

## Strategic Orientation Based Research Model of SME Performance for Developing Countries

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— *Review of* —  
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### ABSTRACT

Performance of Small and Medium Enterprises (SMEs) has been considered as one of the most important driving force behind economies of both developed and developing countries due to their multiple contributions. In most of the developing countries, the performance of the SMEs is a key issue today. Strategic orientation of SMEs is one of the most critical factors for their success. The SMEs in developing countries are considered less strategically oriented than those of developed countries. But most of the studies in developing countries have focused the effect of single strategic orientation coupled with other factors on SME performance. This study proposes a research model of SME performance based on strategic orientation for developing countries. The proposed model suggests significant interaction between three major strategic orientations and SME performance in developing countries. An interaction among market orientation, entrepreneurial orientation, learning orientation and SME performance has been incorporated into the model. The model contributes for better understanding of complex interactions between strategic orientations and SME performance in developing countries.

**Key words: - Strategic Orientations, SMEs, Performance**

### 1. Background

For many years, Performance of SMEs has been the main focus of many researchers. It has been considered one of the most important critical factors behind economic success of both developed and developing countries due to their multiple contributions in economic growth, employment generation and innovations (Kongolo, 2010; Asian Productivity Organization, 2011). The importance of SMES to economies in different aspects is being continuously indicated by number of researchers (eg. Ghobadian and Gallear, 1996; Ladzani and Vuuren, 2002; Piech, 2004; Griffin and Ebert, 2006; Asian Productivity Organization, 2006, 2011)

According to (Ghobadian and Gallear, 1996) SMEs are the most dynamic businesses in any country. They play a key role in achieving socio-economic goals. SMEs exert a strong influence on the economies of all nations (Ladzani and Vuuren, 2002). They are also considered as vehicles for innovation and technology diffusion (Piech, 2004). SMEs create new products, processes and ideas through innovation and add more vigour to the market place (Griffin and Ebert, 2006). They are the engines of economic growth, cornerstones for creativity and innovation, and seedbeds of entrepreneurship (Asian Productivity Organization, 2006). In most of the countries, SMEs contribute more than 75 percent of the national Product (Asian Productivity Organization, 2011). Accordingly, the importance of high performed SMEs for any country and economy is obvious.

## 2. Problem

In most of the developing countries, performance of SMEs is one of the key issues since they are less productive and faces many constrains (Davidsson, 2004). More than 90% of enterprises in the Asian productivity organization (APO) member countries are SMEs and they account for about 75 percent of the Gross Domestic Product. But in many countries they face the constraints of technological backwardness, lack of human resource skills, weak management systems and entrepreneurial capabilities, unavailability of appropriate and timely information, insufficient use of information technology, poor product quality. As a result, there exists a low level of performance (Asian Productivity Organization, 2006, 2011).

## 3. Literature Review

### 3.1 Firm performance

Generally firm performance refers to the success of the firm. Alchian and Demsetz, (1972) defined it as “*the comparison of the value created by a firm with the value owners expected to receive from the firm*”. According to Flapper, Fortuin, and Stoop, (1996) it is “*the way organization carries its objectives into effect*”. Studies in firm performance have extended into two main streams March and Sutton, (1997). The first is to investigate the ways of improving the firm performance and the second is to study the predictors of firm performance. Consequently, firm performance has widely been studied as a dependent variable in organizational research (Rogers and Wright, 1998; March and Sutton, 1997). Most of the studies which used performance as a dependent variable have attempted to explain the variation of the performance of SMEs (Carton and Hofer, 2010; Brush and Vanderwerf, 1992).

### 3.2 Strategic Orientation and Firm Performance

Commonly, strategic orientation refers to umbrella term covering different constructs such as market orientation (MO) Entrepreneurial Orientation (EO) and Learning Orientation (LO). Barney, (1991); Hoq and Chauhan, (2011) have indicated strategic orientations as organizational resources which can improve the success of SMEs. Some other researchers consider strategic orientations as dynamic capability that represents the organization’s ability to integrate and built internal and external competencies (Teece, Pisano and Shuen, 1997; Zhou, Yim, and Tse, 2005). There are other authors who consider orientations as elements of the organizational culture (Nobel, Sinha and Kumar, 2002). This view characterised the concept as a set of attitudes, values and behaviours of the organization. It is very clear that different authors and have viewed strategic orientations through different lenses and it is very critical for the success of SMEs what so ever the lenses which it is viewed through.

