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Competitive Strategy Orientations of Small and Medium Business Owners and their Performance Impacts: The Case of Paint Manufacturing SMEs in South-Western Nigeria

Ade Oyedijo (Department of Business Administration and Management Technology, Lagos State University, Ojo, Lagos, Nigeria)

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Abstract

This paper outlines the results of a study of the competitive strategy orientations of 92 small and medium sized paint manufacturing enterprises in Southwestern Nigeria. Three sets of paint manufacturing SMEs which had substantially divergent competitive strategies, i.e. Differentiation (28) Low cost (33) and mixed strategies (31) were identified and compared using data generated through a survey. The data analysis using correlation matrix and simple linear regression reveals a highly significant impact of the three strategies on the performance of the sampled firms. Results of the analysis revealed a significant difference between the performance of companies that used differentiation and low cost as standalone strategies and the performance of firms that used the two strategies together. Those using mixed strategies performed better than those using stand alone strategies on all the three performance parameters of total income/revenue growth, sales growth and customer complaints. A possible explanation for this result is the flexibility which the combined use of the two strategies introduces into the operation of the firms that adopted this dual approach.

Author(s)

Ade Oyedijo

Department of Business Administration and Management Technology Lagos State University, Ojo, Lagos, Nigeria
Email: oyedijo98@yahoo.com

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Introduction

The strategic management practices of small and medium-sized enterprises (SMEs) have received little specific attention from researchers. As in many other areas of scholarly inquiry into business activity, empirical research in strategic management has tended to focus upon larger concerns (e.g. Gup and Whitehead 2000; Lenz, 1990; Leontiades and Tezzel, 1994; Hopkins and Hopkins, 1994, 1997; Miller and Cardinal, 2001; Haveman, 1993; Harris and Ogbonna, 2001). In recent years while much attention has been given to small scale businesses by Nigerian policy makers, politicians, practitioners and academics, little research has been done on strategic management practices within the small business sector of the Nigerian economy. This is surprising in view of the importance of small and medium scale business organizations as critical engines of employment and economic growth (Brouthers, et.al. 1998). In the case of the Nigerian manufacturing sector, over 90% of all businesses are SMEs according to generally accepted official definition (SMEDAN, 2009). The under representation of SMEs in terms of strategic management research data seems inappropriate when the scale of this sector is considered. This fact, together with the key role that manufacturing inevitably plays in economic prosperity, strongly suggests the importance of increasing our understanding of the management of strategy in manufacturing SMEs in Nigeria.

Given recent government policy regarding the identification and encouragement of high-growth SMEs in Nigeria, an important gap in the extant literature is any reliable empirical evidence concerning possible linkages between business performance and the strategies utilized by SMEs. The primary objective of this study therefore, is to reveal the competitive, business level strategies that are being utilized by these firms and the impacts of such strategies on the performance of the sampled enterprises.

Background – The Significance of SMEs

According to SMEDAN (2009), a business is defined as small in the manufacturing sector if it employs fewer than 100 employees. While there is no official definition of what constitutes a medium-sized enterprise, businesses with between 100 and 199 employees are generally considered medium-sized (McMahon, 2001). Thus SMEs in the manufacturing sector may be considered as organizations employing less than 200 workers.

The strategic importance of SMEs in the economic development of any nation is well recognized. Kilby (1965) observes that small and medium scale enterprises are the spring boards for inventions, adaptations and general technological development. According to Ogundele (2007), SMEs represent 90% of the enterprises

in African, Caribbean and Pacific (ACP) countries. They also provide 70% of employment opportunities for the citizens and promote the development of local technology. Kuratko and Hodgetts (2001) have observed that small businesses employ 53% of the private workforce and account for 47% of sales and 51% of private sector gross domestic product.

