

Assessment of the Effects of Moderating Factors of Entrepreneurial Orientation on the Performance of SMEs in Tanzania

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Abstract

This conceptual study was conducted in order to assess the effects of the Moderating Factors of Entrepreneurial Orientation (EO) on the performance of SMEs in Tanzania. According to the literature EO refers to the strategy making process that provides organizations with the basis for entrepreneurial decisions and actions. The dimensions of EO are innovativeness, proactiveness, risk taking, competitive aggressiveness and autonomy. The need for firms to exercise EO has been widely recognized. In less developed countries like Tanzania where the growth rate of SMEs is very limited, the subject matter has not been fully exploited for firms to cope and understand the effects of EO on firm performance especially the SMEs. To the authors' best knowledge there exists only a few studies in Tanzania on EO especially those looking at the moderating factors and linking them to SMEs performance. According to the literature several moderating factors such as cultural orientation and organizational structure (internal factors), social economic factors and political and legal factors (external factors) have a contribution on the applicability of EO hence performance of SMEs. The study found out that the moderating factors have an effect on performance of SMEs. However there is a need for research to test the applicability of moderating factors of EO and firm performance in a Tanzanian context.

Key words: entrepreneurial orientation, moderating factors, firm performance, SMEs

INTRODUCTION

Entrepreneurial Orientation (EO) has acknowledged significant conceptual and empirical consideration, representing one of the few areas in entrepreneurship research where a growing body of knowledge is mounting. According to Rauch *et al.* (2009), in less developed countries, there exist few researches on EO hence creating opportunities for researchers to review, and estimate the cumulative understanding on the relationship between EO and business performance.

According to the literature several EO moderating factors such as cultural orientation and organizational structure (internal factors), social economic factors and political and legal factors (external factors) have a contribution on the applicability of EO hence performance of SMEs (Gathungu *et al.*, 2014; Wiklund and Shepherd 2005). This literature study therefore aims at assessing the effects of the moderating factors of entrepreneurial orientation on performance of SMEs in Tanzania.

EO refers to the strategy making processes that provide organizations with a basis for entrepreneurial decisions and actions (Lumpkin and Dess, 1996; Wiklund and Shepherd, 2003). Lumpkin and Dess (2001) define each dimensions of entrepreneurial orientation where they define innovativeness as willingness to support creativity and experimentation in introducing new products or services despite of novelty, technological leadership, and R&D in developing new processes. They also define risk taking as a tendency to take bold actions such as venturing into unknown new markets, committing a large portion of resources to venture with uncertain outcomes, and/or borrowing heavily. Lastly, they define proactiveness as an opportunity-seeking, forward-looking perspective involving introducing new products or services ahead of the competition and acting in anticipation of future demand to create change and shape the environment.

As the number of studies examining the relationship between EO and performance is ever increasing, it is a different case in Tanzania. According to the researchers' best knowledge, no study has been conducted in Tanzania that looks at the effects of moderating factors of EO and the performance of SMEs. Few studies that dealt with EO focused mostly on the relationship between EO and performance (LeRoux and Bengesi, 2014).

In Tanzania the growth rate of SMEs is very limited and this is caused by many factors (LeRoux and Bengesi, 2014). Most entrepreneurs engaging themselves in small and medium scale enterprises fail to grow due to a number of problems including the moderating factors on EO. It should be noted that Miller (1983) conceptualized three dimensions of EO which are innovativeness, risk taking, and proactiveness while Lumpkin and Dess (1996) added two dimensions which are competitive aggressiveness and autonomy but the literature and findings show that these dimensions depend mostly on the moderating factors. For example, it is possible that an aggressive "undo the competitor" strategic stance, as suggested by an EO, is perceived as positive by important stakeholders and rewarded in some cultures but negative and punished in others. This suggests that the

influence of EO on performance may vary as a function of cultural norms. As early as 1993, Hofstede noted that management theories were culturally bounded. Also many studies on EO have largely explored the link between EO and performance (Al-Swidi and Mahmood, 2011; Callaghan and Venter, 2011; LeRoux and Bengesi, 2014; Radipere, 2014; Rauch *et al.*, 2009; Wiklund and Shepherd, 2005). This literature study goes beyond this primary advance by discussing the effects of the moderating factors of EO on the performance of SME in Tanzania.

The need for firms to exercise entrepreneurial orientation has been widely recognized. In developing countries like Tanzania the subject matter has not been fully exploited for firms to cope and understand the effects of entrepreneurial orientation on firm performance especially the SME. Several moderating factors such as cultural orientation, organizational structure, social economic factors and political and legal factors are likely to have a contribution on the applicability of entrepreneurial orientation in the performance of SMEs. The performance of SMEs depends largely on entrepreneurial orientation which is accompanied by the moderating factors (Gathungu *et al.*, 2014; Wiklund and Shepherd, 2005).

