

## Mediating Role of Competitive Advantage on the Relationship Between Entrepreneurial Orientation and the Performance of Small and Medium Enterprises

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**Abstract:** In recent years, the performance of Small and Medium Enterprises (SMEs) is generating a vast amount of argument among practitioners, researchers, educators and policymakers. Therefore, this study examined the influence of entrepreneurial orientation and competitive advantage on SMEs performance in Nigeria. It also examined whether competitive advantage mediates the relation between entrepreneurial orientation and performance of SMEs. Self-administered questionnaires were employed to collect data from the total of 283 respondents from SMEs in Kano, North Western Nigeria. This study used Partial Least Squares Structural Equation Modeling for data analysis and hypotheses testing. The results indicates significance and positive relationship between entrepreneurial orientation and SMEs performance. Similarly, the result indicate a significance positive relationship between competitive advantage and performance. Entrepreneur's orientations and competitive advantage are important drivers of firm performance. The findings further shown as expected, competitive advantage mediates the relationship between entrepreneurial orientation and the performance of SMEs. As implication, the study contributes to resource-based view theory from Nigerian context and offers some suggestions to policymakers.

**Key words:** Entrepreneurial orientation, competitive advantage, SMEs performance, Nigeria

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### INTRODUCTION

The performance of Small and Medium Enterprises (SMEs) is generating a vast amount of argument among practitioners, researchers, educators and policy makers. The characteristics and determinants of the performance of SMEs have been and always will be a focus of discussion and importance (McKelvie and Wiklund 2010). Due to the unique constraints and limitations faced by SMEs such as having a limited number of employees, insufficient financial resources, a lack of educational background and experience and a lack of managerial expertise, among other limiting factors (Aris, 2007), efforts are continuously being made to understand how the performance of SMEs could be developed and further enhanced. These efforts are important since this sector of the economy is recognized as one of the crucial engines of growth for a country's economy (Kassim and Sulaiman, 2011). SMEs provide employment to teeming population this is because of their level of creativity/innovation and utilization of local raw materials that do not need high level of technology process. Osotimehin *et al.* (2012) argued that SMEs are very vital engine for economic

development. They contribute significantly to the economic and social improvement of the nation-state. However, SMEs contribute <46% to the GDP in Nigeria which show low performance of the sector.

There are lots of empirical studies on the determinants of SMEs Performance. Some of the factors studied include social network, competitive advantage, innovation and entrepreneurial orientation (Covin *et al.*, 2006; Lucky *et al.*, 2011; Wiklund and Shepherd, 2003; Martinette and Lesson, 2012; Witt, 2004; Bueno and Ordonez, 2004). The main focus of this research is to investigate the impact on performance of SMEs in Nigeria from the perspectives of Entrepreneurial Orientation (EO) and Competitive Advantage (CA). Nevertheless, despite these remarkable studies, less attention has been paid to the mediating effects of competitive advantage on SME performance. Even if any, the findings of such studies are unconvincing, signifying a potential mediator variable (Baron and Kenny, 1986).

Therefore, the objective of this study is to examine the relationship entrepreneurial orientation and the competitive advantage and SMEs Performance. The study will also examine whether competitive advantage mediates

the relation between entrepreneurial orientation and performance of SMEs. The study is organized as follows: section two provides the literature review and the research framework. section three; research methods, measurement of variables, section four; result and discussion of the study are presented. In section five, the managerial implications of the study and the recommendations for future research are discussed.

### **Literature review**

**Business performance:** Performance is among the most significant dependent variable for researchers concerned with almost all areas of management (Richards, 2008) for the reason that it explains how well an organization is doing (Obiwuru *et al.*, 2011). In all aspects of strategic management and management field, the term performance is not new (Aminu and Shariff, 2015). For example, performance assessment or evaluation, performance management and performance measurement are frequently used in various field of business and or management science. Nevertheless, there is no one best accepted definition of performance, it depends on the area and specialties of the person defining it. SME performance has been studied by a number of researchers in several literature and they concentrated mostly on examining causes of performance, in which relatively many variables were recognized as the factors influencing SMEs performance. Organization performance is defined as the ability of a firm to realize its objectives such as high profits, good financial outcomes, good quality products, a large market share and long-term survival, using relevant strategies for action. It is an indicator of how well a firm realizes its objectives (Ho, 2008).