### 3.3 Entrepreneurial Orientation and Firm Performance

Atuahene-Gima, (2001) investigated the effect of EO on small firms’ product innovative performance and found that high EO positively affect performance. Baker and Sinkula, (2009) examined the direct effect EO on profitability in a sample of SMEs in USA and found that EO profitability through innovation success. Barrett, Balloun, and Weinstein, (2005b) found that EO correlates with performance in non for profit organizations. Becherer and Maurer, (1997) investigated the effect of EO in entrepreneur-led US SMEs. Results indicated that EO correlates with performance. Wang, (2008) found positive effect of EO on performance. Frishammar and Horte, (2007) proved significant effect of EO on new product performance of medium scale manufacturing firms in Sweden. Results also proved innovation dimension of EO positively related with new product performance. Li, (2005)

found that EO have positive effects on managerial networking and in turn increase the performance in Chinese foreign invested firms. Li, Liu and Zhao, (2006) in a study in Chinese firms indicated that EO has positive effects on new product performance. Li, Zhao, Tan, and Liu, (2008) in a study proved that innovativeness and proactiveness dimensions of EO strengthen the positive relationship between MO and performance. Liu, Luo, and Shi, (2003) found that higher level of EO, increase the competitive advantage of state owned Chinese companies. Hult, Hurley, and Knight, (2004) found, in large scale industrial firms, positive relationship among EO innovation and performance. Kropp, Lindsay, and Shoham, (2008) indicated that EO lead to lower performance in the early stage of international business ventures. Roukonen and Saarenketo, (2009) in a case study analysis of small scale Finnish software firms found that EO combined with strong LO and MO has significant effect on internationalization. Luo, Sivakumar, and Liu, (2005) found that EO affect organizational performance. Schindehutte, Morris, and Kocak, (2008) in a conceptual study emphasized that EO, would influence how firms perform. Tzokas, Carter, and Kyriazopoulos, (2001) found that EO improve the operational competencies of in small scale manufacturing firms in Greece. Tajeddini, (2010) investigated the effect of EO on the performance of hotel industry in Switzerland and found that EO has an effect on the business performance. Barrett, Balloun, and Weinstein, (2005a) claimed that the effect of EO on performance depends on the industry or market. Hoq, and Chauhan, (2011) conducted a study in SMEs in Bangladesh and found that EO positively related to firm performance in hostile business environment. Chandrakumara, De Zoysa, and Manawaduge, (2011) shown that EO produces more positive effect on the performance of small firms than medium scale firms. Fauzul, Takenouchi, & Yukiko, (2010) in a study in Sri Lankan SMEs, proved positive relationship between EO and firm performance.

### **3.4 Market Orientation and Performance**

Reijonena, and Komppulab, (2010) showed that the dimensions of MO are success factors in SMEs. Hoq, and Chauhan, (2011) found that MO positively related to firm performance in Bangladesh hostile business environment. Lin, Peng, and Kao, (2008) examined the effect of MO on firm innovation and performance and found positive relationship. Frishammar, and Andersson, (2008) claimed that strategic orientations has a limited effect on international performance of Swedish SMEs. Merlo & Auh, (2009) examined positive relationship between MO and performance and the relationship is influenced by marketing sub units. Mavondo, Chimhanzi, and Stewart, (2005) found that MO affects different types of innovation performance. Kaya and Seyrek, (2005) in a study of manufacturing firms in turkey shown that level of EO should be selected based on the level of MO. Izquierdo, and Samaniego, (2007) conducted a study in Spanish firms. The study investigated effect of MO, on social effectiveness of non-for Profit organizations. Results indicated that effect of different strategic orientations differ according to the organizational goals. Fritz, (1996), found that market orientation has a significant importance in corporate management success. Berry, (1996) in a study in a sample of high-tech firms in UK found that firms gradually grow when they shift from TO to MO. Barrett, Balloun, and Weinstein, (2005a) found that effect of MO depend on the nature of the industry or market. Tzokas et al. (2001) found that MO improves the organizational competencies of SMEs. Slater and Narver, (2000) found that MO has positive and significant effect on firm performance. Voss and Voss, (2000) proved that MO is not important when the firms have non profit goals. Shaw, (2000) claimed that successful German companies in UK characterised with MO. Schindehutte et al. (2008) propoed that MO will influence how firms perform. Zhou, Yim, and Tse, (2005) shown that MO leads the technology based innovations. Paladino, (2009) claimed that higher level of MO increase the financial performance while low level of MO

