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ISFA-As Intervening Financial Literacy and Culture towards Organisational Financial Performance: A Transformational Leadership Approach

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This study aims to reveal a new model that sits between financial literacy and organisational financial performance. In this examination, researchers propose Intellectual Stimulation Financial Accountability (ISFA) as a link between financial literacy and organisational financial performance. A strong knowledge and understanding of financial literacy is required by a transformational leader to manage an organisation's financial activities. Financial activities can affect the financial performance of organisations in the form of financial accountability. Notwithstanding this, ISFA can encourage an organisation's financial performance. It can also act to encourage the creation of a new culture for organisational financial management.

Key words: *ISFA, Financial Literacy, Organisation Culture, Financial Performance, Leadership Transformational.*

Introduction

Financial management correlates the acquisition, financing and management of assets to the achievement of company goals (Horne and John, 2005). Bryan's research (2003) states that effective corporate knowledge management can provide sustainable competitive advantage through the process of sharing, creating and exploiting. The study of Lee *et al.,* (2010) explains that leaders who empower their followers' knowledge can increase more than 40% of differences in organisational performance. Knowledge empowerment creates optimisation for employee performance, especially in the completion of knowledge-based tasks (Xue *et al.,* 2011). Leadership encourages team members to solve shared problems and participate in decision making, so that they have the opportunity to share knowledge.

Remund (2010) reveals the financial literacy (knowledge, competence, and skills) of members used to build an effective and efficient organisation through operational values. Lusardi and Michell (2006) explain financial literacy is needed as a measure of financial competence in solving various financial problems. The Indonesian financial services authority (2013), indicates knowledge, skills, and competencies in financial management can affect an organisation's financial performance (Agyei *et al.,* 2014). Thus, organisational performance can be improved through the path of transformational leadership by stimulating follower intelligence and on the basis of financial literalization.

Literature Review

Transformational Leadership

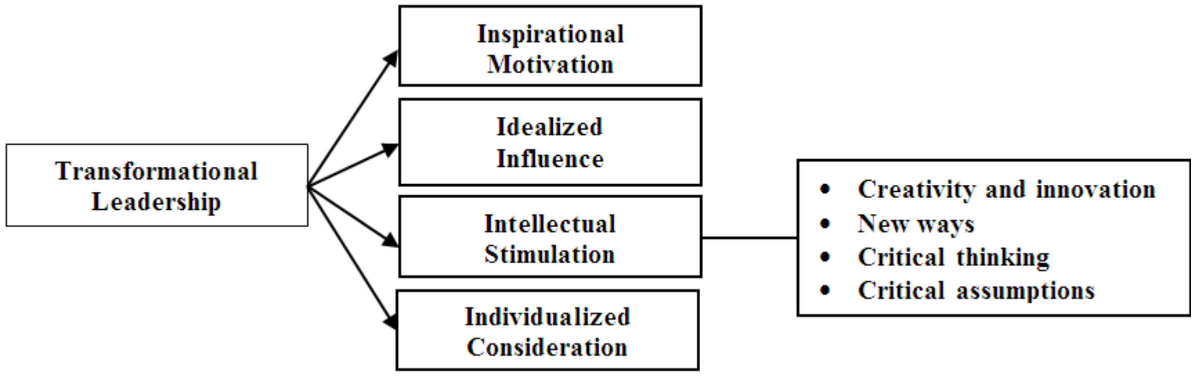
Bass and Avolio (1994) reveal four dimensions of transformational leadership: (i) idealized influence; (ii) inspirational motivation; (iii) intellectual stimulation; and (iv) individualised consideration. A transformational leadership approach, through intellectual stimulation, is aimed at questioning existing beliefs, assumptions, and values against the values of solving organisational problems (Avolio and Bass, 2004; Elkins and Keller, 2013; Sundi, 2013). Knowledge illustrates new creative ideas in solving organisational problems (Bass and Avolio, 2004; Bass and Riggio, 2006). Bycio *et al.,* (1995) found transformational leadership to have a very strong positive relationship with intellectual stimulation on the efforts made by subordinates.