Richards (2008) defined organizational performance as encompassing three specific areas of organization outcomes: financial performance, product market performance and shareholder return. Based on the study by Lusthaus *et al.* (2002) business performance can be defined in terms of the following elements: effectiveness refers to the ability of the organization to attain its objectives Vis-a-vis those competitors in the same market, e.g., sales growth and market share. Efficiency: accuracy, how economically the organization can turn resources/inputs into results, financial viability: ability to nurture required funds and relevance: adaptive to the stakeholders and its environment. Tangen (2003) argue that organizational performance measures as metrics selected to measure the efficiency and/or effectiveness of an accomplishment/achievement by the business organization. Business performance can be measured

quantitatively or qualitatively (Augustine *et al.*, 2012). In other words, it can be measured either by looking at economic variables or non-economic variables.

Several studies on business performance use a number of organizational resources to measure performance of SME's. Some of the factors include social capital, short term debt, total quality management, IT usage, learning orientation, social network, innovation and Entrepreneurial orientation (Covin *et al.*, 2006; Lucky *et al.*, 2011; Witt, 2004; Bueno, 2004; Fornoni *et al.*, 2012; Al-Swidi and Mahmood, 2012; Augustine *et al.*, 2012).

Nevertheless, studies have revealed that entrepreneurial orientation can influence the performance of SME's (Fatoki, 2011; Lechner and Gudmundsson, 2014; Mutlu and Aksoy, 2014; Polat and Mutlu, 2012; Tang and Tang, 2012).

A number of studies used competitive advantage in investigating firm performance (Tovstiga and Tulugurova, 2009; Mahmood and Hanafi, 2013; Martinette and Leeson, 2012). In addition, since SMEs are not operating in a vacuum, an encouraging business environment and healthy overall economic situation as a whole are good predictors of performance (Huang and Brown, 1999). Smedan argued that harsh business conditions and other environmental factors are other issues affecting SME development and performance. However, to ensure the content validity and internal consistency of the measures, there is need to conduct the reliability and validity test of the construct in different environments, economies and context at large before conducting the main survey.

**Entrepreneurial orientation:** Entrepreneurship has long been often linked with firms pursuing to increase competitive position (Covin and Slevin, 1986; Covin and Lumpkin, 2011; Miller, 2011).

According to the idea introduced by Schumpeter (1934) entrepreneurship as a concept is characterized by strategic orientation and innovative behavior in pursuit of profitability and growth (Carland *et al.*, 1988) and the process also comprises of merging resources for value creation in an organization (Tan, 2007). Others have defined entrepreneurship as the process of creating new venture, new entry and taking advantage of opportunities by maximizing resources in ways which have impacts on the market (Lumpkin and Dess, 1996; Wiklund, 1999).

However, empirical studies shows that firm with better EO perform better, entrepreneurial characteristics found to have positive influence on SMEs performance (Shehu and Mahmood, 2014). Similarly, entrepreneurial

skills improve better access to resources including financial resources (Mohammed and Nzelibe, 2014). Based on this premise it is expected that EO can improve SME performance. Thus, this study suggests that:

- H<sub>1</sub>: Entrepreneurial orientation will be positively related to SMEs performance

**Competitive advantage:** Tovstiga and Tulugurova (2009), confirm that the firm’s internal resource base is a determining factor of competitive advantage in small and medium firms. A firm uses its unique resources to create offerings that have superior value to customers. Additionally, as important firm resources CA can improve firm performance. Wiklund and Shepherd (2003) report that competitive advantage influence firm performance. This can also be seen by Jeen *et al.* (2010) and Martinette and Leeson (2012) that there is positive link between competitive advantage and SMEs performance. Furthermore, Lopez-Gamero *et al.* (2009) conducted a study on the relationship between environmental variables and firm performance with Competitive advantage and firm resources as mediator variables. The findings shows that a firm’s resources and competitive advantage act as mediator variables between environmental protection and financial performance relationship.

