

The Relationship between Distinctive Capabilities, Innovativeness Strategy Types and the Export Performance of Small and Medium-Size Enterprises (SMEs) of Malaysian Manufacturing Sector

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Abstract

This study was conducted to investigate the relationship between distinctive capabilities, innovativeness, strategy types and the export performance of SMEs in the Malaysian manufacturing sectors. The conceptual framework is developed based on the distinctive capabilities, innovativeness, strategy types and the export performance. This study is based on a sample survey consisting of 121 SMEs in the manufacturing sector. Using structured questionnaires, the data were collected by mail as well as interviews with owner-managers of the SMEs. The finding indicates that there is no significant relationship between distinctive capabilities, innovativeness and the strategy types on the export performance of SMEs.

Introduction

Small and medium- sized enterprises (SMEs) play a significant role in the business system of both developed and developing economies (United Nations, 1993). This study examines the impact of distinctive capabilities, innovativeness and strategy types on the export performance of SMEs, and the model built suggested the relationship between distinctive capabilities, innovativeness and strategy types can affect SMEs export performance. In the Malaysian context, discussion on small-sized enterprise is always associated with medium-sized enterprises. Like other developing countries, Malaysia is also having difficulties in considering a definition of SMEs. This study defined SMEs as firms that employ less than 200 employees, based on the previous research done by Salleh, M. I. (1990) and Mohd. Asri (1999). This definition is similar to the one used by the World bank (1984), United Nations (1986) and the Asian Development Bank (1990) who defined small enterprises as firms employing fewer than 50 employees and medium enterprises as firms employing between 50 to 199 employees.

Literature Review

The Distinctive Capabilities

The literature on strategic management suggests distinctive capabilities or competencies as an important part of an organization's resources and competitive advantage. Mintzberg and Quinn (1991) noted that theoretical relevance of distinctive

capabilities as source of competitive advantage can be traced back to the early work by Selznick (1957).

Graig and Grant (1993) defined a firm's distinctive capabilities or competencies as both tangible and intangible resources, comprising of financial, physical, human, technology, reputation and relationship which a firm owns.

Aaker (1989) noted that the assets and skills of the firm, which are the basis for competition, provide the foundation for sustainable competitive advantage. Furthermore, Aaker pointed that it is the essence of strategic management to develop and maintain these assets and skills as well as to choose these strategies so that they can be turned into sustainable competitive advantages.

Identifying and classifying resources or assets in a firm is a difficult task (Graig and Grant, 1993). However, basically, resources can be grouped into tangible and intangible assets. Ansoff, (1965), Wheellen and Hunger (1995), and Price (1996) classified business functional areas into general administration, operations/ production, marketing, finance, human resource management, engineering and R & D and public relations. Hitt and Ireland (1985) developed distinctive capabilities instrument comprising 55 capabilities grouped according to seven functional areas; a) general administration, b) production/operations, c) engineering, research and development, d) marketing, e) finance, f) personnel, and g) public and governmental relations. The distinctive capabilities variables used in this study are adopted from this literature review.

Innovativeness

Innovativeness is defined by Urabe (1988) as the generation of a new idea and its implementation into a new product, process, or service, leading to the dynamic growth of the national economy and the increase of employment as well as to a creation of pure profit for the innovative business enterprise. Further, Albach (1988) indicated that development of a new idea into a product, process, or service can increase a firm's market share, and leads to a better firm's performance. Firms which effectively implement innovativeness can enjoy several possible profits. Firms can benefit from increased productivity and adaptability owing to process improvements (Sankar, 1991, Burgelman and *et al.*, 1988). In addition, implementation of new ideas can increase company productivity and efficiency, lead to higher firm's performance (Edosomwan, 1989). Study of Edosomwan (1989) also showed that effectively using organization's new ideas will create an environment conducive to innovativeness. The developments can then create new opportunities for the firm and provides firms with competitiveness advantages (Abernathy and *et al.*, 1988).

In simple terms, innovativeness involves the commercial exploitation of new ideas. As Freeman (1982) indicated that innovativeness is the first commercial transaction involving the new product, process, system or device.