Tanzania experienced the removal of trade barriers which has increased internationalization of firms to enter new markets leading to the strong competition between local firms that were formally protected and the foreign firms. This shift has introduced new operating conditions and challenges. Studies indicate that most firms are not responding effectively hence losing customers and poor enterprise performance. It should be noted that other studies stress the importance to understand entrepreneurial behaviors in the context of socio-economic, political and cultural environment in which it occurs (Welter and Smallbone, 2011). It is from this background that authors were prompted to find out the effects of the moderating factors of EO on firm performance.

The general objective of this study is to assess the effects of moderating factors of entrepreneurial orientation (EO) on performance of SMEs in Tanzania.

METHODOLOGY

In this paper a conceptual framework has been proposed whereby organizational structure, cultural orientation, political and legal framework, and socio-economic factors moderate the linkage between EO and SMEs performance. The methodology adopted for this paper is a conceptual modeling to present a description framework which can unite

the significant predictors of firm performance in SMEs. To build this conceptual model we have reviewed several research papers in detail. A detailed literature review of about 40 conceptual and research papers written by various researchers was carried out. The literature review was conducted through searches in different data bases with different search words in different combinations (entrepreneurial orientation, SME, entrepreneurship, performance, culture, moderating factors, growth, development, political and legal factors, socio-economic factors, organizational structure, Tanzania, Africa, Botswana, Ethiopia, Ghana, Kenya, Nigeria, South Africa, Uganda, Zambia and Zimbabwe). Special emphasis has been given to studies conducted in the context of the moderating factors of EO and SMEs performance. Although limited in number but special attention was given to studies conducted in Africa, Tanzania in particular.

The literature review takes in to account the scholarly sources from 1973 to 2015. In addition to scholarly articles, other data sources employed in this study include: highly cited books, conference proceedings and working papers in the field of entrepreneurial orientation research. These sources have been reviewed to have a broad insight of any prospective gaps in the previous studies. Additionally, information from official websites of various national and international research agencies and institutes have been reviewed to present the interesting findings with reference to issues discussed in the paper. It should be noted that this methodology was adopted from Hafeez (2012).

DEFINITION OF KEY TERMS

Entrepreneurial Orientation

It is very difficult to find a single definition of EO as there are many scholars who have researched and defined the concept. For example we have Lumpkin and Dess (1996: 136-137): "EO refers to the process, practices and decision-making activities that lead to new entry". Avlonitis and Salavou (2007: 567) define it as: "EO constitutes an organizational phenomenon that reflects a managerial capability by which firms embark on proactive and aggressive initiatives to alter the competitive scene to their advantage". To sum all the definitions of the concept, EO is defined basing on the dimensions that influence it. It can therefore be defined as a strategy making process that enable firms to be innovative, take risks, compete aggressively, act autonomously and proactively (Khandwalla, 1976/77; Miller, 1983; Lumpkin and Dess, 1996; LeRoux and Bengesi, 2014). However, this study argues that the dimensions should be backed up by the moderating factors especially when defining the concept from the Least

Developed Countries (LDCs) and emerging economies perspective where these moderating factors acts as a threat to the SMEs in their attempt to be creative, innovative, take risks, autonomy, aggressive and proactive. That is why as explained earlier; it is difficult to find a clear single definition of EO.

Moderating factors

As defined by Baron and Kenny (1986: 1174), "in general terms, a moderator is a qualitative (e.g., sex, race, class) or quantitative (e.g., level of reward) variable that affects the direction and/or strength of the relation between an independent or predictor variable and a dependent or criterion variable. Specifically within a correlation analysis framework, a moderator is a third variable that affects the zero-order correlation between two other variables. In the more familiar analysis of variance (ANOVA) terms, a basic moderator effect can be represented as an interaction between a focal independent variable and a factor that specifies the appropriate conditions for its operation." Linking to the study objectives the moderating factors of EO which are organizational structure, cultural orientation, political and legal framework as well as social-economical factors affect the direction and strength of EO and SME performance.

Firm performance

The clarity of firm performance continues to challenge scholars due to its complexity. The definition of firm performance is based on measures such as profitability, market value, growth (financial performance) and employee satisfaction, customer satisfaction, environmental performance, social performance and strategic performance (non-financial performance) (Santos and Brito, 2012).

