



FACTORS OF SUSTAINABLE FIRM PERFORMANCE AND THE MEDIATING ROLE OF STRATEGIC OPPORTUNITY RECOGNITION: A CONCEPTUAL STUDY



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ABSTRACT

Article History

Received: 25 July 2018

Revised: 29 August 2018

Accepted: 3 October 2018

Published: 8 November 2018

Keywords

Strategic entrepreneurship
Exploration
Sustainable firm performance
Sustainability development
SMEs
Malaysia.

JEL Classification

L10; L26; Q01.

The significant role of Small and Medium Enterprises (SMEs) in economic development has been acknowledged and focused for a very long time. They dominate the business establishment around the world. The current challenging and volatile business landscape has called for greater scrutiny to identify survival toolkit for SMEs, given that SMEs are very much important to the dramatic economic changes. Thus, understanding practices that may damage business success is needed urgently. With this crucial and critical situation, it is the time now to identify an alternative approach to understand practices that lead to business success. The purpose of this study is to concentrate on the influence of strategic entrepreneurship (SE) which is manifested in exploration activities only that in-turn represented by strategic opportunity recognition construct, on sustainable SMEs performance in Malaysia. This paper is an attempt to address this challenge by developing a framework for the assessment of recognizing the important role of SE in efficiently contributing to the achievement of Sustainable Firm Performance.

Contribution/ Originality: This study contributes in the existing literature on organizational sustainability performance which was found to be limited, particularly by focusing on SMEs in context of Malaysia. It is hoped that this article will instigate research ideas among scholars paving way towards empirical examining of SMEs' sustainable performance and its drivers.

1. INTRODUCTION

The significant role of SMEs in all countries around the globe for economic development has been acknowledged and focused for a very long time, in which SMEs dominates the business establishment around the world (Rahman *et al.*, 2016). During the past decade, the terms "globalization", "liberalization" and

“internationalization” were the popular terms used in the economic field and received a great attention and acknowledgment by researchers around the world. A report from OECD (1997) on SMEs involved in globalization activities provide evidence that SMEs are internationalizing more rapidly compared to the past. Most of them are generating earnings in the global market more than their home countries (Chelliah *et al.*, 2010).

The major economic activities moving towards globalization and the system of distribution and production are continuing to evolve worldwide. The international trade connects the countries and creates new structure and new relationship which business decisions and actions in one part of the world can affect significantly other places. The effect of globalization trends will create the fast changing technological environment which enables the information processing and telecommunication possible to coordinate research, production operation and marketing around the world; thanks to the growth of global markets, increase competition and force government to adopt market oriented-policies, both internationally and domestically (Zulkifli-Muhammad *et al.*, 2009).

Most of the firms are small in every country, SMEs account for 93 per cent of enterprises in non-OECD countries and OECD countries micro firms and SMEs account for over 95 per cent. On average, 83 per cent of them are MSME and operate in the service sector including wholesale and retail. They also account for two-thirds of the total employment in developing and developed countries, but the contribution to GDP is lower, at around 35 per cent in developing countries and 50 per cent in developed countries. SMEs are less productive compared to large firms by 70 per cent (World Trade Report, 2016).

New SMEs consider very important factor to solve the challenges of job creation, equal sharing of income, sustainable economic growth and overall improvement of economic development (Fatoki, 2014). Poverty has become a major issue all over the world especially in the developing country (Hamdan *et al.*, 2012) and for those countries experiences high level of poverty and income inequality, SMEs was expected to be the critical solution to solve the issues (Fatoki, 2014).

Current dynamic business environment and fast changing technological trend force the companies to change their ways of doing business, be more innovative and constant adaption to stay competitive on market especially during economic crisis will increase number of bankruptcies (Shirokova and Ivvonen, 2016). Many past researchers have studied the success and failure factors of SMEs to gain competitive advantage. In order to gain competitive advantage in marketplace, SMEs must involve heavily in innovation but most SMEs were constrained due to smallness of the firms (Aziz and Samad, 2016).

Malaysia has recognized the significant contribution of SMEs to the country's economic development since 1960s and expected to transform towards developed country by year 2020. Malaysian government has given a lot of focus to SMEs development including putting in place policies and institutional framework to address development needs and, financial and technical support as well. Many public policies established by government to provide friendly environment for SMEs growth and success, increase competitive advantages globally and locally to enhance SMEs contribution to nation GDP.