In the study by Damanpour (1987), specialization and organizational slack had strong effects on technical innovation. The importance of innovativeness has been acknowledge conceptually but rarely examined empirically. There is empirical support for positive relationship between competitive intensity and innovativeness (Zajac, Golden and Shortell, 1991). According to Damanpour (1987), innovativeness can take place in shorter the manufacturing cycle time and lowering the cost, and also by changing the product design, product variety and management process by restructuring the organization. This study adopted Damanpour model in measuring the innovativeness of the SMEs. However, the recent study done by Lin and Chen (2007) shows that 80% of the surveyed firms applied technological innovation in the firms, and the technological innovation factor did not explain the sales.

Strategy

Strategy is defined as a major action taken or planned by the management of a business organization, considering its resources, skills and environment risks. Corporate strategy usually refers to the product- market choices of the firms (Hofer and Schendel, 1978).

Strategic management is important to an organisations (David, 1999, Wheelen and Hunger, 1995). Firms use business strategy to outline the fundamental steps that they plan to follow in order to accomplish their objectives. Glueck and Jauch (1984) grouped the objectives to be achieved by organisations as to achieve long range objectives such as to generate profits, improve marketing and sales, objectives related to the workforce such as efficiency, motivation, as well as improving corporate responsibility.

Diversification refers to the act of extending the number of product lines or entering into a variety of industries. Vertical integration is used to mean the act of attempting to control material resources (back- ward integration) or to control the channel of distribution (forward integration).

There are three different levels of corporate level strategy, business level strategy and functional level strategy, the theoretical and empirical studies of the relationship between strategy and organisational performance have mainly emphasised on business level strategy (Lee, 1987).

Porter (1980) noted that a firm can gain its competitive advantage by producing value for its customers. Porter also stressed that a firm can gain its competitive advantage by performing the chain of strategically important activities (such as

production, marketing, sales, service, human resource management, technology development, procurement activities) cheaply or better than its competitors. Further, Porter concluded that strategic types based on these activities are known as generic strategies. According to Porter, the three generic strategies are low cost, differentiation and focus. This study adopts Porter's three generic strategies (low cost, differentiation, focus) for the research. Since this study chose SMEs as the sample, "focus strategy" is adopted as "niche strategy" to suit to the sample of this study.

The Performance

The primary goal of adopting effective management process is improved organisational performance. As such, some methods of measuring organisational performance are needed to determine how well an organisation is functioning as a result of adopting the strategic management process.

Organisational performance can be measured by many criterion. In general, the literature suggests that organisational performance is commonly measured in terms of effectiveness, efficiency, growth and productivity.

However, according to Robinson (1982); Montanari, Morgan and Bracker (1990), firms tend to focus on effectiveness when measuring their organisational performance.

Montanari, Morgan and Bracker (1990) suggested that organisational effectiveness may be measured in terms of financial measures, operational measures as well as behavioural measures. First, the authors noted that the financial measures such as profitability and growth can be used to access the financial performance of an organisation. Second, the operational measures such as productivity, resource acquisition, efficiency and employee reaction can be adopted to assess the effectiveness of the work flow as well as work support in organisations. Third, behavioural effectiveness measures such as adaptability, satisfaction, absence of strain, development and open communication can be adopted to determine individual performance.

Goodman and Pennings (1997) pointed that there is still disagreement on the meaning of organisational effectiveness. According to the authors, in addition to various definitions by different authors, there is also the tendency among authors to view effectiveness as either one-dimensional or multidimensional.

Goodman and Pennings further claimed that the underlying differences in conceptualising organisational effectiveness resulted from the different views concerning the nature of organisations. According to the authors, the different views concerning the nature of organisations have implicitly or explicitly determined the conceptual definition of organisational effectiveness. The first view sees an

organisation as a rational set of arrangements and emphasised toward achieving certain goals defined effectiveness in terms of the goals attainment. Second, the open-system perspective of organisations defined effectiveness as the degree to which an organisation can maintain all its components.