SMEs are generally regarded as important to world economies (Birch 1989; Storey, 1994). In fact, it has been argued that SMEs make up the largest business sector in every world economy (Culkin and Smith, 2000). For many years now, governments in different parts of the world are increasingly promoting and supporting the growth of SMEs as a part of their overall national development strategy (Abdullah, 2000; and bin Bakar, 2000). Apart from the fact that they dominate in terms of absolute numbers, SMEs are very important because they are the key drivers of employment and economic growth (Wang, Walker and Redmon, 2008). At a macro economic level, SMEs are considered by governments as a keystone to regional economic and community regeneration because such firms absorb back into the workforce the employees that are made redundant by the restructuring, rationalization downsizing and outsourcing taking place in large firms (Storey, 1994; Frank and Landstorm, 1998). This provides income to regions thereby stimulating local economic activity and driving wealth and further creation of employment (Walker and Webster, 2004). SMEs are also commonly noted for contributing to economic growth through their innovative activities despite their generally limited capacity for research and development (R&D) investment (Acs and Andretch, 1990). For example, Peacock (2004) reported that SMEs in Australia contributed 54% of all significant technology innovations even though their share of R&D investments represented just 20% of technical innovation expenditure. It has also been argued that SMEs contribute to the development of the society through the redistribution of political power arising from the ownership of small and medium scale businesses by more people in a country (Deaking, 1996; Storey 1994). In addition, SMEs offer consumers a greater opportunity for choice by operating in fragmented or niche markets which larger firms either cannot economically enter or are reluctant to enter because of 'unattractive' risk – return consideration (Brouthers, et. al; 1998). Nigerian SMEs present a unique setting for the study of the practice of strategic management. Unlike SMEs in Western and Asian economies, most SMEs in Nigeria generally lack access to funds and structured government support despite the existence of some institutions established for this purpose. Thus, most of them struggle for survival amid intense competition and rivalry with larger firms, and so may seek to employ strategies that are designed to help

them compete and navigate the difficult environment in which they operate.

Literature Review and Theoretical Framework

A popular argument in the literature is that the pursuit of efficiency or cost leadership requires a particular kind of organizational structure and culture that is very different from the one that would be appropriate for innovation or differentiation (Porter, 1980; Bowman, 1990). According to this view, it is not feasible to pursue both strategies simultaneously. It is argued that the skills and resources, the structure and systems and the culture, style and overriding values of the organization needed to best deliver low cost products are quite unique and distinct from those required by a firm to achieve superior profit performance and a sustainable competitive advantage through a strategy of differentiation (Bowman, 1990). While cost strategy requires skills in controlling the raw materials, power, components, labour, machinery or storage space, as well as a heavy investment in training to help reduce the costs of scrap and reworking, product differentiation requires a clinical skill that predisposes a firm to a deeper understanding of its customers' requirements than could be done by its competitors. A product differentiation strategy thus requires a high degree of competence in a wide area of management and organization and a labour force that is highly trained, experienced, self-motivated and able to work together as a team. People are the key resource in this organization and are thus expensive. While cost leadership requires extensive effort to improve the efficiency of the firm, the quality of the products or services carries a greater emphasis under a differentiation strategy.

Contrary to the theoretical position of Porter (1980) and Bowman (1990), empirical studies have found that a firm can use differentiation strategy and low cost strategy together and still perform very well (e.g.) Murray, 1988; Miller, 1992; Kotha and Swamidass, 2000). The conflicting positions between theory and the findings from empirical tests of the theory suggest the need for a further investigation of the postulates and the existing results in different organizational contexts. The small business sector provides an opportunity for this.

Hypotheses

Based on a review of theory and previous studies, it is postulated as follows:

1. Total income and sales growth in paint manufacturing SMEs that are pursuing product differentiation or cost leadership strategies exclusively will be higher than in paint

manufacturing SMEs that are pursuing both strategies together.

2. Paint manufacturing SMEs that are using product differentiation or cost leadership strategies exclusively will experience less customer complaints than paint manufacturing SMEs that are mixing product differentiation with cost leadership strategies.

Sample, Data and Methodology

The Sample and Data Collection

The population of the study was owner-managers of small and medium paint manufacturing firms and they were located across Southwestern Nigeria. A data base on small and medium manufacturers held by the Nigerian Association of Small and Medium Scale Industrialists (NASMSI) provided the sample frame from which the final pool of southwestern owner managers of small and medium paint manufacturing firms was drawn. The final pool of owner – managers to whom questionnaires were mailed was 128. It is acknowledged that due to constraint of finance available to the author, the survey involved a one wave effort and resulted in the return of 92 usable questionnaires out of the 103 received. This gives an effective response rate of 89.3%.