There is abundance report in Malaysia show SMEs highly contributed in the economic development. There are three major SME sectors in Malaysia including Manufacturing, Agriculture and Service sectors (Rahman *et al.*, 2016). Malaysian SMEs have performing well for past one decade, with outperform growth and grew at annual rate of 7.1% versus 4.9% growth for the overall economy. The Government had started 139 SME development programmes in 2014 cost about RM5.1 billion which supported more than 500,000 SMEs across all sectors. SME GDP growth increased double-digit rate of 13.6% and the overall GDP rising significantly to 36% (2013: 33.5%) (SME Annual Report, 2014/2015).

Technology is fast changing the way of competition and strategy moving toward a 'new competitive landscape' in the twenty-first century. The new competitive landscape shows that firms exist in highly turbulent and often chaotic environments. In such an environment produce disorder, disequilibrium, and significant uncertainty, managers need to develop new tools, new concepts, new organizations, and new mind-sets in order to survive. It

presents new issues, new concepts, new problems and new challenges which refer to as a 'technological revolution.' Managers and government policy makers need to deal with major strategic discontinuities that are changing the way of competition; new tools and approaches are being needed. Most industries are affected by process of globalizing and advanced by new communications technologies, new economies in process equipment and logistical technology. This new competitive landscape is becoming very important and obvious (Bettis and Hitt, 1995).

Nowadays the volatile business environment and fast technological changes force the companies to follow new ways of conducting business, including constant update and align with frequent changes and innovations in order to stay competitive on the market. In the event of economic crisis may critically affect most of the SMEs, decrease the development rate and increase the number of bankruptcies (Shirokova and Ivonen, 2016). No organization is able to escape from huge impact of these dramatic changes.

The current challenging and volatile business landscape has called for greater scrutiny to identify survival toolkit for SMEs, given that SMEs are very much important to the dramatic economic changes. Therefore, understanding practices that may damage business success is needed urgently. With this crucial and critical situation, it is the time now to identify an alternative approach to understand practices that lead to business success (Ahmad and Seet, 2009). With combination of brilliant strategy management and entrepreneurship it may able to assist the firm to attain sustainable firm performance.

Previous study shows that few important reasons of majority SME failures, apart from the financial constraints, management skills and marketing issues also hinders them from surviving and growing. There are too many issues that have been discussed in the SME literature with regards to the challenges and business difficulties and there is a limited study that organizes SME challenges according to their severity towards business (Rahman *et al.*, 2016). In case of Malaysia, there is no reliable figure published, so for the estimated failure rate of SMEs is approximately of 60 percent which is three times higher than SMEs in Australia's (Ahmad and Seet, 2009). It reflects that SMEs in Malaysia are facing serious issues and plenty of obstacles to stay competitive advantage in the market place locally or international (Khaliq *et al.*, 2011).

The main focus of entrepreneurship is about opportunity seeking behaviour whereas strategic management focus is on competitive advantage seeking behaviour. Strategic entrepreneurship is the integration of entrepreneurial (i.e., opportunity-seeking actions) and strategic (i.e., advantage-seeking actions) perspectives to design and implement entrepreneurial strategies that create wealth (Hitt *et al.*, 2001). Thus, strategic entrepreneurship is entrepreneurial action that is taken with a strategic perspective (Hitt *et al.*, 2002).

The focus of this study is on SE as a firm level phenomenon. SE signifies an achievable answer to solve the issues of fast changing competitive landscape in order for SMEs to remain competitive and sustaining efficiency while continuously follow the rapid changes in the market. With the aim of companies develop and exploit current competitive advantages while supporting entrepreneurial actions that exploit opportunities that will help create competitive advantages for the firm in the future, it is very critical for SMEs to comprehend the Strategic Entrepreneurship and its impact on sustainable firm performance (Hitt *et al.*, 2002).

Therefore, this study is to concentrate on the influence of SE which is manifested in exploration activities only that in-turn represented by strategic opportunity recognition construct, on sustainable SMEs performance in Malaysia. SMEs are chosen in the study due to they dominate the intact business establishments in Malaysia more than 99 per cent but only contributed around 36 per cent of countries GDP (SME Annual Report, 2014/2015).

