THE IMPACT OF BUSINESS MEASUREMENT SYSTEM ON ORGANIZATIONAL PERFORMANCE

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Statement of Originality

The work described in this Final Year Project, entitled "The Impact of Business Measurement System on Organizational performance" is to the best of the author's knowledge that of the author except where due reference is made.

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ABSTRACT

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By

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The general objective of this study was to investigate the impact of business measurement system on organizational performance. Specifically, the purpose of this study was to examine the influence of operational performance measurement (OPM), empowerment measurement (EM), integration measurement (IM) and strategic alignment measurement (SAM) on organizational performance. The study was conducted on the financial institutions based in Malaysia. Four broadly hypothesized relationships were tested and data were collected by means of questionnaires. Data collected through questionnaires in this research were analyzed using Statistical Package for Social Sciences (SPSS) Version 19.0 and SmartPLS 2.0. Test such as confirmatory factor analysis (CFA), convergent validity, discriminant validity, and reliability test were carried out to assess measurement model, whereas t-value test used to assess structural model. The results showed that OPM and SAM were significantly related to organizational performance, whereas EM and IM were not significantly related to organizational performance. This study have revealed the employees view of business measurement system on organizational performance and provided both theoretical and practical implications that could be very beneficial to scholars and practitioners.
ABSTRAK

PENGARUH SISTEM PENILAIAN PERNIAGAAN TERHADAP PRESTASI ORGANISASI

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CHAPTER 1

INTRODUCTION

1.1 Background

The business measurement system has been seen as critical for organizations to position themselves strongly in an international stage and a competitive environment. Research not only suggests a relationship between strategies, but also that performance measures, can, and perhaps should be linked to strategy. The revolution in the business environment has led to changes in the nature of work, organizational performance, competition, organizational roles, business benchmarking and business measurement systems. In response to these business changes, many organizations have been continuously developing philosophies, approaches, and methodologies to improve their performance and efficiency. These approaches are such as Total Quality Management, Benchmarking, Balance Scorecard, Supply Chain Management, Six Sigma, and Organizational Learning.

Traditionally, business performance has been measured in few ways. One of the earliest performance measures could be as early as in the early twentieth century which the Du Pont brothers developed return-on-investment (ROI) that could measure profitability of investments in a diversified, modern organization. (Chandler, 1977). In addition to this, profit growth rate, net or total assets growth rate, return on
sales, shareholder return, growth in market share and return on net assets have also been adopted since mid-1900 (Hancott, 2005). However, these business measurement systems is mainly focus on short term financial performance and budgetary control which can overlook other long-term growth such as Research and Development, maintaining customer relationship and constant improvement. Therefore, many of the practitioners and academicians study on the problems to overcome weaknesses and improve the current situation.

Many organizations collect a vast amount of information, but don’t have an effective system for translating this feedback into a strategy for action (Moullin, 2004). Business measurement system helps organization to collects information such as statement of financial position, changes in equity or cash flow statement to compare present data with past data to identify the approaches required to improve performance and to set out the approaches throughout the organization. Tippins and Sohi (2003) propose organizational performance is measured on four dimensions: relative profitability, return on investment, customer retention and total sales growth. In recent years, many organizations have been using performance measurement system to measure and monitor their organizational performance. In this study we will be investigating at four dimensions which are operational efficiency, empowerment, integration, and strategic alignment on how these dimensions can influence organizational performance.

Past studies have showed that operational performance measurement determines that how important the factors such as market share, return investment and profit margin can influence the organizational performance. Besides, this measurement also able to shows the quality of the decision makers in making their
decision by directing their attention and action which are relevant to organizational goals and hence improve organizational performance (Amaratunga & Baldry, 2002).

Moreover, a business measurement system and the information it provides is essential for empower self-managed teams to operate. It is because the owner and the team should be in a position to make decisions that will improve their effectiveness and allow them deliver on the agreed target. Therefore, by using empowerment measurement, we will be able to observe whether the empowerment brings impact on the organizational performance.