improve innovations. Nobel, Sinha, and Kumar, (2002) in a longitudinal study found that higher level of customer orientation dimension of MO and selling orientation increase organizational performance. Rhee, Park, and Lee, (2010) found MO has a positive effect on innovation performance in technology intensive firms in South Korea. Results indicated that LO influence innovation performance which in turn improve the organizational performance. LO also mediate the relationship among EO, MO and innovation performance. Luo, Sivakumar, and Liu, (2005) found that MO affect organizational performance in a study conducted in a sample of marketing and other senior managers in China. Roukonen and Saarenketo, (2009) found that MO has an effect on internationalization. The relationship is stronger when MO is combined with LO and EO. In a study conducted in the context of developing country, Keskim, (2006) found that MO has direct effect on innovation and performance. Knotts, Jones, and Brown, (2008) proved that in 1690 small scale manufacturing firms, surviving organizations focus more on PO while non-survivors focus more on MO. Jeong, Pae, and Zhou, (2006) indicated that both customer orientation dimension of MO influence performance and profitability. Hult, Hurley, and Knight, (2004) conducted a study in large scale industrial firms in US and found that MO has a greater effect on performance in higher market turbulence environment. Pulendran, Speed, and Widing, (2003) shown that MO positively related to business performance. Kurtinaitiene, (2005) investigated the relationship between MO, and performance in a sample of mobile telecommunication businesses in European Union and proved positive relationship. Farrell, (2000) found positive relationship between MO performance in manufacturing firms in Australia. Foley and Fahy, (2004) developed a conceptual framework and proposed that MO increase the organizational performance. Liu et al. (2003) found that higher level of MO increase the competitive advantage of state owned Chinese companies. Salavou, (2005) investigated the direct effect of MO on product development performance and found it is positive. Salavou, Baltas, and Lioukas, (2004) indicated that high level of LO increases the innovation performance of SMEs. Baker and Sinkula, (2002) argued that MO facilitates the firm innovation. Baker and Sinkula, (1999b) found that MO has an indirect effect on performance through innovation in large scale firms. Atuahene-Gima, Slater, and Olson, (2005) claimed both reactive and proactive MO is essential for the performance of the firm. Li et al. (2008) proved that MO positively related to firm performance. Li et al. et al. (2006) found that MO has no positive effects on new product performance. Li, (2005) found that MO has positive effects on managerial networking and in turn increase the performance. Lee and Tsai, (2005) found that MO has a direct effect on performance. Frishammar and Horte (2007) proved that MO has a significant effect on new product performance. Aziz and Yassin, (2010) emphasized the importance of MO to obtain a sustainable competitive advantage and success performance outcomes in smaller agro-food organizations. Santos-Vijande, Sanzo-perez, Alvarez-Gonzalez, and Vazquez-casielles, (2005) indicated the market orientation affects organizational performance. Farrel and Oczkowski, (2002) found LO has a significant effect on organizational performance. Bhuiyan, Mengue, and Bell, (2005) suggested that MO affects significantly on performance. Becherer and Maurer, (1997) indicated that MO correlates with performance but has no significant effect on performance. Ledwith and Dwyer, (2009), in a study in Ireland Small firms found that the MO is not a good predictor of new product performance and organizational performance. Barrett et al. et al. (2005b) found that MO correlates with performance while it also correlates with creativity and organizational flexibility. Baker and Sinkula, (2009) indicated that MO affects profitability of SMEs in USA through innovation success. Appaiah and Singh, (1998) found that MO affects organizational performance. Atuahene-Gima and Ko, (2001) found that MO leads to high performance in SMEs.

### 3.5 Learning Orientation and Performance

Lin et al. (2008) found that LO fully mediate the relationship between MO and innovativeness and performance. According to Barrett et al. (2005a), effect of LO on organizational success depend on the industry. Zehir and Eren, (2007) found that LO has positive effects on new business venturing. Rhee et al. (2010) indicated that LO influence innovation performance which in turn improve the organizational performance. LO also mediate the relationship among EO, MO and innovation performance. Roukoni and Saarenketo, (2009) found that LO has an effect on internationalization in small scale Finnish software firms. Keskim, (2006) found that LO has direct effect on innovation and performance in developing countries. Hult et al. (2004) found positive relationship between LO and innovation performance. Kurtinaitiene, (2005) found positive relationship between LO and organizational performance. Gao, Zhou, and Yim, (2007) proved that MO positively affects performance when demand uncertainty is low and it is even detrimental to performance when the demand uncertainty is high. Farrell, (2000) found a positive effect of LO on performance. Foley and Fahy, (2004) developed a conceptual framework based on existing literature and proposed that LO and MO increase the organizational performance. Foley and Fahy, (2004) proposed that LO is positively related to organizational performance. Liu et al. (2003) proved that higher the level of LO and higher the competitive advantage of state owned Chinese companies. Salavou, (2005) proved that LO, MO has a combined effect on new product performance in SMEs in Greece manufacturing sector. Salavou et al. (2004), In their study in SME sector, found high level of LO leads to innovation performance. Baker and Sinkula, (2002), developing a conceptual model, proposed that LO and innovation LO is essential for firm innovativeness. Baker and Sinkula, (1999b) found that LO has a direct effect and indirect effect through innovation on performance. Lee and Tsai, (2005) found that LO has a direct effect on performance, while there is an indirect effect through innovativeness. Wang, (2008) found that LO mediate the relationship between EO and organizational performance. Santos-Vijande et al. (2005) found that LO affect establishing long term customer relationships in Spanish SMEs. Wang and Wei, (2005) proved that MO has an effect on creating competitive advantage of software firms in Taiwan. Farrel and Oczkowski, (2002) found that LO explain organizational performance. Barrett et al., (2005b) found that LO correlates with performance of non profit organizations.