Anjali and Anand (2015) see intellectual stimulation as the ability, commitment, dedication, and hard work of subordinates to achieve organisational goals. Is'haq *et al.,* (2008) views intellectual stimulation in the form of leaders' motivations to innovate and be creative. They are motivated to produce new behaviours, create an environment that is tolerant of extreme positions and to question the values and perceptions of followers' beliefs about the organisation. Cheung and Wong (2011) reveal a positive relationship between transformational leadership styles and intellectual stimulation through employee innovation and creativity in new approaches to completing work. Innovations are developed in company employees to drive growth (Bhatia, 2013) by recognising market opportunities to build sustainable organisational innovation (Burton and Thakur, 2009). Mumford *et al.,* (2000) has provided a literature review on creativity and innovation and conclude that individuals' willingness to innovate and be creative depends on the organisational climate.

Intellectual stimulation builds a significant relationship between transformational leadership and employee performance and commitment (Masi and Cooke, 2000). Thus, intellectual stimulation on transformational leadership is strongly associated with improving organisational performance (Boerner *et al.,* 2007) on increasing employee motivation (Bono and Judge, 2003); greater employee commitment, loyalty, and satisfaction (Bass and Riggio, 2006).

Figure 1 below provides a conceptualisation of transformational leadership:

Figure 1. The Transformational Leadership Dimension



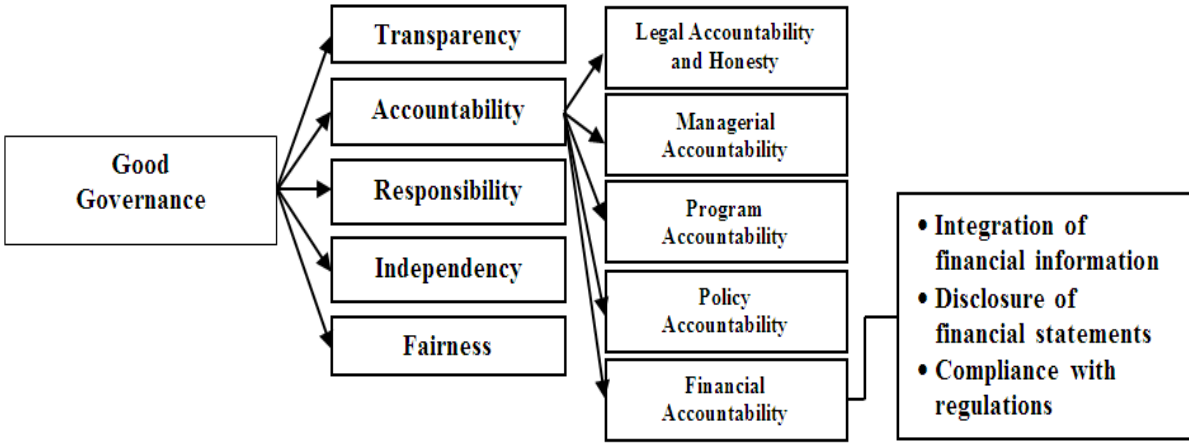
Good Governance

Governance is associated with performance as meeting criteria for policy decisions and managing the organisation efficiently, accountably and transparency have to be managed exceptionally well. (Jreisat, 2004). Parker (2007) states that corporate governance of legislators, regulators, professions, business entities, the media and the general public is achieved through governance principles that involve corporate management, a board, shareholders and other stakeholders (OECD, 2004). General principles of good corporate governance include transparency, accountability, responsibility, independence and fairness as benchmarks in achieving company sustainability for stakeholders (KNKG, 2006).

An account-based governance accounting system (Shaoul *et al.,* 2012) assesses company investment in the areas of investor analysis and evaluation (Hendry *et al.,* 2007). In order to guarantee accountability, accountability of financial statements is reported periodically to stakeholders. The reports cover five areas (Rasul, 2002: 11): (i) legal accountability and honesty; (ii) managerial accountability; (iii) program accountability, (iv) policy accountability and; (v) financial accountability. Ulum (2010), on the other hand, separates accountability into financial and performance accountability. Indicators of financial accountability are demonstrated through integrity of financial transaction information, disclosure of financial statements and compliance with applicable regulations.