The process of determining the performance of an organisation requires the selection and the measuring of a set of key variables that can allow the organisation to detect as well as monitor its competitive position in the business in which it engages. In another words, measuring performance is also one of the important steps in the strategic control process (Griffith, 1987; and Wheelen and Hunger, 1995).

In Kemp *et al.* (2003) study on the innovativeness and the firm performance indicated that the firm performance could be measured on various concepts, such as sales per employee, value of export, total assets and operation profit ratio. This study adopted Kemp *et al.* measurement of export performance. In this study, the export performance refers to the sales of manufactured products exported to other countries for sale. Export performance is measured in term of average of export sales (average value of export).

Relationship between Distinctive Capabilities, Innovativeness, Strategy and Export Performance.

The ability of an organisation to survive and succeed is influenced by various factors, some of which can and some which can't be controlled. Therefore the performance of an organisation is a function of the controllable and uncontrollable variables (Kim and Lim, 1988).

In this study, the distinctive capabilities variable was based on the seven general functional areas found in most manufacturing firms. The distinctive capabilities variable was measured by using the instrument developed by Hitt and Ireland (1985).

This study adopts Damanpour's (1987) study as the measures of firms's innovativeness performance. The innovativeness in this study is measured from the aspects of lowering costs, changing product design, manufacturing cycle time, product variety and organization restructuring. The distinction between organization and innovativeness is important because it relates to a more general distinction performance and technology (Evan, 1966). Administrative and innovations imply potentially different decision- making processes (Daft, 1978) and together they represent changes introduced in a wide range of activities in an organization. This innovation dichotomy has been shown to relate differently to the same predictor variables (Kimberly and Evanisko, 1981, Damanpour, 1987; Han *et al.*, 1998). According to Damanpour (1991), organizational performance depends more on innovations of different types than each type alone. Further to that, innovation of

different type influence and often complement each other (Han *et al.*, 1998). Innovativeness is more effective in helping organizations to maintain or improve their level of performance (Damanpour and Evan, 1984).

Many studies of organizational innovation have measured innovation by the number of innovations adopted in given time period. When multiple innovations are studied, the influence of innovation attributes decreases. Differentiating studies on the basis of scope of innovations studied should provide useful information for explaining the instability of empirical research findings.

For technical innovativeness, it covers new product, improvement in current product whether in terms of performance or aesthetic, implementation of new automation, new equipment, new processes or technique of operation for shorter cycle time, design for manufacturability and finally improvement in the raw materials or supply.

Management chooses and implements competitive strategies to face the fast and dynamic changes in the environment. Since strategy is meant for competing with other organisations, the results of strategy implementation can be seen from the performance achieved by the organisation (Beard & Dess, 1981; Parnell & Wright, 1993).

The strategies developed by organisations can be influenced by how management perceives the environment faced by them (Daft, Sormunen & Parks, 1988). Even though firms face the same environment, they might choose different strategies (Thomas, Litschert & Ramasamy, 1991).

Organisations in a turbulent environment are likely to choose a differentiation strategy compared to organisations operating in a stable environment (Marlin *et al.*, 1994). In their analysis, Kim and Lim (1988) found that high performance organisations adopting the cost leadership and differentiation strategy operate in different environments. In addition, Parnell and Wright (1993) stressed that organisations implementing the prospector strategy or differentiation strategy enjoy high-income growth as compared to organisations implementing cost leadership and focus strategy. In assisting the foreign manufacturing firms in Malaysia to cope with the new challenges, the Malaysia government has already began accelerating the operation of the manufacturing firms through various steps such as focusing on quality, encouraging more high technology ventures, introducing further tax cuts, developing efficient operations and upgrading the standards of health and safety. These will influence the strategy practices and performance of the foreign manufacturing firms in Malaysia. Furthermore, the Malaysia government will continue to transform the manufacturing industry into a more dynamic sector with

high value added, capital intensive, high technology as well as skill and knowledge intensive manufacturing industry.