The above hypothesized relationships were tested using data collected through self-administered, structured questionnaires containing essentially close-ended questions. The questionnaires were administered on chief executives and marketing directors, or in some cases other directors within the 92 randomly selected small and medium scale paint manufacturing companies in southwestern Nigeria. In order to appreciate the study setting and test the questionnaire prior to its use, a pilot study involving face-to-face interviews with five small business owner – managers was undertaken. The questionnaire was then refined in the light of experience.

This research is concerned only with small and medium paint manufacturing businesses in southwestern Nigeria. There are two reasons for this. First, over the last few years, the performance of the small and medium scale manufacturing sector in Nigeria has been a major pre – occupation of policy – makers and government departments dealing with industry and trade. The sector has been characterized as non – competitive by international standards and it is considered to have failed in performing the traditional and modern social and economic roles of the sector (Oshagbemi, 1998; Ogundele 2007). The second reason is that it is highly probable that cross-industry differences in the nature of business activities could confound findings relating to SME

strategies and to SME growth and performance more generally. Such influences are, to a reasonable extent, controlled for by examining a single industry.

Additional focus is provided to this research by considering only paint manufacturing SMEs that are legally organized as proprietary companies. There are two main reasons for this further narrowing down of the unit of analysis. First, as Freedman and Godwin (1994) indicate, a particular concern with legally organized proprietary companies is not uncommon among SME researchers worldwide. As they observe, “it would appear that, in so far as the issue is concerned, the limited liability company is of more interest to the small business research community than are unincorporated firms.

Second, the primary concern in this research is with SME strategy, growth and performance, and it is more likely that these will be evident in businesses that are legally organized as proprietary companies (Freedman and Godwin 1994; Grey 1992; Hughes and Storey 1994). There are 128 paint manufacturing SMEs legally organized as proprietary companies in Southwestern Nigeria at the time of this study. The final data used in this study covered 92 firms.

Table 1: Selected Demographic Characteristics of Respondents and Their Firms

Age of business	Frequency	Percent
0 – 5	16	17.39
6-10	49	53.26
Above 10	27	29.35
Total	92	100%
No of employees		
Below 50	40	43.48
51-100	38	41.30
Above 100	14	15.22
Total	92	100%
Product diversity		
Single–line product	79	85.87
Multi-line product	13	14.13
Total	92	100%
Gender of owner manager		
Female	07	7.61
Male	85	92.39
Total	92	100%
Qualification held		
Secondary school	16	17.39
Polytechnic Diploma	27	29.35
Four years degree/ HND	40	43.48
Masters degree	09	9.78
Total	92	100%

Source: Field Survey (2011)

Construct and Questionnaire Design

Two constructs were measured in this study. They are performance and competitive strategy orientation. Performance was measured by sales growth over a period of three years, reported number of customer complaints over a period of six months, total income/revenue growth over a period three years and growth in customer base over a period of three years.

Following Boyd’s (1991) suggestion for replications of existing strategic management frameworks/constructs, we adapted two of Porters (1980) generic strategies scales to measure product differentiation and low cost strategies. Adaptation of existing strategic management constructs in different environments is not without precedent. Alpkın, et.al. (2005) for example adapted Ramanujan et.al. (1987) and Porter’s (1980) scales in their empirical study of strategic planning trends in Turkish small firms. Suffice to state that in this study, it was decided to reveal the competitive strategies of paint manufacturing SMEs in southwestern Nigeria and assess the impacts of such strategies on their performance. The causal links between the key components in the construct are also investigated.

The questionnaire was made up of four sections A, B, C and D. Section A contained six main questions that deal with the demographic characteristics of the respondent owner – managers and their firms. Section B contained questions that deal with the competitive strategy orientations of the firms. In this section, firms were asked

to describe or choose their methods of handling competition using a series of items that covered the differentiation and low cost approaches. Section C contained questions that deal with the sales growth, total income/revenue growth, incidence/frequency of customer complaints in the firms, and growth in customer base. These parameters were used as measures of performance.

In order to assess the importance of differentiation and low cost strategies to small business owner – managers, a factor analysis was employed to establish the key factors important in competitive strategy decision making. The importance of the 10 variables/items highlighting the competitive strategy construct is presented in Table II and it shows that all the 10 variables are statistically significant with all variables showing high mean values.