Figure 2 below depicts the elements of good corporate governance:

Figure 2: Dimensions of Good Corporate Governance

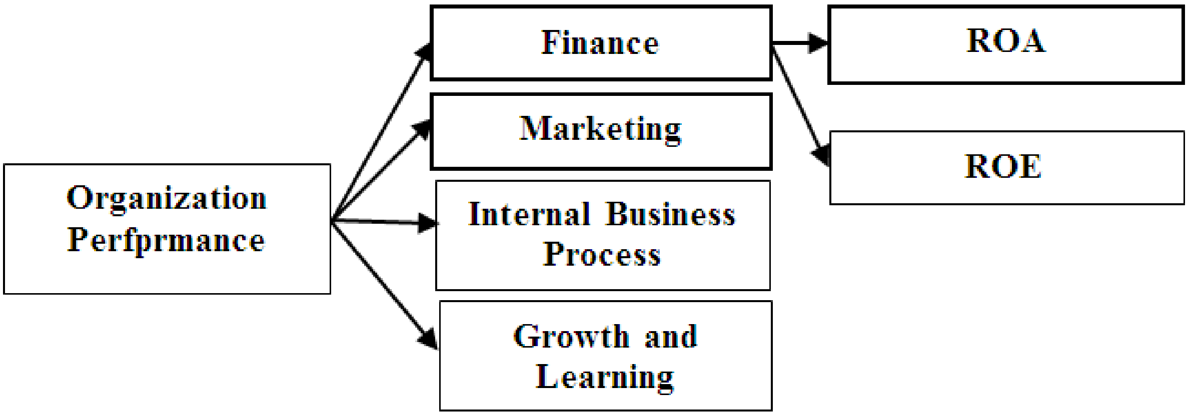


Organisational Performance

With regards to organisational performance, Mulyadi's (2009) balance scorecard is used to measure organisational performance via four perspectives: finance, customers, internal business processes and growth and learning. Strategic measurements in management and business are specified through the measurement of financial performance (Rowe, Morrow and Finch, 1995). Snell and Youndt (1995) measure organisational performance through ROA and correlate this with HRM as a control. An HRM approach centres on behavioural control and results show that when executives are knowledgeable about cause-effect relationships and control inputs, then performance will be higher. Darwish and Singh (2013) use organisational performance as an objective (ROA and ROE) to measure variations in performance brought about by market regulation mechanisms.

Figure 3 below depicts the dimensions of Organisational Performance:

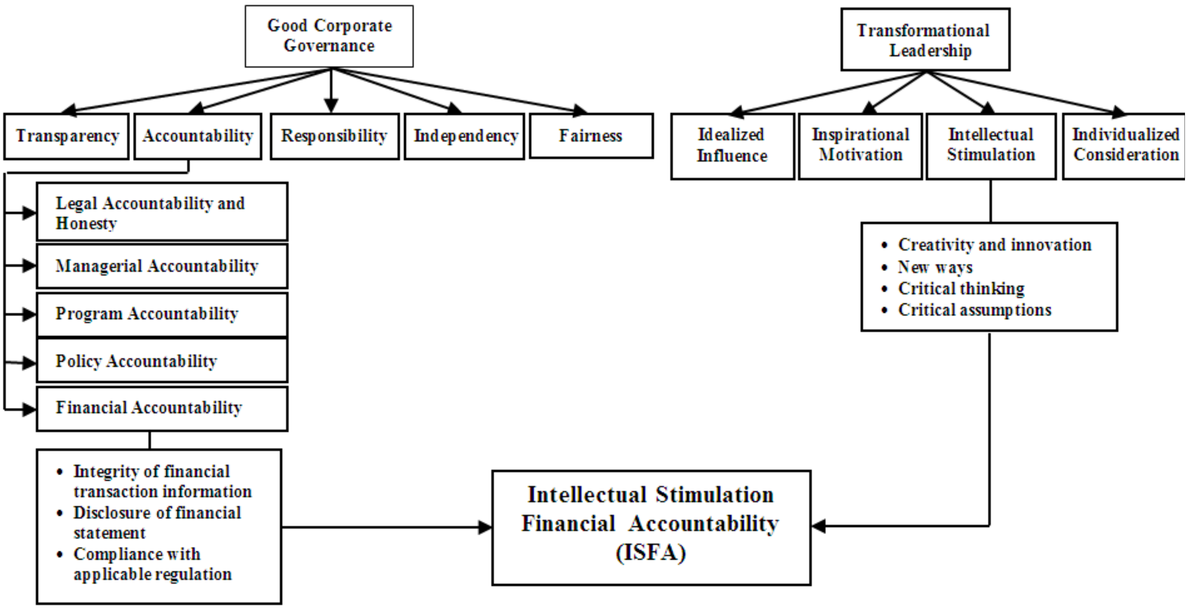
Figure 3. Dimensions of Organisational Performance