The Research Framework

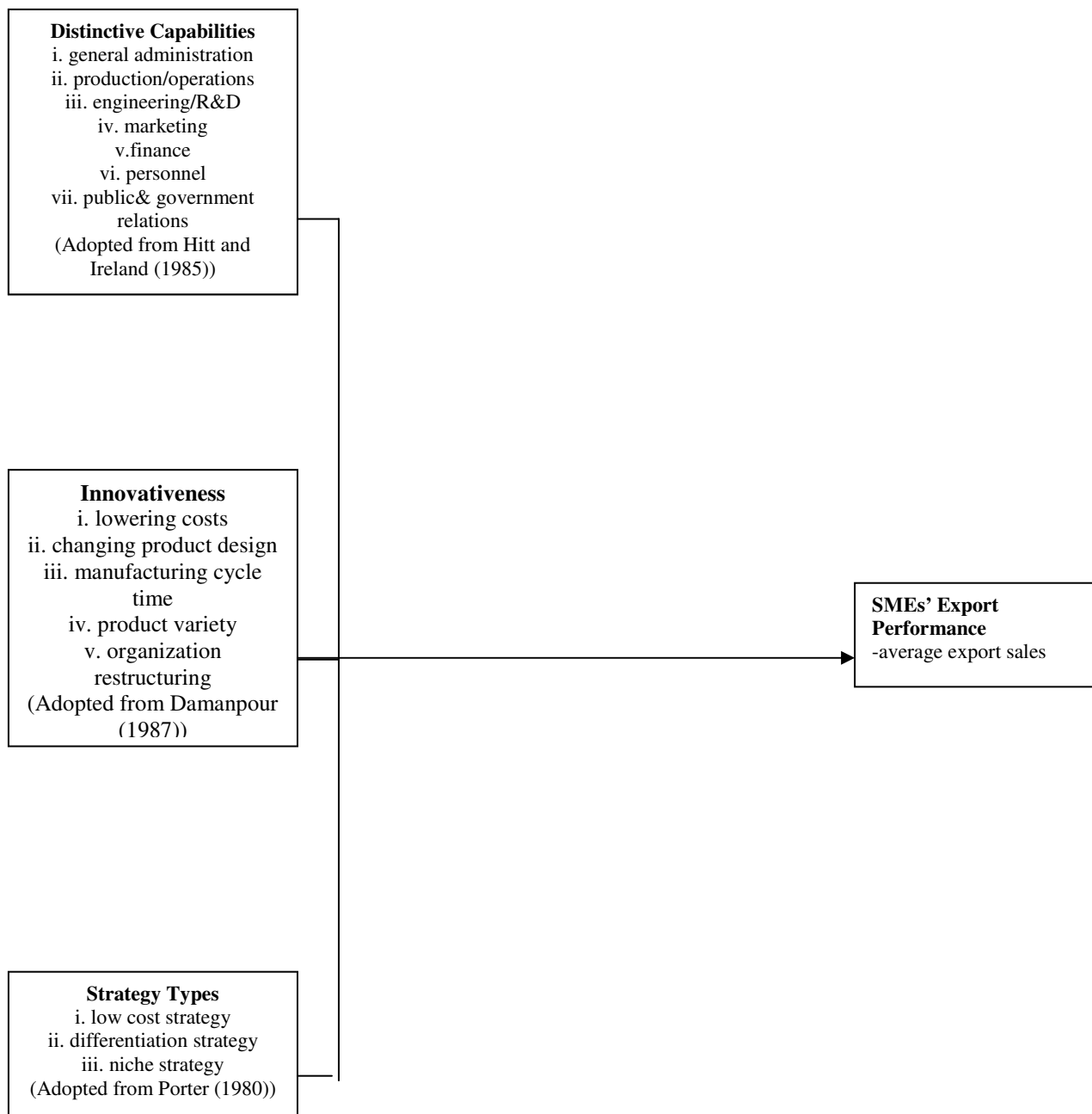


Figure 1: The Research Model

Research Methodology

The SMEs registered in the Small and Medium Industry Development Corporation (SMIDEC) were used as the sampling frame in the study. The organisations selected from the list are those that are involved in manufacturing activities and have been listed for at least five years. Mailed questionnaires were used to collect the data required for the study, at the same time, interview with the Chief Executive Officer (CEO) of certain SMEs was conducted for those SMEs which did not return the questionnaires. The questionnaires were sent to the chief executive officer of each firm requesting them to respond to the questionnaire.