Based on this premise it is expected that competitive advantage can improve SMEs performance and also, Competitive advantage can serve as mediating variable between entrepreneurial orientation and SME performance. Thus, this study suggests that:

- H<sub>2</sub>: Competitive advantage will be positively related to SMEs performance
- H<sub>3</sub>: competitive advantage mediates the relationship between entrepreneurial orientation and SMEs performance

In this study, we use Resource- Based view (RBV) with a major emphasis on how organizational resources develop and affect its performance (Kamyabi and Devi,

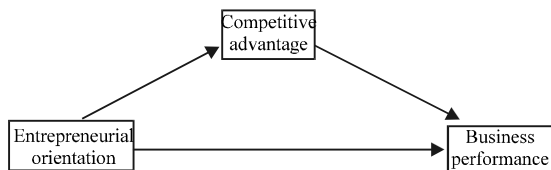


Fig 1: Research framework

2012). The RBV also encourage the attainment of SME resources, there by linking external resources with performance.

**MATERIALS AND METHODS**

**Data and samples:** Data collected from the sample of 283 small and medium enterprises in Kano North Western Nigeria. The sample of the study cover different types of SMEs in Kano metropolis. We decided to choose Kano because it have a large number of SME’s in the whole Northern part of Nigeria and also second to the Lagos state in the whole country. Self-administered questionnaires were distributed personally to the SMEs in different location. Before the survey was administered, the managers/owners of the SMEs were in the beginning explain about the objectives of research, and we also notified them that participation in the current study is voluntary. The effects of Common Method Variance (CMV) was reduce through the adoption of numerous procedural remedies as recommended by Podsakoff and Organ (1986). In order to decrease evaluation apprehension, all participants were well educated that there is no right or wrong answers to questions; there answers will be treated confidentially; it takes only 9-16 min to fill in all questions in the questionnaire and also their answers to the questions would be combined in such a way that none of them ca be identified.

**Measurements:** Based on the recommendation by Churchill, we adopted the measurements from previous research to use in the present research context. SME’s performance items were adapted from (Suliyanto and Rahab, 2012, Vorhies and Morgan 2003), EO will be based on the work of Idar and Mahmood (2011), which is rooted from the research by Covin and Slevin (1986) and CA is adopted from the research by Ramaswami and coauthors. We requested participants to point out their answers on a 5-point scale, ranging from “1” “strongly disagree” to “5” “strongly agree” on all items under study. Lastly, in order to improve scale items, all questions in the study were transcribed in a simple, specific and concise language in both English and Hausa.

**Data analysis:** Partial Least Squares-Structural Equation Modeling (PLS-SEM) was adopted for this study because it is well enhanced to be used as a research tool in strategic management, marketing and other social (Hair *et al.*, 2011, 2013a).

**Descriptive analysis of study sample:** Out of 283 participants, 30% were owners of the business, 47% are at different categories of Managers and 23% are Owners/Managers of the business. Also, the majority of the participants in the study that is 244 (79%) were males whereas the remaining 59, representing 21% were females. Regarding the educational level, those with Non-formal education constituted 63 respondent which represent 22% of the respondent, Primary education constitute 28% of the respondent, secondary education constituted 81 responses, representing 29% of the responses, Certificate/diploma/NCE constituted 36 responses representing 13% of the respondents, followed by Graduates with 12 responses, representing 4% and finally are those with postgraduate experience amounting to 12 responses representing only 4% of the total response. This pointed out clearly that the majority of SME owner managers in Kano are the holders of secondary school certificates followed by those with non-formal education.