Basic Theoretical Model

Figure 4 below presents the theoretical model of this study:

Figure 4. Integration of Corporate Governance and Transformational Leadership



Proposition for Intellectual Stimulation Financial Accountability (ISFA):

Proposition: That by encouraging creativity, innovation and critical thinking, Intellectual Stimulation of Financial Accountability (ISFA) will be enhanced so that organisations can realise their financial performance.

Figure 5. Intellectual Capital Stimulation Financial Accountability Proposition

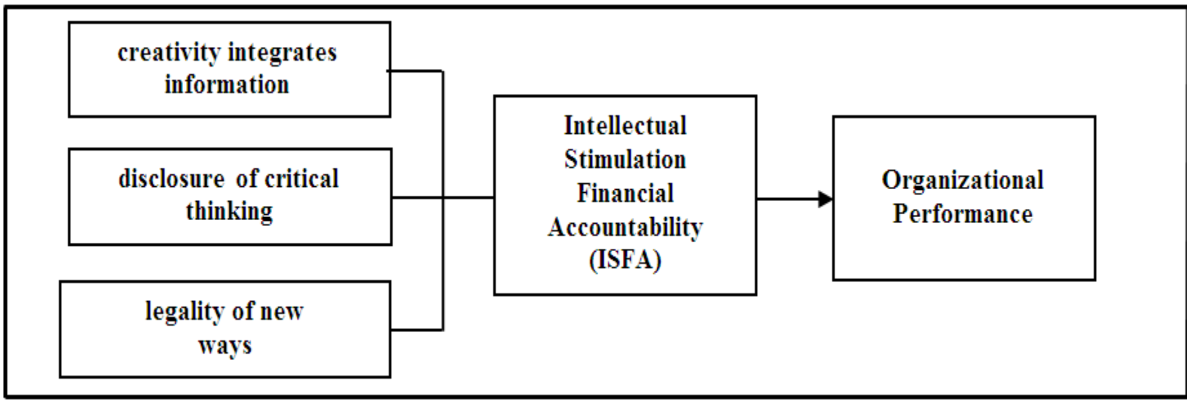
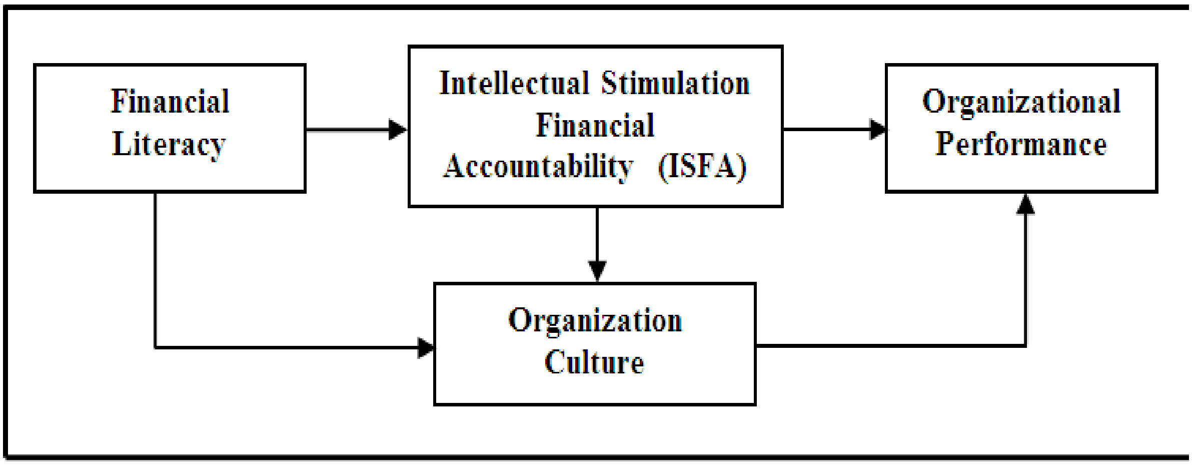