The 50 distinctive capabilities developed by Hitt and Ireland (1985), which grouped into seven functions, were tested in the questionnaires. The seven functions in this study were measured in terms of their levels (degree) in the firms. The levels of the distinctive capabilities were determined by requesting the owners/manager to rate each capability on a five-point numerical scale ranging from “*none*” to “*very high*”.

This study adopts lowering costs, changing product design, manufacturing cycle time, product variety and organization restructuring as the measures of SMEs innovativeness, which grouped into five functions, were tested in the questionnaires. The five functions in this study were measured in terms of their levels (degree) in the firms. The levels of the innovativeness were determined by requesting the owners/manager to rate each level of innovativeness on a five-point numerical scale ranging from “*very low*” to “*very high*”.

This study adopts low cost strategy, differentiation strategy and niche strategy as the measures of SMEs’ strategy types, which grouped into three groups, were tested in the questionnaires. The three types of strategies in this study were measured in terms of their rating in the firms. The rating of the strategy types were determined by requesting the owners/manager to rate each strategy types on a five-point numerical scale ranging from “*least applicable*” to “*most applicable*”.

There are various concepts in measuring performance, such as sales per employee, export sales, growth rates of sales, total assets, total employment, operation profit ratio, turnover and return on investment (Kemp *et al.*, 2003). Further, according to Yusuf (2002), alternative measures of performance may differ, depending on the size and type of firm or its ownership. This study adopted Kemp *et al.* (2003)’s study in measuring the export of the firm.

Statistical Methods Used

This study used various statistical methods to test the hypotheses of the research model. The hypotheses were tested using the regression analysis. The first part of the analysis is concerned with the descriptive statistics of each of the items under each

main variable. The regression analysis is used to test hypothesis 1, 2 and 3. The regression analysis is used to test the significant mean differences between the export performance measure and the distinctive capabilities, innovativeness and strategy types variables.

Hypotheses

Three hypotheses were tested for this study. They are:

1. There is a significant relationship between distinctive capabilities and the export performance of SMEs.
2. There is a significant relationship between innovativeness and the export performance of SMEs.
3. There is a significant relationship between strategy types and the export performance of SMEs.

Results

Table 1 presents the summary of the firms by type of industry.

Table 1: The Sample Firms By Type Of Industry

Type Of Industry	Frequency /(Percentage)
1. Food	17 (14.0)
2. Beverage	8 (6.6)
3. Agricultural products	2 (1.7)
4. Building material & related products	10 (8.3)
5. Stationery	3 (2.5)
6. Packaging, labeling & printing	6 (5.0)
7. Ceramics & tiles	2 (1.7)
8. Tobacco	1 (0.8)
9. Textile products	10 (8.3)
10. Wood products	1 (0.8)
11. Furniture & fixtures	6 (5.0)
12. Paper Products	4 (3.3)
13. Industrial chemical	3 (2.5)
14. Pharmaceutical products	3 (2.5)
15. Rubber products	2 (1.7)
16. Plastic products	4 (3.3)
17. Non-metallic products	1 (0.8)
18. Electrical, electronics products	15 (12.4)
19. Supporting products	8 (6.6)

20. Souvenirs & handicrafts	2 (1.7)
21. Sports goods & equipment	1 (0.8)
22. Jewellery & related products	1 (0.8)
23. Motor vehicles components	2 (1.7)
24. Household appliances	6 (5.0)
25. Laboratory equipment	1 (0.8)
26. Miscellaneous	2 (1.7)
Total	121

The descriptive statistic output for the firm characteristics is presented by Table 2.