Theoretically, it is apparent, that opportunity recognition is essential to achieving SMEs performance (Sambasivan *et al.*, 2009) but previous studies have given less research attention to these prominent factors, namely prior knowledge, social capital, environmental conditions, entrepreneurial alertness and opportunity recognition in their studies, it is rarely portrait as one of the vital resources of the SMEs, and very few studies exist that have linked these factors to SMEs performance (George *et al.*, 2016). Therefore, the study fills in the missing links in strategic opportunity recognition and sustainable SMEs performance research by proposing a research framework

that could adequately address the issues of generating and improving SMEs performance capable of providing the required employment, growth in GDP, export performance and provide economic growth and development at large ((Pulka *et al.*, 2018) with sustainability perspective. Therefore, the study contributes to the body of knowledge by providing a framework on the relationships between prior knowledge, social capital, environmental conditions, entrepreneurial alertness, and sustainable SMEs performance, and moderating role of strategic opportunity recognition.

Consequently, the primary objective of this study is to develop the scholarly conceptual framework for the understanding of how prior knowledge, social capital, environmental conditions, entrepreneurial alertness impact on the sustainable SMEs performance and also to examine the mediating effect of strategic opportunity recognition on the relationships between prior knowledge, social capital, environmental conditions, entrepreneurial alertness on the sustainable SMEs performance. While the arrangement of the rest of this paper is as follows; literature review on sustainable SMEs performance, prior knowledge, social capital, environmental conditions, entrepreneurial alertness and strategic opportunity recognition. The discussion is supported by review of Resource-Based View (RBV) theory, conceptual framework for the study and conclusion.

2. LITERATURE REVIEW

2.1. Sustainable SMEs Performance

Chan *et al.* (2017) argue that firm performance will show how effectively an organization operates their business and it is the key measurement used to gauge the business success or survival of an organization. Firm performance can be measured by multiple ways, i.e. financial performance (Eshima and Anderson, 2017) firm operational excellence, revenue growth, customer relationships (Chan *et al.*, 2017) annual employment growth, real annual sales growth and annual productivity growth (Williams *et al.*, 2017). According to Eshima and Anderson (2017) in order to better understand the growth of firm performance, it must take into consideration by expanding firm boundaries to new entrepreneurial opportunities which improve the firm's ability to change its understanding of market expectation. They also argue that by increase in the firm's resource base which will increase in the firm's total assets. In order to solve the problems occurred by traditional (accounting-based) performance measures, the performance measurement framework was developed and among the most popular one is the Balanced Scorecard by Kaplan and Norton (1992;1996). Therefore, it was used in many organizations as core management tool to guide firm business strategy and used by top management team to translate intangible assets into tangible outcomes or financial (Ogunsiji and Ladanu, 2017). With the current challenging and volatile business landscape, SMEs need to fully utilize whatever resources they have to optimum capability in order to gain and maintain better competitive advantage in the market place with highest performance that can support the business sustainability.

2.2. Strategic Entrepreneurship (SE)

Hitt *et al.* (2001;2002) defines entrepreneurship as the identification and exploitation of previously unexploited opportunities. The shared goal and purpose of entrepreneurship and strategic management is to create wealth. The main outcomes from creation (entrepreneurship) and exploiting current advantages while simultaneously exploring new ones (strategic management) can be tangible, such as increase firm wealth, and intangible, such as improve firm's intellectual and social capital. Consequently, the entrepreneurial and strategic perspectives should be integrated to examine entrepreneurial strategies that create wealth and they called this approach as SE. They also concluded that SE is entrepreneurial action with a strategic perspective i.e. the integration of entrepreneurial (opportunity-seeking behaviour) and strategic (advantage-seeking) perspectives in developing and taking actions to create wealth. Strategic actions are those companies who develop and exploit current competitive advantages and in the meantime supporting entrepreneurial actions that exploit opportunities which will help the firm to create competitive advantages in the future.