Figure 6. Basic Theoretical Model of Intellectual Stimulation of Financial Accountability



Relationship Between Variables

Effect of Financial Literacy on Intellectual Stimulation Financial Accountability

The concept of financial literacy consists of several aspects: financial knowledge (ANZ, 2005; Hung *et al.,* 2009; Fillis and Rentschler, 2010; Huston, 2010; Remund, 2010; OECD, 2013); financial operational experience (Orton, 2007; Fillis and Rentschler, 2010; OECD, 2013); the ability to communicate about different financial concepts (Remund, 2010); the ability to use concepts in different financial instruments (Hung *et al.,* 2009; Huston, 2010; Remund, 2010);

the ability to make adequate financial decisions (Remund, 2010; OECD 2013); attitudes towards the use of financial instruments (Orton, 2007) and; public trust in the financial operations carried out (Huston, 2010; Remund, 2010; OECD 2004).

The financial domain is understood as personal finance, budgets, investments and savings and loans (Remund, 2010). Given this, financial literacy can greatly affect a person in making decisions related to finance (Xioa, *et al.,* 2014). Subsequently, knowledge about financial literacy assists greatly in achieving long-term goals (Rosacker *et al.,* 2009). Knowing about financial sustainability and its challenges for transformational leaders is also critical. Leaders are are required to gain knowledge as a way to transform financial results into positive and personal financial trends (Ayayi and Sene, 2010).

Hypotheses

The following hypotheses are proposed:

***H1:* That w*hen the financial knowledge of transformational leaders increases, the accountability of financial statements also increases*.**

Wang *et al.* (2016) show a positive and significant correlation of transformational leaders with employee competencies which are described as indicators of the quality of the relationship between leaders and followers. Knowledge sharing and creation happens through the exchange of employee knowledge with organisations (Van and Ridder, 2004). This has become a positive factor for successful organisational performance (Oyemomi *et al.,* 2016). Connelly and Kelloway (2003) reveal that leader support significantly influences the organisational knowledge needed to create and maintain a knowledge sharing culture (Lin and Lee, 2004). Birasnav *et al.,* (2011) claim that transformational leaders build a culture of knowledge to support and shape employee behaviour. They do this by developing a set of values, assumptions, and competencies related to knowledge. Transformational leaders play a major role in developing organisational environments. They apply and manage knowledge efficiently so as to enhance organisational learning (Aragon *et al.,* 2007). Liu and DeFrank (2013) positively associate transformational leaders with individual intentions to share knowledge.

Given the above, the second hypothesis proposed is as follows:

H2: That as the transformational leader's financial knowledge competence increases, the accountability of the organisation's financial statements will also increase.

Leadership characteristics include abilities, personality traits, values, motives, knowledge, and skills (Zaccaro *et al.,* 2004). In the context of leadership, these skills provide much insight into the 'type' and style of leader working in the organisation (Mumford *et al.,* 2000). A leader's emotional and political skills are referred to as social assessment skills (Mumford *et al.,* 2000), social capacity (Zaccaro, 2007) and social intelligence (Ferris *et al.,* 2005).

Empirical findings consistently support the positive effects of emotional intelligence on leadership potential, the emergence of leaders, and transformational leadership styles (Brackett *et al.,* 2011; Daus and Ashkanasy 2005; Leban and Zulauf, 2004). Emotional control reflects emotional skills and involve self-monitoring and acting (Riggio, 1986). To build effective workplace relationships, research findings demonstrate that self-awareness is an important characteristic and is positively related to leadership potential as well as intellectual leadership competence (Higgs and Aitken, 2003). Recognising the emotions of others positively predicts transformational leadership behaviours among organisational leaders (Rubin *et al.,* 2005).

Therefore, the following hypothesis is proposed:

H_3 : That if the financial skills of transformational leaders increase, then accountability of organisational financial statements will also increase.

