magee	2002	If the impact of organizational culture is not taken into consideration, organizational practices such as performance management could be counterproductive because they are interdependent so that a change in one will impact the other.
Kandula	2006	The key to good performance is a strong culture. Two organizations in the same industry and in the same location: the one with a positive and strong culture can achieve a better performance than the other
Asree, Zain and Rizal	2010	Leadership competence and the organizational culture are important factors which impact on responsiveness and performance of firms

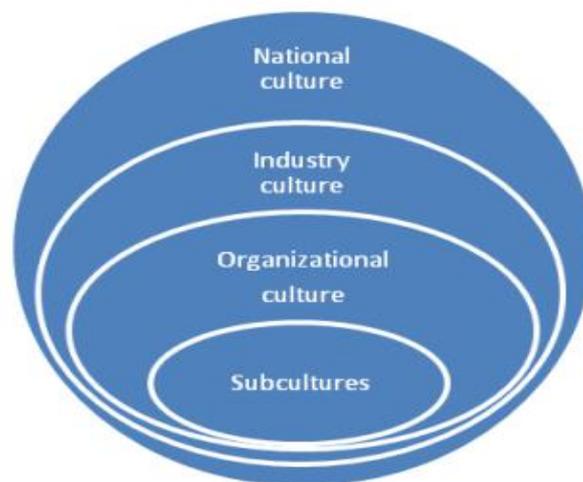


Figure 1. Different cultural populations and their impact on organizational culture freely interpreted.
 Sources:Liker & Hoseus (2008).

External focus	Adaptability	Mission
	<ul style="list-style-type: none"> · creating change · customer focus · organizational learning · 	<ul style="list-style-type: none"> · strategic direction · goals · vision
Internal focus	Involvement	Consistency
	<ul style="list-style-type: none"> · empowerment · team orientation · capability development · 	<ul style="list-style-type: none"> · core values · agreement · coordination / integration
	Flexible	Stable

Figure 2. Denison’s Model of Culture and Effectiveness
Source: Davidson (2003) 49; Zakari, Poku, & Owusu-Ansah, W. (2013)