SMEs

In this study SMEs stand for Small and Medium Enterprises. The literature shows that there no one definition of SME. In fact each country has its own definition of SMEs. The term "small" and "medium" implies that SMEs is defined according to the size which includes the number of employees, capital invested, share capital, number of shareholders, market share, annual turnover, total asset value, composition of management and degree of formalization (LeRoux and Bengesi, 2014). Table 1 summarizes the definition of SMEs as applied in Tanzania.

Table 1: Tanzania definition of SMEs

Category	Number of employees	Capital investment (in Tsh) 1 USD = TSH 1600
Micro enterprise	1-4	Up 5 million
Small enterprise	5-49	5 to 200 million
Medium enterprise	50-99	200 to 800million
Large enterprise	100+	Above 800 million

Source: SME Development Policy, April 2003

LITERATURE REVIEW

Introduction

For several years the policy setting in Tanzania has not been encouraging to support SME development. It should be remembered that the country shifted from a closed economy to the open economy with the privatization of the state owned enterprises. This created pressure to most Tanzanians especially those who were employed since they lost their jobs. In response to economic hardship they established SMEs as a way to earn a living but no research and development was conducted to access whether or not the environments factors were favorable to their entrepreneurial endeavors. It is due to this that growth of SMEs was hampered by several factors including the policy environment that was not supportive. The role of the government and private sector involvement through credit financing and research and development is more important. (LeRoux and Bengesi, 2014).

The literature indicates that performance can be enhanced when key variables are appropriately associated (Naman and Slevin, 1993). This is the annotation and the roots of the contingency theory which suggests that congruence or "fit" among key variables such as industry conditions and organizational processes is critical for obtaining finest performance (Lawrence and Lorsch, 1967). Contingency theory states that the relationship between two variables depends on the level of a third variable. Introducing moderator factors into any relationship helps to reduce the potential for misleading inferences and permits a "more accurate and unambiguous understanding" of contingency relationships. Because of its concern with performance implications, contingency theory has been essential to furthering the development of the management sciences (Venkatraman, 1989). Therefore, to understand the effects of EO on firm performance, one has to assess the effects of moderating factors of EO and performance.

The literature discusses a number of variables that potentially moderate the EO-performance relationship (Lumpkin and Dess, 1996; Zahra and Covin,

1995; Zahra and Garvis, 2000). There is however little consensus on what constitutes suitable moderators but both internal and external variables have been discussed by the literature to have an effect on EO-Performance (Wiklund & Shepherd, 2003). Although a number of conceptual arguments have been recommended in favor of moderating variables, few potential moderators have been used across a sufficient number of EO.

Internal Factors Moderating Entrepreneurship Orientation

In one study the results shows variation in entrepreneurial orientation owed to enterprise informalization, value based compensation and access to resources (Ullah *et al.*, 2013). Moreover, the findings indicate that access to resources is the major considerable predictor while enterprise informalization is the subsequently leading predictor. Hence, it is in line with conclusion that enterprises related factors play an important role in determining entrepreneurial orientation.

The national culture also has an effect on EO and firm performance. Yoo (2015) found out that while performance-oriented culture has positive influence on SMEs risk-taking and proactiveness, human-oriented culture has negative influence on proactiveness. This shows that despite the firms' culture, also the national culture can have an effect on performance. It can therefore be said henceforth that culture should be managed in its own merit since it affects attitude towards new venture creation and development as well as uncertainty avoidance (Zainol, 2011). Hence it is clear that the performance of SMEs does not rely solely on EO dimensions of managers or employees but also on moderator factors including cultural orientation.

Opening up their statement with "innovate or die" Madhoushi *et al.* (2011) proved that the dimension of EO is moderated by other factors both internal and external. Their study results indicated that entrepreneurial orientation both directly ($B = 0.38$) and indirectly through the knowledge management ($B = 0.377$) affected innovation performance. Hence, knowledge management acts as a moderator factor between entrepreneurial orientation and innovation performance.

Religiosities which can be both an internal and external factor also have an impact on EO and business performance. Zulkifli and Rosli (2013) found a positive relationship between religiosity, Entrepreneurial Orientation and Business Success. In Tanzania the country have no region but its people have religions where they worship. Therefore SMEs managers should take

this into consideration since from the available literature it has shown a positive relationship with performance.

In one study conducted in Tanzania, it was found out that workshop, vocational training, industrial, managerial experience and family background do influence the growth of SMEs in Tanzania (Isaga 2015). In contrary, Entrepreneurial experience and level education successfully completed by the owner-manager are not important in explaining SMEs growth. The study gives evidence on the importance of moderating factors of EO on firm performance.