Effect of Financial Literacy on Organisational Culture

The most important competencies (Prahalad and Hamel, 1990) are developed through practical, theoretical, and organisational strategic knowledge (Sanchez and Heene, 1997) and centred on cues, habits, and scientific understanding (Whitehill, 1997). Cohen (1993) views organisational culture as a complex combination of formal, informal, procedural and interaction systems. Components of formal organisational culture include leadership, structure, policies, reward systems, socialisation mechanisms and decision-making processes. Components of informal organisational culture include behavioural norms, values, role models, organisational myths and rituals, organisational beliefs, historical anecdotes, and language (Cohen, 1993; Dion, 1996; Frederick, 1995; Schein, 2004; Trevino, 1990; Trevino and Brown 2004). One organisational culture framework, developed and synthesised by Alvesson (2002), identifies cultural metaphors and thinking models (Alvesson, 2002). Intezari *et al.,* (2017) reveal that knowledge creation, sharing and implementation have a positive influence on organisational culture related.

Subsequently, the following hypotheses is proposed:

H_4: That if the organisation's financial knowledge increases, then the organisation's financial culture will increase.

Ajzen (2002) argues that self-efficacy is an element of internal and externals controls. Individual behaviour is a social construct consisting of distance, power, individualism, masculinity, uncertainty avoidance and long-term orientation.

Huhtala *et al.,* (2012) reveal personal projects as personal work goals in the context of organisational culture. The results show significant personal work goals from the perspective of individuals and the organisation, because personal work goals guide the orientation of individual behaviour (Pomaki *et al.,* 2004) to workplace welfare (Hyvönen *et al.,* 2009). Employees who consider their work environment supportive of achieving their goals, report positive work attitudes in the majority cases (Maier and Brunstein 2001; ter Doest *et al.,* 2006); and demonstrate greater commitment to the organisation (Meyer and Allen 1997) and; report improved welfare (ter Doest *et al.,* 2006). Projects or personal goals can also be conceptualised in a life span context (Freund 2007). With regard to personal work goals, Hyvönen *et al.,* (2009) identifies seven categories (in order of size) that contribute to an organisation's ethical culture: (i) competency goals, (ii) development goals, (iii) welfare goals, (iv) job change goals, (v) job security goals, (vi) organisational goals and; (vii) financial goals. Consequently, research into individuals' beliefs are reflected through their behaviour and the effect of this behaviour on the organisation.

H_5: That if the level of competence in financial knowledge increases, then the organisational culture of finance will increase.

A company can gain a competitive advantage by increasing their efforts to develop knowledge, skills and attitudes of employees in order to maximize organisational performance and the ability to compete effectively (Ainissyifa, 2012). Wagonhurst (2002) states that training and development entails skills development, setting measurable goals, and producing observable behavioural changes. Since the costs of training and development programs are excessive, companies must evaluate the extent to which the benefits derived from training and development programs are implemented. The research identified that organisational culture is related to employee commitment to the organisation. Building a corporate culture on teamwork, communication, training development, and recognition of rewards create employee ownership and commitment to the organisation.

H_6: That if the ability of members of the organisation in the field of finance increases, then the culture of financial organisations will increase.

Wood and Winston (2005), state that leader accountability is associated with the actions and expectations leaders have. Orlikoff (2005) suggests accountability and leadership are mutually inclusive, and accountability, like leadership, is a choice. Effective leadership requires acceptance and emphasis on accountability by the board to improve organisational performance, activities, and situations (Carver, 2005). Morton (2005) found a culture of compliance requires accountability and is seen as an essential component. Business leaders are under close supervision, and, as such, a lack of accountability gives rise to specific problems (Waldman and Galvin, 2008). Romito (2005) and many executives view accountability as a critical success factor for businesses and consider a lack of accountability a major concern. Ethical failure in accountability can lead to whistle blowing. 'Bureaucratic structures, paternalistic control, and cover-up take precedence over transparency, accountability and dialogue when an organisation loses its moral compass' (Griffin *et al.,* 2013). Clearly, accountability is an important practice for society; conventional wisdom shows there is never too much accountability.

H$_7$: That when the application of organisational accountability increases, the values of organisational accountability will increase

Kotter and Heskett (1992) found that having a culture of "adaptive values" can significantly improve performance in the long run. Lee and Yu (2004) investigated the relationship between types of organisational culture in Singapore and found that the strength of organisational culture is often associated with organisational performance. Swiss *et al.,* (2012), found that the national cultural dimensions adopted for the study (distance of power, long-term orientation, and individualism) were positively related to innovation and customer orientation. Additionally, this had a positive relationship with organisational performance. Chen (2011) revealed that research on a work culture that influences financial performance is a structure formed through adaptive values found in organisations.