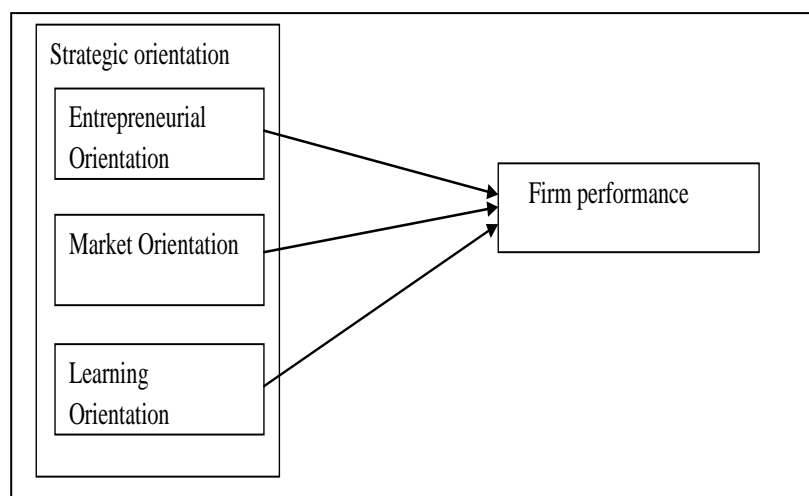
## 4 Strategic Orientation Based Model of SME Performance

Existing literature reveals that Strategic orientations have been used in many prior studies to explain the performance of SMEs. But prior researchers have used different orientations separately or combination of two orientations as predictors of SME performance (eg. Ledwith & Dwyer, 2009; Li et al. 2008; Gao et al. 2007; Kropp et al. 2006; Santos-Vijande et al. 2005). As Hakala and Kohtamaki; (2011); Kropp et al. (2006) pointed out that the effect of orientations on performance has been investigated individually or single orientation coupled with other factors.

Strategic orientations have been considered as organizational resources (Hoq & Chauhan, (2011); Barney, 1991). Valuable and unique resources are the source of the competitive advantages in SMEs (Amit and Schoemaker, 1993; Barney, 1991). Hoq and Chauhan, (2011) and Inmyxai and Takahashi, (2009) argue that lack of resources and capabilities in SMEs is a barrier for them to develop their own markets and to use the experience, economies of scale and scope for achieving competitive advantage. Recent research findings have concluded that interrelation among different strategic orientations provides sustainable competitive advantage for organizations (Hult et al. 2004) and firms that continue balancing different strategic orientations perform better (Bhuian et al.,

2005 Nobel, et al. 2002). It is also evident that strategic orientations are very important for the organizations in developing countries (Keskim, 2006). Dharmasiri, (2009) emphasized the importance of strategic orientation for the success of the organizations in developing countries. Chandrakumara et al. (2011) also have suggested the need of investigations of the impact of mixed orientations on firm performance in developing countries.

Accordingly, based on the available literature, it can be argued that strategic orientations qualify as predictors of SME performance in a research model. Three strategic orientations, EO, MO and LO which are very important for SMEs have not previously been studied in a single research model. Therefore these three orientations are incorporated into the proposed research model and three direct paths from selected strategic orientations to the firm performance are proposed. Schematic representation of the proposed model is depicted in the figure 1. The model hypothesises that EO, MO and LO are positively related to firm performance.



**Figure 3.1**  
**Research model**

## 5. Conclusion

By considering the role of strategic orientation of SMEs in developing countries, it is obvious that understanding of the relationship among entrepreneurial orientation, market orientation, learning orientation and firm performance is very important. The research model proposed in this paper integrates these three strategic orientations into a model. As practical implications of the study, SME owners and managers will be able to focus on the level of different strategic orientations of their organizations in order to improve the performance. In addition, policy makers and planners in entrepreneurial education in developing countries can use findings to foster the strategic gesture of potential and actual entrepreneurs. This paper proposes a theoretical model which incorporates only direct relationships between strategic orientations and firm performance. Further understanding of the proposed direct relationships will pave the way for future researchers to study more complex models which include possible mediating and moderating relationships.

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