A visual assessment of the correlation matrix of the principal components of the factors indicated a considerable degree of inter – item correlation (see table IV). In addition, from the correlation matrix, the Bartlett test of Sphericity ($p < 0.00000$) and the Kaiser – Meyer – Olkin (KMO) measure of sampling adequacy index (value of 0.730) confirm the appropriateness of the data for exploratory factor analysis (EFA). The exploratory factor analysis with varimax rotation produced the two factors, i.e. differentiation strategy and low cost strategy, that we used as our study constructs. Differentiation strategy and low cost strategy were used as dimensions of generic competitive, business level strategies. The factor loading of the items shown in table IV confirmed the adapted scales as displayed.

Table 2: Factor Loading of Generic Strategies

	Initial Eigen Value			Extraction sums of square loadings			Rotation sum of square loadings		
	Total	% of variance	Cumulative %	Total	% of variance	Cumulative %	% of variance	Cumulative %	Total
1	6.247	62.076	62.076	4.851	58.759	58.759	2.423	49.625	49.625
2	1.229	8.509	70.585	0.906	10.641	69.400	2.216	19.775	69.400
3	0.719	7.177	77.762						
4	0.613	6.291	84.056						
5	0.561	5.861	89.917						
6	0.503	4.192	94.109						
7	0.471	3.927	98.036						
8	0.389	1.240	99.276						
9	0.368	0.658	99.342						
10	0.328	0.066	100.000						

Extraction method: Exploratory factor analysis, Total variance explained: 69.4%

The means, standard deviations and mean differences from the test values are shown in Table III. The reliabilities and correlation coefficients for each variable are shown in Table IV. Each mean is significantly higher than the mid value of the scale from 1 to 5 (3) as the test value of the one sample test. The Cronbach's alpha reliability scores of differentiation strategy, low cost strategy, sales growth, total

income/revenue growth, incidence/ frequency of customer complaints, and growth in customer base are 0.91, 0.88, 0.93, 0.94, 0.89 and 0.92 respectively. All the scales are above the generally accepted reliability level of 0.07 (Nunnally, 1978). Results of correlation analysis showed that the variables are positively and strongly correlated ($P < 0.01$).

TABLE 3: Descriptive statistics of the variables showing means, standard deviations, mean differences and one sample tests

Variables	Test value	Mean	Std deviation	Mean difference	T	P value
Differentiation strategy	3	3.9107	0.9638	0.8977	10.441	0.000
Low cost strategy	3	4.1078	0.6817	0.9391	10.433	0.000
Sales growth	3	3.8912	1.0333	0.9029	11.317	0.000
Total income/revenue growth	3	3.8716	0.8135	0.9486	11.973	0.000
Incidence/frequency of customer complaints	3	3.7156	1.0331	0.9299	11.316	0.000
Growth in customer base	3	3.9118	0.7136	0.9019	10.441	0.000

Note: Based on a scale of 1 (totally disagree/not important) to totally agree/very important)

Table 4: Reliabilities and correlations of the measures

Variables	0	1	2	3	4	5	6
Differentiation strategy	0.94	1					
Low cost strategy	0.87	0.7161**	1				
Mixed strategy	0.96	0.7314**	0.7112**	1			
Sales growth	0.88	0.6382**	0.6711**	0.6831**	1		
Total income/revenue growth	0.89	0.7153**	0.7132**	0.6441**	0.7131**	1	
Incidence/frequency of customer complaints	0.90	0.6780**	0.6781**	0.5432**	0.6720**	0.6223**	1
Growth in customer base	0.91	0.6721**	0.6381**	0.6721**	0.5311**	0.6722**	0.6451**

** $P < 0.01$ (one sample t – test)

The nature and direction of the relationships among the generic strategies (Differentiation, Low cost and Mixed) and performance variables (sales growth, total income/revenue growth, incidence/frequency of customer complaints, and growth in customer base) are examined by multiple regression analysis. Performance variables were regressed against Differentiation strategy, Low cost strategy and Mixed strategy using four models. Table V presents the effect of the generic strategies on performance for the three samples. The finding shows that for the three samples, sales growth, total income/revenue growth, incidence/frequency of

customer complaints and growth in customer base are significantly affected by Differentiation, Low cost and Mixed strategies. The result also shows that there is a significant difference between the performance of companies that are using Differentiation strategy or Low cost strategy alone and the performance of companies that are using the two strategies together. Result of the analysis showed that the performance of firms that were using Differentiation and Low cost as standalone strategies was lower than the performance of the firms that used mixed strategies.