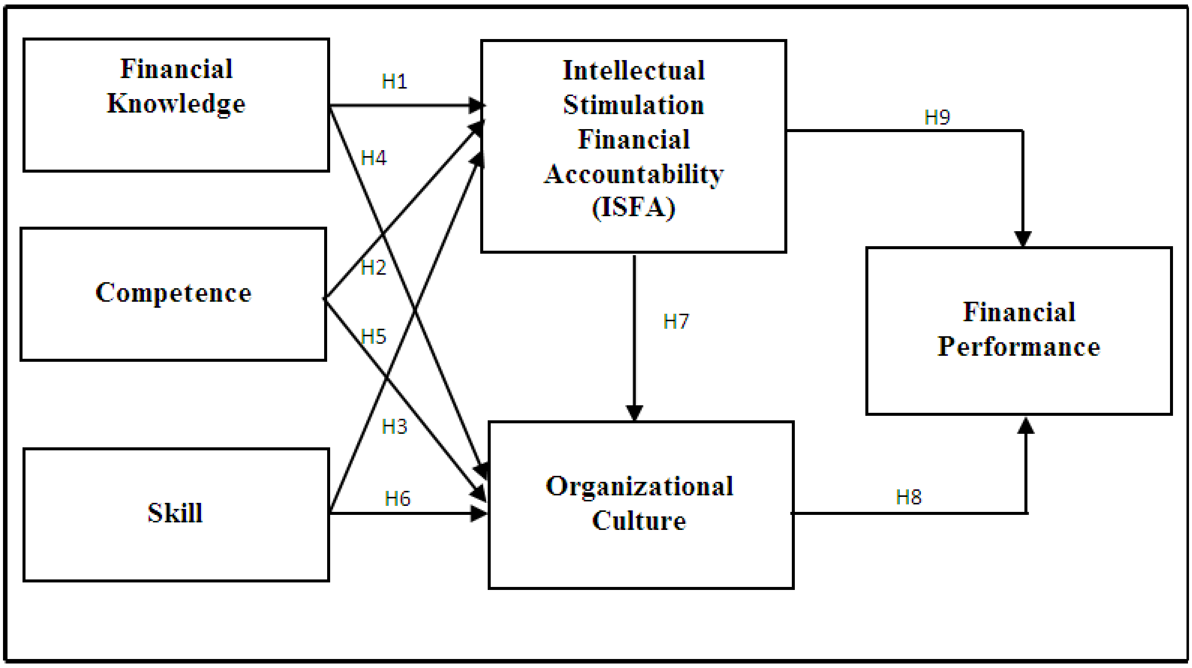
Therefore, the following hypothesis is proposed:

H$_8$: That if the organisational culture in presenting accountability in financial statements increases, then the financial performance of the organisation will increase.

New perspectives on the management of knowledge workers (Bergström *et al.,* 2009; Bos-Nehles *et al.,* 2017; Boxall *et al.,* 2014; Cäker and Siverbo, 2014; Millar *et al.,* 2017; Thompson and Heron, 2005) examines how leadership behaviour shapes the central mediating role of leaders. Empirical results show a positive relationship between creativity, company performance (Von Nordenflycht 2007), and innovation (Baron and Tang 2011).

H$_9$: That if creativity in preparing the accountability of financial statements increases, then financial performance of the organisation will increase.

Figure 7. Empirical Research Model



Source: Developed for this study

Conclusion and Recommendations for Further Research

The development of the Intellectual Stimulation Financial Accountability (ISFA) model in this study was used to bridge existing studies in in the context of organisational financial performance. Predicting and explaining financial literacy as a key variable of organisational success on organisational financial performance depends on three resource factors: knowledge, competence, and ability. In this model, the connection of financial literacy with financial performance is linked through the role of transformational leaders. At the level of financial knowledge, transformational leaders use their financial knowledge to stimulate new ideas in the form of organisational accountability.

Empirical research using the overarching ISFA model can be applied in a variety of organisations that range from profit organisations, government organisations, to non-profit organisations.

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