Rensburg (2013) argue that almost all the researchers in the SE borrows opportunity-seeking behaviour (exploration) from entrepreneurship and combines it with advantage-seeking behaviour (exploitation) from strategic management and can be deployed into small-medium sized enterprises and large corporations. While Mathews (2010) define SE as business activity that drives the economy with new directions through recombination of resources, activities and routines by firms, and the entrepreneur as the economic agent who lacks of resources (but knows where to find them), who able to recognise the opportunities that can be turned into profit, and exploit these opportunities through resource mobilization and activation in order to gain profit from it. Kyrgidou and Hughes (2010) define SE as a process that enable firm efforts to identify opportunities with the highest potential to lead to value creation, through the entrepreneurial component and then to exploit them through measured strategic actions, based on their resource base. They propose a reinforced and further developed model in relation to the eight consolidated components shown in Figure 1, i.e. resource management, opportunity identification, growth, innovation, acceptance of risk, vision, flexibility and dynamic capability. Therefore, a firm's ability to continually improve and fully utilise current resources and create new ones is important to maintaining competitive advantages and the entrepreneurial exploitation of opportunities over time. Therefore, the framework for this study consists of strategic opportunity recognition and the influential factors: prior knowledge, social capital, entrepreneurial environment and entrepreneurial alertness.



Figure-1. Strategic Entrepreneurship Model

Source: Adapted from Kyrgidou and Hughes (2010)

2.3. Prior Knowledge

Prior knowledge has been identified as an important factor in opportunity identification in entrepreneurship research (Venkataraman, 1997; Shane, 2000; Baron, 2006). Shane (2000) argues that people will have different stocks of information due to their life experience, and as a result some people are more likely able to recognize certain opportunity than others. According to Shane (2000) entrepreneurial knowledge can be defined as “prior knowledge of markets, prior knowledge of ways to serve markets, and prior knowledge of customer problems”. Literature on opportunity recognition by entrepreneurs indicates that knowledge and information acquired through prior work experience will improve an individual's ability to identify opportunities (Shane, 2000; Shepherd and DeTienne, 2005). Tacit knowledge, especially the one that is acquired through work experience over certain years, also can improve opportunity identification and leads to the discovery of a new opportunity, a new market, or a new solution to customer's problems (Ardichvili *et al.*, 2003). Park *et al.* (2017) argue that people who obtained

knowledge from a social network and prior experience will have a better opportunity to get into new market compared to those who not. Knowledge gain from business experience and operation management will improve entrepreneur alertness and enable them to identify new opportunity. Tang (2010) argues that prior knowledge about markets enables people to understand demand conditions, therefore facilitating opportunity discovery. Prior knowledge of how to serve markets helps to identify opportunities because people know the rules and operations in the markets. Finally, prior knowledge of customer problems or needs would stimulate opportunity identification because such knowledge helps trigger a new product or service to solve customer problems or to satisfy their unmet needs. Prior knowledge is one of the vital resources needed by the SMEs to generate and sustain competitive advantage and better performance. Hence, it is hypothesised in the study that:

H: Prior knowledge has a significant positive effect on Sustainable SMEs performance.

2.4. Social Capital

Entrepreneurs need information and resources that may contribute to the richness of their store of knowledge in the opportunity recognition process, which can be attained by using social capital (Shane, 2000; Ardichvili *et al.*, 2003; Baron, 2006). Tang (2010) argues that social capital can provides networks and able to help entrepreneurs to overcome institutional constraint by supporting entrepreneurs' obtained important information and knowledge which will enhance and contribute to opportunity recognition. Hernández-Carrión *et al.* (2017) stressed that social capital is a source of sustainable competitive advantage and it is valuable, rare or scarce, inimitable, and a non-substitutable resource. Due to each individual has access to different social networks and own different kinds of relationships within these networks and this are the inimitable aspect of social capital. They also argue that social capital resources contribute to improving small firms' economic performance in terms of sales growth, market share, and success in launching new products or services. Therefore, given the above, it is hypothesised that:

H: Social capital has a significant positive effect on Sustainable SMEs Performance.

2.5. Entrepreneurial Environment

George *et al.* (2016) argue that environmental factors can highly influence for economic growth, social and political contexts, geographic location, cultural values and also affect entrepreneur's opportunity identification process. Technological, political, social, regulatory, and other types of change offer a continuous supply of new information about different ways to use resources to enhance wealth. By making it possible to transform resources into a more valuable form, the new information alters the value of resources and, therefore, the resources' proper equilibrium price which help in the processes of opportunity recognition (Schumpeter, 1934; Shane and Venkataraman, 2000). Tang (2008) argues that four dimensions of environmental factors are critical to opportunity recognition including governmental, socio-cultural, financial and non-financial variations in the environment in which entrepreneurs recognize and exploit opportunities. This is critical because variations in socio-economic, cultural, and governmental conditions can influence the way individuals evaluate opportunities and affects their judgement to lookout for new business opportunities and sustain competitive advantage. Tang (2010) argues that entrepreneurial environment exposes entrepreneurs to and enhances their realization of different stocks of knowledge. When the knowledge accumulated through individuals' idiosyncratic experiences is formally acknowledged, the capability to spot opportunities will be heightened. Therefore, given the above, it is hypothesised that:

H: Entrepreneurial environment has a significant positive effect on Sustainable SMEs Performance.