Table 5: Effect of Competitive Strategies on Firm Performance

(1) Constant	<u>Model 1</u> Dependent variable: sales growth			<u>Model 2</u> Dependent variable: Income/revenue growth			<u>Model 3</u> Dependent variable: frequency of customer complaint			<u>Model 4</u> Dependent variable: Growth in customer base		
	B	t	Sig.	B	t	Sig.	B	t	Sig.	B	T	Sig.
Independent variables	7.145	71.189	0.000	6.318	63.419	0.000	5.641	48.960	0.000	5.869	49.636	0.000
Differentiation strategy	0.516	4.318	0.000	0.473	4.486	0.000	0.512	4.557	0.000	0.533	4.363	0.000
Low cost strategy	0.436	4.137	0.001	0.512	4.335	0.002	0.514	4.471	0.000	0.516	4.318	0.002
Mixed strategy	0.841	7.436	0.000	0.833	6.317	0.000	0.861	7.426	0.000	0.813	7.633	0.000

P > 0.05

Discussion of Result

This study examined the choice of generic competitive, business level strategies by paint manufacturing SMEs in southwestern Nigeria and their impacts on the sales growth, revenue growth, incidence of customer complaints and growth in customer base. The study showed that Differentiation strategy, Low cost strategy and Mixed strategy are highly adopted by the sampled paint manufacturing SMEs and that all of them affect each other positively. The study showed that the generic strategies are highly positively correlated and are not alternatives to each other contrary to the theory of Porter (1980) that organizations must have different sources and skills to be able to implement these different strategic postures successfully.

The finding of this study supports and reinforces the conclusion reached by some previous researchers that Differentiation strategy and Low cost strategy can be followed by a firm simultaneously and profitably provided that the firm possesses an appropriate blend of organizational control procedures, incentive systems, leadership styles as well as the structure, skill, shared perspective, culture, resources, climate and atmosphere required to implement the strategies effectively (e.g. Murray 1988; Miller 1992; Gupta 1995; Kotha and Swamidass 2000). The result is also consistent with empirical evidence which suggests that organizations simultaneously pursue a mix of (perhaps contradictory) strategies (Bowman and Ambrosini, 1997; Whittington, et.al 1999). A combination of the two strategic orientations into a dual strategy may enhance the strategic agility of a firm and contribute to its performance more than if only one of the two strategies was used.

Managerial Implications

With reference to the managerial implications of the findings, it can be asserted that the evidence of reliability, item correlation, tests of goodness of fit and conceptual coherence associated with the results of this study suggest

that the findings will be useful as an important insight for policy makers, practitioners and academic researchers who are interested in strategic management in the small business sector. Specifically, the managerial implications of this study point to the need for firms to explore a combination of the two strategies i.e. Differentiation and Low cost, to achieve competitive advantage and improved performance.

Implications for Theory

On the theoretical front, the findings from this study appear to contradict the theory of Porter (1980) that a firm cannot successfully use Differentiation and Low Cost strategies simultaneously and profitably on the basis that each strategic posture requires different organizational skills, practices and conditions. This study suggests the need for further rigorous empirical test of the bases of Porter's theory.

Summary and Conclusion

The results of this study show a high and positive correlation between Differentiation, Low Cost and Mixed strategies. The result also reveals a highly significant impact of the three strategies on the performance of the sampled firms. Since significant differences were found in the performance of firms that were using stand alone strategies and those that were using mixed strategies with the latter category doing better on all the performance measurement parameters used for the analysis, we may conclude that a mixed strategy is practically more useful than a standalone strategy. A possible explanation for this result is the strategic synergy which the integration and combined use of Differentiation and Low Cost strategies introduces into the operations of the firms that adopt this dual approach. Apart from pointing to the possibility of successfully combining Differentiation and Low cost strategies to achieve competitive advantage and improved performance, the result of the study contradicts the theory of Porter (1980) that the two popular generic strategies Differentiation and Low cost are mutually exclusive.

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