External Factors Moderating Entrepreneurship Orientation

Despite the noticeable contribution of SME in both economic growth and economic development, they have been for long time faced with social and economic problems mostly being economic problems. Kira and Zhongzhi (2012) argue that the main problem facing Tanzania SMEs is lack of access to finance. Their results specified that firm's location, industry, size, business information, age, incorporation and collateral influence access to debt finance. Lack of enough capital limits the growth and expansion of most SMEs in Tanzania. SMEs access to finance is essential for cash flow management and reduces shortage of cash flow (Kira and Zhongzhi, 2012). Access to finance is very importance for firms to be innovative, competitive, aggressive, proactive and autonomy.

Most SMEs rely on internal resources since they can't access external finances and this limits their expansion and growth (Kira and Zhongzhi, 2012). Ullah *et al.* (2013) emphasize that access to resources and then its efficient reallocation or reorganizing is essential to entrepreneurial orientation; otherwise, wastage of available resources is adverse or can offset entrepreneurship. The argument means that SMEs need more access to financial resources and they have to efficiently and effectively utilize such resources when attained. Kira and Zhongzhi (2012) point out that there are two main sources of external financing for SMEs which are equity and debt.

The literature shows a positive relationship between SMEs capital structure and their characteristics. The characteristics include attributes such as firm's location, firm industry, firm size, firm age, firm's legal status and the availability of collateral and business information. Before the privatization of the national enterprises, Cooperative Rural Development Bank (CRDB) used to give credits with favorable conditions but since then these attributes are not in favour of many SMEs hence poor access to finance.

Therefore there exists a financial gap between the demand and supply of credits to SMEs (Kira and Zhongzhi, 2012).

Ambad and Wahab (2013), state that when business environment seems as hostile, proactiveness affects firm performance positively. This proves that the moderating factors of EO (which constitute the business environment) affect performance positively. Previous studies have shown consensus that hostile environmental factors affect entrepreneurial orientation and performance. Khandwalla (1977), states that the environments are hostile when it is risky, stressful, and dominating. Hostility is manifested by the degree of threat to the firm and characterized by unsafe industry setting, powerful competition, and lack of business opportunities (Covin and Slevin, 1989).

The literature also proves that the contingency theory still holds that the strength of the entrepreneurial orientation-relationship varies with the existence of a third variable such as organizational structure, environment, and others. For example, empirical research found that there is no positive straight effect of entrepreneurial orientation on firm performance but, when the environmental uncertainty is included as a moderating factor, entrepreneurial orientation is positively related to firm performance (Ambad and Wahab, 2013; Li *et al.*, 2005).

Although not proved statistically in Tanzania, the cross-cultural study conducted by Kreiser *et al.* (2002) proved that among 1671 SMEs in Australia, Costa Rica, Finland, Greece, Indonesia, Mexico, the Netherlands, Norway, and Sweden, the effect of entrepreneurial orientation was found to be stronger when the environment is hostile.

Nuiami (2014) found out that environmental instability (environmental dynamism, environmental complexity and environmental predictability) has a significant positive indirect effect on innovation performance. This indirect moderating effect calls for a precautionary measure to take environmental factors into consideration for firms to grow and prosper. The literature in that study shows that several other studies have been conducted relating EO, environment factors and firm performance and they concluded that there exists a positively relationship.

It is in this same context that Ullah *et al.* (2013) emphasize that both environmental dynamism and environmental heterogeneity are significant predictors of entrepreneurial orientation and has a positive influence on it. This is due to the fact that the factors were highly correlated at $5\% = 0.05$

level of significance. To support the argument, the literature further shows that Jalali (2012) found out that environmental determinants effected innovativeness and risk taking which are also two basic dimensions of entrepreneurial orientation. This fact shows that the dimensions of EO are moderated by other factors and therefore it is premature to conclude that there is a direct link between EO dimensions and firm performance. This is in contrast with Jalali (2012) who argues that innovativeness as one of the EO dimensions is the most effective strategy that help firms to handle the hostile environment hence export performance.

Soininen *et al.* (2012) carried out a study to find the impacts of global economic crisis on SMEs and to test if EO matters. Using a sample of almost 200 Finnish small and medium-sized enterprises the study indicated that the different dimensions of the EO can have diverging effects on how firms are affected by the recession. In general, the more innovative and proactive the firm is, the less its operations are affected by the recession and the more risk-taking the firm is, the more its profitability is affected by recession. Taken together this means that socio-economic factor as a moderating factor has a direct and indirect effect on EO and firm performance.