2.6. Entrepreneurial Alertness

George *et al.* (2016) define alertness as the capacity to possess keen insights into identifying entrepreneurial opportunities. Kirzner (1973) introduces the theory of entrepreneurial alertness, which helps improve our

understanding of opportunity processes. Tang (2008) argues that entrepreneurs have special sense of “smelling” opportunities and have the quality of lookout for unnoticed features of the environment and constantly seeking new ideas which they may never be conscious of their alertness, or aware at their disposal. Therefore, in order to increase the chance for the opportunity to be recognized, entrepreneurs need to be exposed to a friendly environment that will “switch on” their alertness. George *et al.* (2016) also argue that many scholars have agreed that if a person’s level of alertness is high, opportunities can be identified even without actively searching for them or by simply observing the phenomena. Tang (2008) found that entrepreneurs with higher alertness are more committed to their new ventures, behaviourally, physically and work affectively towards success. Thus, entrepreneurs not only need to identify opportunity, but grasp opportunity to success. Only then they can remain with their businesses regardless of the high risks, and uncertainty associated with new venture creation in order to sustain competitive advantage. Therefore, given the above, it is hypothesised that:

H₁: Entrepreneurial alertness has a significant positive effect on Sustainable SMEs Performance.

2.7. Strategic Opportunity Recognition

George *et al.* (2016) state that for the last three decades, research studies investigating how individuals recognize entrepreneurial opportunities have advanced rapidly and have become a key topic in the modern entrepreneurship literature. They classify existing contributions into six influential factors: prior knowledge, social capital, cognition/personality traits, environmental conditions, alertness, and systematic search. According to Shane and Venkataraman (2000) even though an entrepreneurial opportunity may exist, it can only be successfully exploited, if an individual recognizes the existence of the opportunity and its value. George *et al.* (2016) argue that two major types of entrepreneurial opportunity exist in the literature i.e. (Schumpeter, 1934) viewed opportunities as central to new resource combinations and considered that novel combinations could not only take the form of products or services, but could also be discovering new methods for production, new ways to organize a market, or new raw materials. Kirzner (1973) however, pinpointed that neither market demand nor resources might exist in their final form, but must be invented. Furthermore, he emphasized that opportunities are at the core of market imperfections with the potential to create economic returns. Therefore, regardless of the perspectives taken regarding opportunities, the literature acknowledges that entrepreneurial opportunities involve diverse processes for creating value. Sambasivan *et al.* (2009) has theoretically and empirically justified the role of opportunity recognition as a mediating variable with positive impact to firm performance and based on the output, the better the opportunity recognition of the entrepreneur, the better is the success of the venture in terms of sales volume and sales growth. Hence, in line with the Sambasivan *et al.* (2009) it is hypothesised that:

H₂: Strategic opportunity recognition has a significant mediating effect on the relationship between prior knowledge and sustainable SMEs performance.

H₃: Strategic opportunity recognition has a significant mediating effect of on the relationship between social capital and sustainable SMEs performance.

H₄: Strategic opportunity recognition has a significant mediating effect on the relationship between entrepreneurial environment and sustainable SMEs performance.

H₅: Strategic opportunity recognition has a significant mediating effect on the relationship between entrepreneurial alertness and sustainable SMEs performance.

3. CONCEPTUAL FRAMEWORK AND UNDERPINNING THEORY FOR THE STUDY

The conceptual framework of the study is based on resource based view as expounded by Alvarez and Busenitz (2001) which is known as resource based theory (RBV). Resource heterogeneity is the most basic condition of resource-based theory and it assumes at least some resource bundles and capabilities underlying production are heterogeneous across firm, but not all resources have the potential of sustained competitive advantages. In order to