For business activities, manufacturing/manufacturing related activities had 36%; services/ICT 25%; Public limited with 20%; Cooperative societies with 16% and Others with 3%. It was discovered that the sales turnover of the respondents is N50, 000 or less represent 11% of the respondents; above N50, 000<N200, 000 are 16%; (1million naira is equivalent to USD 6,250); N200, 000<1,000,000 are 24%; 1<10 million naira are 38%; above 10<25 million are 11%. The last range. This perhaps indicates that the businesses are small in nature. With regards to the number of employees in the business, the descriptive statistics reveal that the respondents with less than 5 employees was 17%, followed by 5-19 employees with 54%, 20-50 employees with 51% and lastly, 50-150 and 150 and above employees have 4% each. It was also revealed that majority of the business are in partnership in nature with 51% of the total respondent, followed by sole proprietorship and private limited with 27 and 22%, respectively.

**RESULTS AND DISCUSSION**

**Assessment of measurement model:** Before the major analysis, a number of assumptions of linearity, normality, and multicollinearity were checked (Hair *et al.*, 2010; Tabachnick and Fidell, 2007). Also, common method bias was evaluated with Harman’s single factor test. After these assumptions remained satisfied, we apply Partial Least Square (PLS) path modeling via Smart PLS 2.0 M3 software (Ringle *et al.*, 2012).

Additionally, reliability and validity are the two main criteria used in PLS-SEM analysis to evaluate the outer model (Hair *et al.*, 2013; Hulland, 1999; Ramayah *et al.*, 2011). The reliability is assessed using composite

Table 1: Cross loadings

Latent variables	Items	Business performance	Competitive advantage	Entrepreneurial orientation
SMEs performance	PER01	0.7254	0.3327	0.3476
	PER02	0.3635	0.7597	0.2665
	PER03	0.6515	0.2677	0.2597
	PER04	0.7722	0.3075	0.3312
	PER05	0.7128	0.2932	0.3166
Competitive advantage	CA03	0.2936	0.7031	0.4851
	CA04	0.2489	0.7003	0.4347
	CA05	0.2697	0.7825	0.4926
	CA06	0.3523	0.7705	0.4745
	CA07	0.2689	0.7346	0.4768
	CA12	0.3249	0.7038	0.5517
	EO2	0.2833	0.4821	0.6458
Entrepreneurial orientation	EO4	0.3364	0.3961	0.739
	EO5	0.3852	0.5133	0.7809
	EO6	0.2885	0.5626	0.742

Table 2: Reliability and validity of constructs

Latent variables	AVE	Composite reliability	Cronbach’s alpha
Business performance	0.5264	0.8471	0.7744
Competitive advantage	0.5376	0.8744	0.828
Entrepreneurial orientation	0.5309	0.8184	0.7056

Table 3: Latent variable construct

Latent variables	1	2	3
Business performance	0.725		
Competitive advantage	0.405	0.733	
Entrepreneurial orientation	0.449	0.665	0.728

Reliability (CR) whereas validity is evaluated using convergent validity Average Variance Extracted (AVE) and discriminant validity via Fornell-Larcker criterion and predictors outer loadings.

In view of that, the Table 1 and Fig. 2 shows that the CR value in this study is between 0.81 and 0.87, this show adequate internal consistency (Nunnally and Bernstein, 1994). Furthermore, all CR values exceeded the recommended threshold value of 0.70 (Hair *et al.*, 2013a, b; Henseler *et al.*, 2009).

Afterward is convergent validity as shown in Table 2 above all values exceed the threshold of 0.5 and this shows that convergent validity of the measurement (Hair *et al.*, 2013a, b). Lastly, we used two popular for evaluating the constructs’ discriminant validity. This consist of examination of cross loadings and Fornell and Larcker (1981) criterion (Hair *et al.*, 2013a, b). Table 3 indicates that separately construct’s AVE square root is greater than its correlation with all other constructs. Additionally, it was discovered that no indicator loaded higher on any contrasting construct (Hair *et al.*, 2013a, b; Henseler *et al.*, 2009).