In supporting the argument that risk can be associated with a number of factors, such as political instability, uncooperative policy and regulatory environment and information asymmetry, which may encumber the realization of a firm's objectives. Tang and Murphy (2012) point out that firms operating in less developed business support services and fragile regulatory environments, experience less protection and are often obligated to unethical behaviours, such as corrupt transactions to legitimize their business. This argument shows the need to address political and socio-economic factors for firms to experience performance, growth and stability.

Some studies reveal that environmental turbulence strongly influences (moderates) all dimensions of EO (Stanley, 2014). As performance of business organizations is subject to environment turbulence, it can be argued that, this environment has impact on the entrepreneurial success. Therefore environmental turbulence is a dynamic, unpredictable, expanding, and fluctuating environment. It is an environment in which the components are marked by change and these changes affects entrepreneurial orientation. (Volberda and Bruggen, 1997).

Summary

In summary the literature above explains the importance of moderating factors of EO on firm performance. These moderating factors of EO as

summarized together in the literature review above are grouped into internal and external factors and they range from organization structure, cultural orientation, political and legal framework to socio-economic factors. It has been found out that these factors affect EO and firm performance.

Conceptual framework

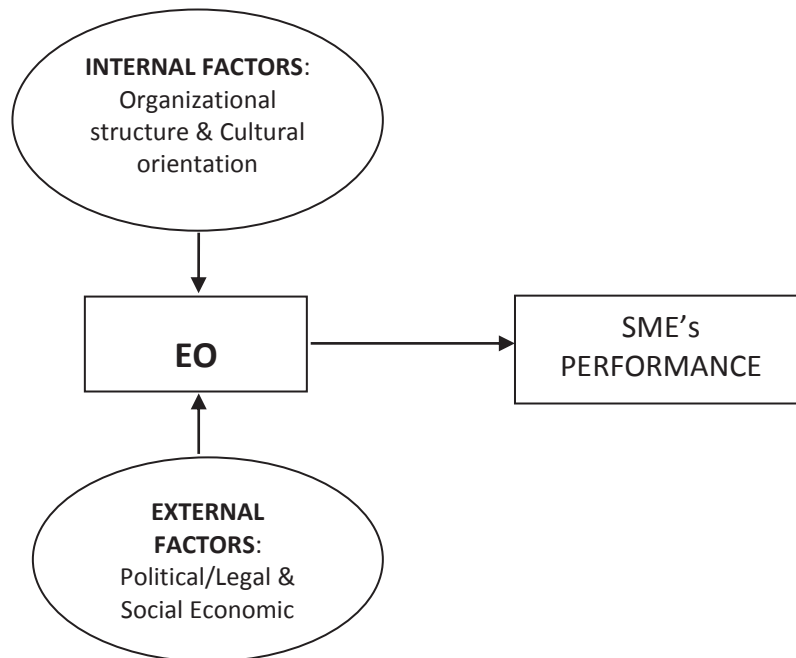


Figure 1: The proposed Conceptual framework

Discussion of findings

The empirical facts on the effects of moderating factors of EO on firm performance have been confirmed. Various researchers have explored internal and external factors that moderate the link between EO and performance. As indicated in the conceptual framework the literature shows the direct and moderating effect of for example strategy, organizational structure, human resource practices, location of the firm, organizational culture and environment, access to finance, legal status, age of the firm and information control system on business performance (Kira and Zhongzhi, 2012).

The literature indicates that there are few studies that have been conducted in less developed countries, Tanzania inclusive. However in the available studies mostly from the developed and developing economies it has been

proved that there is a positive direct and moderating link between EO and SMEs performance.

The limited testing of the effects of the moderating factors of EO on performance in Tanzania and in other emerging economies, as well as the understanding that emerging economies form a different context from previous environments in which EO and SME performance were examined, made this study necessary.

The findings further indicate that EO-performance relationship is more complex than previous studies presents (Ilhami, 2011). However Covin and Wales (2011) allow researchers to use the measure that fits their objectives. It can therefore be noted that the measure of the moderating factors of EO on firm performance is theoretically valid. The findings from this measure that the moderating factor affects EO and firm performance can also be relied on.

Conclusion and Recommendations

Based on theoretical background and the conceptual model, this research paper assessed the effects of the moderating factors of EO on SMEs performance. Together with previous studies this study has presented and discussed studies by Lumpkin and Dess (1996), and Covin and Slevin (1989) whose findings concluded that there is a contingent relationship between EO and the external environment. The literature indicated that there is a positive direct and moderating effect of these moderating factors on the relationship between EO and SMEs performance. Therefore, dimensions of EO alone cannot determine SMEs performance unless they are mingled with moderating factors. Recall that this is conceptual paper and due to few studies conducted in Tanzania, a research must be conducted to test statistically the effects of these moderating factors of EO on firm performance.

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