Table 2: Firm Characteristics

Firm Characteristics	Frequency /(Percentage)
Founder	23 (19.0)
Cofounder	12 (9.0)
Inherited from family	7 (5.8)
Purchased business not from family	11 (9.1)
Hired or promoted by the company	68 (56.2)
Total	121

As shown by Table 2, most of the respondents, 68 (56.2 percent) of them hired or promoted by the company. 23 (19.0 percent) of the respondents are the founder and 12 (9.0 percent) of them are the cofounder. 11 (9.1 percent) of the respondents purchased the business not from family and seven (5.8 percent) of them inherited or purchased the business from the family.

Regression analysis was adopted to examine the significant relationship between distinctive capabilities and the performance of SMEs. Table 3 presents the results for regression analyses for distinctive capabilities variables towards the export performance of SMEs.

Table 3: Regression analyses result between the distinctive capabilities towards the export performance of SMEs

Independent Variable	R square (R ²)	Sig. F value	Beta Coefficients	t-value
Distinctive capabilities	0.030	0.058	0.173	1.916
Dependent Variable: Export Performance				

** significant at 0.01 level (2-tailed)

By looking at the regression results, distinctive capabilities explains 3.0 percent ($R\text{-square}= 0.030$) of the variation in SMEs' performance. The relationship between the distinctive capabilities and performance is not significant ($p=0.058>0.005$). As such, hypothesis 1 was rejected. Therefore, it could be concluded that the distinctive capabilities do not influence the export performance of SMEs. The relationship between the innovativeness and performance is also not significant ($p=0.303>0.005$). The innovativeness explains 0.9 percent ($R\text{-square}= 0.009$) of the variation of the performance of SMEs. As such, the Hypothesis 2 was rejected. This meant that, the innovativeness does not lead to a better export performance.

Generally, the results of the regression analyses for the variables tested in this study have low R-square. The previous studies on Malaysia SMEs done by Hashim (2000) with 100 respondents and Tarsiah (2007) with 84 respondents also show the low R-square, within range 0.1 to 0.9. The low R-square may be contributed by the limited sample size. Owing to the time constraints, the respondents for this study is limited to 121 respondents. This is the limitation for this study.

Table 4: Regression analyses result between the innovativeness towards the export performance of SMEs

Independent Variable	R square (R^2)	Sig. F value	Beta Coefficients	t-value
Innovativeness	0.009	0.303	0.094	1.035

Dependent Variable: Export Performance

** significant at 0.01 level (2-tailed)

The results of the regression analyses for strategy types on export performance are shown in Table 5. The results showed that low cost strategy did not contribute significantly to the export performance of SMEs ($p=0.027>0.005$). For the regression analysis results of differentiation strategy types towards export performance, it is significant ($p=0.003<0.005$). It showed that there is a significant relationship between the differentiation strategy type and the export performance. This meant that, the SMEs which adopted different prices for products exported to different country have better performance. Differentiation strategy with different pricing which suit to the different export market will lead to a better export performance of SMEs. Therefore, SMEs should place the market prices according to the export markets to achieve better export performance.

On the other hand, the results showed that the niche strategy did not contribute significantly ($p=0.081>0.005$) to the export performance of SMEs. Among

three strategy types, the differentiation strategy has significant relationship with the export performance. The other two strategy types, namely, low cost strategy and niche strategy do not influence the performance of SMEs. It is therefore interpreted with the strategy types have partial relationship with the export performance of SMEs. However, the differentiation strategy contributed significantly to the export performance of SMEs. In this study, hypothesis 3 was accepted. This meant that, the SMEs which apply differentiation strategy, these SMEs obtain better export sales to overseas.

Table 5: Regression analyses result between the strategy types towards the export performance of SMEs

Independent Variable	R square (R ²)	Sig. F value	Beta Coefficients	t-value
Low cost strategy	0.041	0.027	0.202	2.246
Dependent Variable: Export Performance				
Independent Variable	R square (R ²)	Sig. F value	Beta Coefficients	t-value
Differentiation strategy	0.074	0.003**	0.272	3.081
Dependent Variable: Export Performance				
Independent Variable	R square (R ²)	Sig. F value	Beta Coefficients	t-value
Niche strategy	0.025	0.081	0.159	1.760
Dependent Variable: Export Performance				

** significant at 0.01 level (2-tailed)

Discussion and Conclusion

This study focuses on SMEs from the perspective of strategic management. The study attempted to examine the influence of strategic management variables on the export performances of SMEs. More specifically, the primary objective of the study was to examine empirically the influence of distinctive capabilities, innovativeness and the strategy types on the export performance of SMEs in the Malaysian manufacturing sector.