Literature in the past showed integration in an organization can produce values to the customers, shareholders, and companies. Processes and functions need to be integrated in order for the organization to operate as coherent system. Measuring integration in the organization can help monitoring the progress on which goal are set. For instance, processes integration by changing corporate structure from vertical into horizontal structure. Thus, integration measurement generates information from a new mechanism to provide feedback and help improve in organizational value and performance.

Then, in this study, we will measure strategic alignment because this dimension is supporting or hindering aspects that are of great importance to the health of the organization (Kuwaiti & Kay, 2000). A good strategic alignment can improve team effectiveness and quality of the decisions. Therefore, by measure the results from the initial strategic, it provides the information and knowledge to the organization to evaluate and improve in the current strategic. The strategic alignment
measurement investigates in the improvement area such as productivity, customer satisfaction, financial performance etc.

Lastly, performance measurement is a way for organization to evaluate their current business strategy and identifies the critical success factors which can increase the organizational performance. In addition to this, organizations need to come out with acceptable and innovative strategies that align and integrate their result or action with the internal and external environment to compete in the industry.

1.1.1 Malaysia Scenario

Recent studies finds that the robust development in the Malaysian services sector has led firm to implement sophisticated business measurement system, emphasising benchmarking as well as systematic and timely evaluation (Amir, Ahmad & Mohammad, 2010). However the dominance of financial measures remains unchanged indicating the presences of both contemporary and traditional attributes in the Malaysia firms’ business measurement system.

Besides, past studies also discovered that Malaysia service firms continue to emphasize financially-based measures and are narrowly focus on internal measures where integration of value chain indicators is missing from the performance measurement system (Malina & Selto, 2004; Chenhall, 2005). In view of the fact that sale growth and Return on Investment (ROI) represent pure financial variables, these results suggest that Malaysia firm rely more on financial measures in
evaluating business performance as compared to non-financial measures (Jusoh & Parnell, 2007) and hence sales, sales growth, net profit and gross profit were among the financial measures preferred by the Malaysia manufacturing firms (Kassim, Aziah, Badriyah & Loos, 1989). Moreover, the business measurement system are design and implemented in a way that matches the organizational objectives rather than focusing on the uniqueness of the service businesses.

In Malaysia, service firms have stronger influence of top management on performance measurement system implementation as the high-power distance between the top management. Therefore, this increases the chance that subordinates will go along their bosses’ decisions, and thereby enhance the effectiveness of performance measurement system development (Hofstede, 1983; O’ Conner, 1995). Besides, the high-power distance in Malaysia may also influence the style and design of organisation’s management control systems (MCS) differently from those Western developed economies (Hofstede, 1980).

Che Ha (2006) found that product innovation is positively associated with marketing effectiveness and financial performance among Malaysia manufactures. It is because firms in the innovation, product efficiency and customer orientation are more likely to engage in innovation activities that require a lot of investment project (Jusoh & Parnell, 2007) which they can use a performance measures such as ROI to evaluate the efficiency of the investment.

Although many studies suggest that mass services have better form of control than the professional service firms, but (Amizawati, 2011) found that with intensified market competition, profit seeking service firms are likely to implement
control system. Measurement in the processes and system itself to match with competitors strategies are essential to ensure the business long-term survival. As a result, business measurement system is important for both mass service and professional organizations because it provides information and guidelines to the managers in designing a better system.

The manufacturing sector in Malaysia is growing fast as the second largest sector after service sector due to the demand from the West countries and this has lead to the use of new and advancement manufacturing environment and recent trends of measuring manufacturing performance (Jusoh & Parnell, 2007). In addition to this, organizations are expected to be more extensive and diverse in developing performance measures which to increase firm performance.