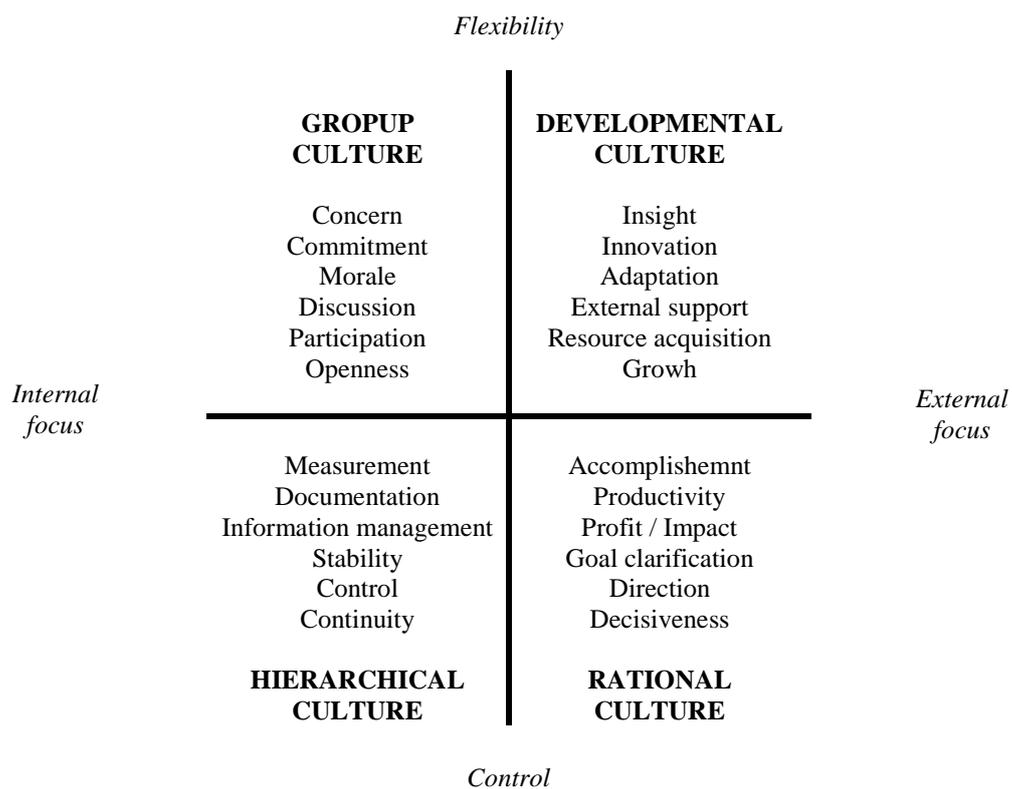


Figure 3. Structure depicting values framework
Source: Denison & Spreitzer, 1991; McDermott & Stock, 1999; Škerlavaj, M., Štemberger, M.I., Škrinjar, R. & Dimovski, V. 2007

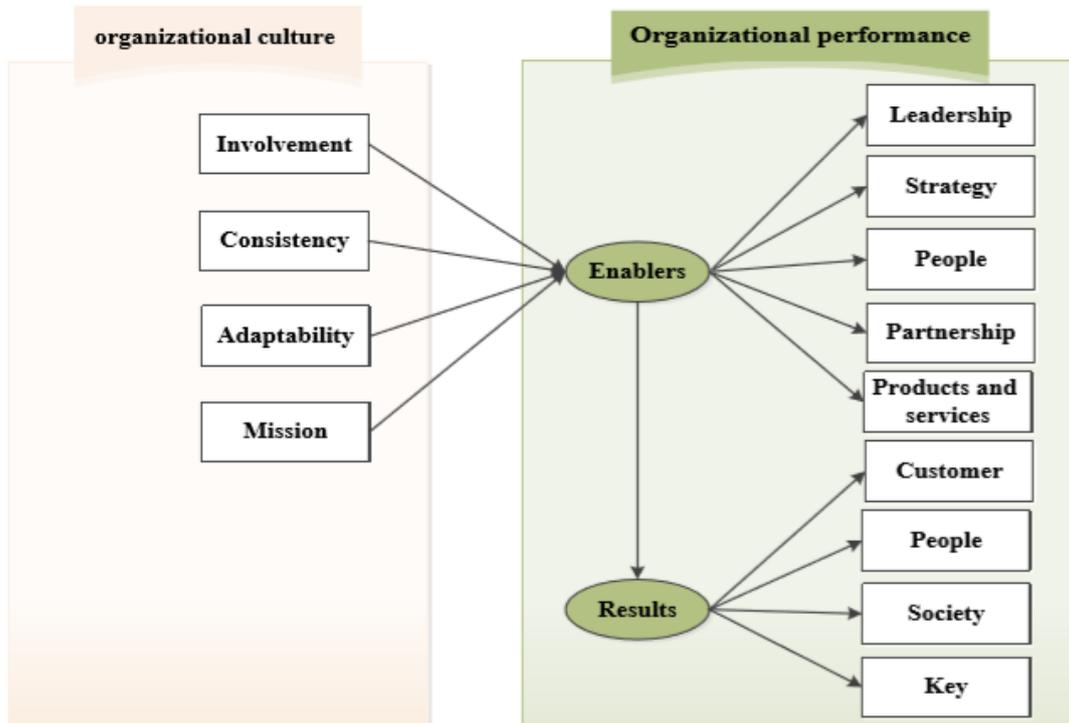


Figure 4. The impact of organizational culture on performance elements.
 Source: Denison, Janovics, Young & Cho Model (2006)

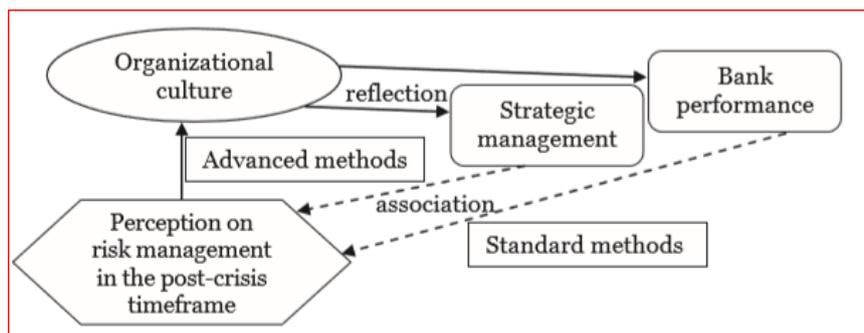


Figure 5. Matis Model of Organizational Culture.
 Source: Matis (2013)