have this potential, the firm resource must be valuable, rare, inimitable, and non-substitutable (Barney, 1991). Resource-based theory suggests that heterogeneity is necessary but not sufficient for a sustainable advantage. For example, a firm can have heterogeneous assets, but not the other conditions suggested by resource-based theory, and those assets will only generate a short-term advantage until they are imitated (Alvarez and Busenitz, 2001). Grant (1991) argued that the resources and capabilities of a firm are used to generate and frame its strategy and they are primary source of the firm's profitability. The key to RBV approach is to understand the relationship between resources, capabilities, competitive advantage and profitability which in particularly to understand the mechanism of competitive advantage that can be sustained over period of time. Alvarez and Busenitz (2001) stated that while the importance of resource heterogeneity among firms has been acknowledged, strategists have given scant attention to the process by which these resources are discovered, turned from inputs into heterogeneous outputs, and exploited to extract greater profits. Thus, they argue that entrepreneurship is about cognition, discovery, pursuing market opportunities, and coordinating knowledge that lead to heterogeneous outputs. Therefore, prior knowledge, social capital, entrepreneurial environment and entrepreneurial alertness serve as the independent variables, sustainable SMEs performance is the dependent variable and strategic opportunity recognition is the mediating variable in line with Sambasivan *et al.* (2009).

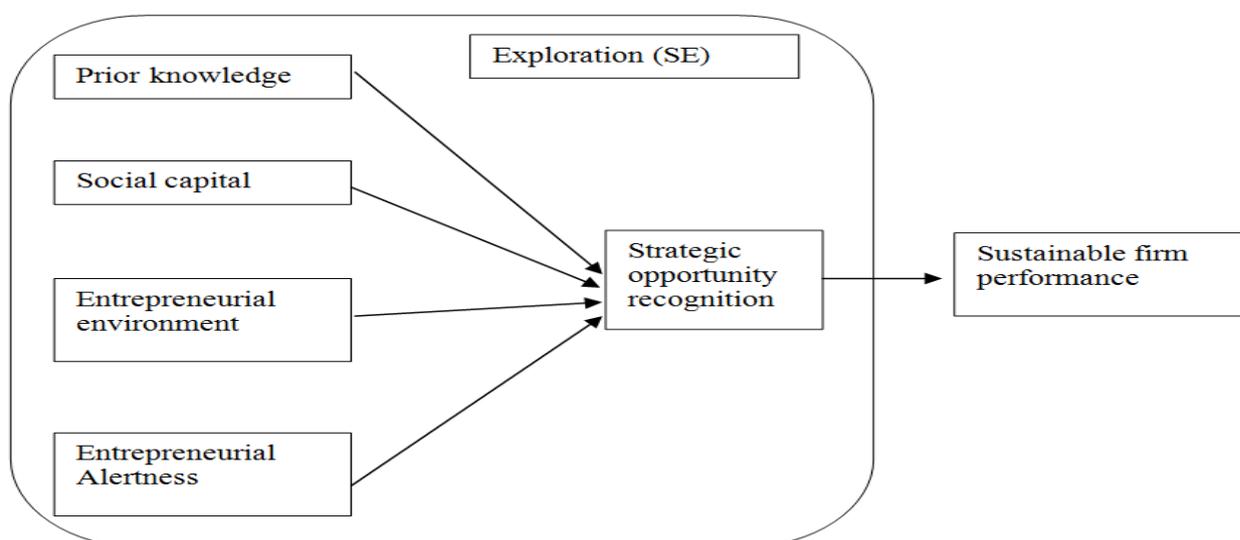


Figure-2. The proposed Sustainable Firm Performance Model for this study

Source The model was developed by the researchers for this study

4. CONCLUSION

The primary objective of this study is to propose a new conceptual framework for determining exploration SE and overall performance of SMEs. The proposed framework discusses the proposed mediating effects of strategic opportunity recognition on the relationship prior knowledge, social capital, entrepreneurial environment, entrepreneurial alertness and SMEs performance. Similarly, the proposed framework is presented as a strategy to be used in linking the inadequate academic explanation in the existing literature on the relationships between prior knowledge, social capital, entrepreneurial environment, entrepreneurial alertness and SMEs performance and mediating role of strategic opportunity recognition. Hence this study serves as basis for future research on exploration SE-SMEs performance. There are number of limitations to this study. Firstly, this proposed conceptual framework needs empirical studies for its validation. It is suggested that future studies should consider other contingent variable i.e. exploitation as mediator to expand the SE – SMEs performance literature.

Funding: This study received no specific financial support.

Competing Interests: The authors declare that they have no competing interests.

Contributors/Acknowledgement: All authors contributed equally to the conception and design of the study.

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