1.2 Problem Statement

Many studies prove that better business performance system leads to better organizational performance. In order to determining the appropriate constructs of performance or effectiveness involves measures ranging from shareholder wealth to profitability to employee satisfaction (Cameron, 1986). It is established that organizational performance could be measured by consolidating measures such as operating profitability margin, Return On Assets (ROA), Return On Investment (ROI), sales growth, stock returns, market shares, operational cost, employee and customer satisfaction, productivity etc.
In one respect, modern business measurement system in general and the Balance Score Card in particular are both targeted as improving poor strategy execution (Edwards, 2001). One of the reasons why companies often fail to translate strategy into action has to do with the performance measurement system, because they failed to collect the right information to monitor progress towards their strategic goals (Edwards, 2001).

Besides, no known studies have been found which the performance measurement is linked to organizational performance. So, by investigating further into performance measurement, we will understand the effects of performance measures can be achieved by adopting an organizational perspective that would help to spell out the mechanism of effect of performance measurement on organizations and organizational performance.

1.3 Research Objectives

1.3.1 General Objectives

The organizational performance is the most concern by the every organization because it helps the company to determine the futures by evaluating the current situation. Many studies have been done to find out the factors which will influence the organizational performance. Hence, this study will also be looking at the effects of business measurement system on the organizational performance.
1.3.2 Specific Objectives

The specifically objectives of this study are:

i. To find out the impacts of operational performance measurement on organizational performance such as return on investment, profit margin, market share, employee absenteeism and customer complaints.

ii. To determine the effects of empowerment measurement on organizational performance such as employee’s authorisation to correct problems, perform creativity and take charge of problems that require immediate attention.

iii. To identify the impact of integration measurement on organizational performance such as company goals, conflicts between department, and communication in the company.

iv. To find out the effects of strategic alignment measurement on organizational performance such as productivity, customer satisfaction, financial performance, and employee satisfaction.

1.4 Research Questions

The aims of the research are embodied in the following four questions:

1. Will operational performance measurement affect the organizational performance?

2. Will empowerment measurement affect the organizational performance?

3. Will integration measurement affect the organizational performance?

4. Will strategic alignment measurement affect the organizational performance?
1.5 Definition of Key Terms

Performance Measurement - the process of quantifying the efficiency and effectiveness of past actions, and a performance measures was defined as a parameter used to quantify the efficiency and/or effectiveness of past actions (Neely et al., 2002)

Organizational Performance - organizational performance is described as the extent to which the organization is able to meet the needs of its stakeholders and its own survival. Therefore, high market share or high profit margin doesn’t fully attaining the description of performance. The organizational performance is influenced by multitude factors that are combined in unique ways to both enhance and detract performance (Griffin, 2003).

Return on Investment (ROI) – which relates net income to invested capital (total assets), provides a standard for evaluating how efficiently management employes the average dollar invested in a business’s assets. An increase in ROI can translate directly into a higher return on the stockholders’ equity. (Jael K. Shim, Joel G. Siegel, 2008)

Empowerment – is defined as the extent to which managers perceive themselves as having authority to make decisions to improve quality and customer satisfaction. (Hayes, 1994)

Integration – is defined as the degree to which an individual manager’s action is harmonious and consistent with the other departments, so that the combined action is contributing to the added value to the customer and enhancing the overall performance (Plant, 1987)
Strategic Alignment – is defined as extent to which the performance measurement system is supporting or hindering aspects that are of great importance to the health of the organisation (Kuwaiti & Kay, 2000).

1.6 Significance of Study

It has been recognized that the theory and principles underlying in measuring business could improve the organizational performance. Many studies have shown that good control in business measurement system will improve the efficiency and effectiveness of the organization, in both financial and non-financial dimensions. Besides, it is important to understand that how the business measurement system variables can align with the business strategies to each level of organization and ultimately improve the organizational performance.

Referring to the research objectives that have been stated, this study is important for the organizations to know how the performance measurement may affect their organizational performance. The outcome of the study is useful for the management and staffs of the organizations to continuously improve in their business measurement system as imposed. The results of the improvement effort finally will benefit the organizations as well. In the long run, this study is a part of periodically and continuously evaluations and reviews series.