As shown in Table 3, Hypothesis 1 states that there is a significant relationship between distinctive capabilities and the performance of SMEs is rejected. These

findings appear not consistent with the study conducted by Stoner (1987). According to Stoner, most small firms recognised the need for building and developing distinctive capabilities as a competitive strategy. Besides Stoner (1987)' study, there are many previous researchers on distinctive capabilities. Hubbard *et al.* (1997) indicated that distinctive capabilities is a skill that an organization possesses that enables it to perform activities. According to Javidan (1998), the distinctive capabilities will influence the core competencies of the organization. Further, Ghosh *et al.* (2001) found that the key success factors and distinctive capabilities contributed to the performance of SMEs. Ghosh *et al.* (2001) measured distinctive capabilities from the aspects of management team, leaderships, correct strategic approach, marketing, develop and sustain capability and good customer and client relationship.

Although the study by Hitt and Ireland (1985) indicated that distinctive capabilities variables does influence the performance of the firm, this study does not congruent with the Hitt and Ireland (1985)'s study. This might be contributed by the Hitt and Ireland (1985)'s instrument which is developed in United States of America to measure distinctive capabilities of SMEs in Malaysia. Owing to the different environment in United States of America and Malaysia, it gives the different findings. Further, as indicated in the study by Ghosh *et al.* (2001) there were other aspects in measuring distinctive capabilities. On top of that, Chameeva (2006) also indicated that there are other competencies for enhancing advantages in SMEs to lead to better performance. These reasons needed to be taken as consideration. Therefore, it is recommended that more comprehensive studies is to be conducted on this distinctive capabilities variable to identify the reasons behind the contradictory findings.

For the results of innovativeness variables towards the export performance, the findings appear not to concur with the study conducted by Abbey and Dickson (1983). Abbey and Dickson (1983) concluded that the climate of innovate R&D units is characterized by rewards given in recognition of excellent of performance and this performance will indirectly influence the performance of the organization. Damanpour (1987) indicates that the importance of innovativeness in the firm has been rarely examined empirically. According to Damanpour and Evan (1984), innovativeness is more effective in helping organizations to maintain or improve their level of performance.

However, despites the above studies, as reported earlier, the recent study done by Lin and Chen (2007) shows that 80% of the surveyed firms applied technological innovation in the firms, and the technological innovation variable does not explaining the firms' performance. Therefore, it is recommended that further studies to give a broader view on this innovativeness variable.

As shown by Table 5, the findings appear congruent with Porter's (1980) study of the three generic strategy types (low cost, differentiation, and focus). Porter noted that the ability of firms to survive will depend upon their ability to adopt strategy types that can differentiate them from their competitors. Novel conclusions have emerged from the present study, that are different from previous researches. It has been concluded from previous studies that there is a significant relationship between the strategy types and the firms' performance, as highlighted in the study of Porter (1987). It was found in the present study that the differentiation strategy type had significant relationship towards the export performance of SMEs. Therefore, the SMEs should practiced differentiations strategy to suit to the different export market to obtain better export performance.

In the last 20 years or so, aspects of the distinctive capabilities of firms may have changed considerably. As a consequence, the distinctive capabilities may no longer relate significantly to the export performance of SMEs. The recent research by Lin and Chen (2007) found no significant relationship between innovativeness and firms' performance. Clear evidence for the operation of a time change factor is supported from the very different nature of the conclusions that were drawn from this latter study. Clearly, changes in the distinctive capabilities, innovativeness and strategy of SMEs with the passage of time provide an opportunity to undertake further research in this area, to clarify the dynamics of the change process.

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