**Structural model:** Following the measurement model and based on satisfactory result, the next stage is to assess the structural model. Initially, the structural model

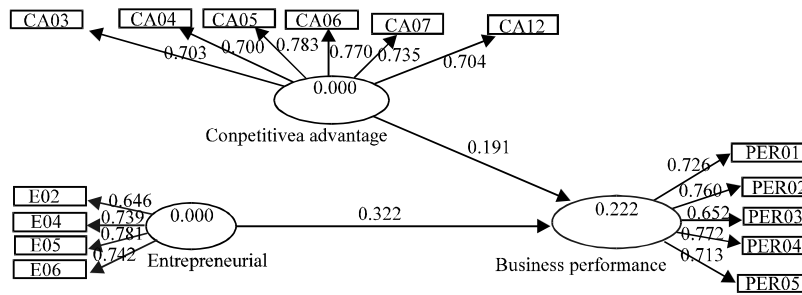


Fig. 2: Measurement model

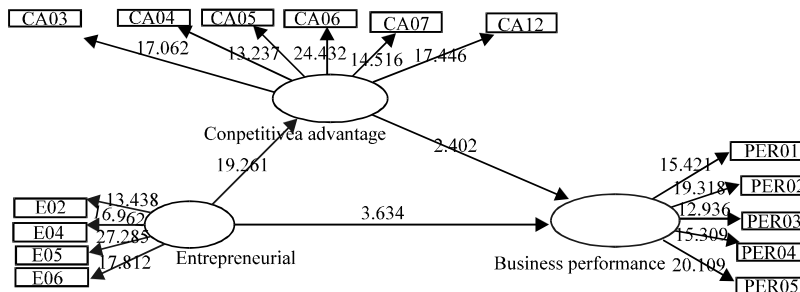


Fig. 3: Results of the structural model analysis

Table 4: Path coefficients and hypothesis testing

Hypotheses	Relationship	Beta	SE	t-stats	p-value	Findings
H1	CA -> Business performance	0.191	0.077	2.475	0.01	Supported
H2	EO -> Business performance	0.321	0.081	3.963	0.00	Supported
H3	EO->EO*CA->Business performance	0.129	0.05	2.349	0.01	Supported

relationships were measured using PLS-SEM bootstrapping for the significance of the correlation. The number of cases used was 5000 sample for bootstrapping procedure (Hair *et al.*, 2011, 2010, 2013a, b; Henseler *et al.*, 2009). The result in Fig. 3 and Table 4 shows the results of relationship between the exogenous variables and endogenous variable of the PLS-SEM analysis.

Precisely, the outcome of the structural model indicates that there is significant positive relationship between entrepreneurial orientation and SMEs performance ( $\alpha = 0.3217$ ,  $t = 3.9637$ ,  $p = 0.00$ ). Therefore, Hypotheses one remained strongly supported. This result is consistent with Shehu and Mahmood (2014) who stated a significant and positive relationship between entrepreneurial orientation and Organizational performance. Equally, Hypotheses 2 predicted that Competitive advantage has a significant positive relationship with SMEs performance. Result show CA affected SMEs performance positively ( $\alpha = 0.1914$ ,  $t = 2.4755$ ,  $p = 0.00$ ). This result is in line with Martinette and Leeson (2012) who reported a

significant and positive relationship between competitive advantage and business performance. Thus,  $H_1$  and  $H_2$  are supported.

**Testing mediating effect:** To test for the mediation effect of the competitive advantage, we follow all the mediation procedures and found that we satisfied the condition of mediation recommended by (Baron and Kenny, 1986). Therefore, Hypothesis 3 predicted that competitive advantage would mediate the relationship between entrepreneurial orientation and SMEs performance. As shown in Table 4, there was a significant interaction effect between entrepreneurial orientation and SMEs performance ( $\alpha = 0.12963$ ,  $t = 2.34921$ ,  $p = 0.00$ ). The result shows that competitive advantage mediate the relationship between entrepreneurial orientation and SMEs performance. In testing the strength of mediation effect the study used Variance Accounted for (VAF) in line with Hair *et al.* (2013) who classified VAF of = 20%, =20 = 80% and =80% as no mediation, partial mediation and full mediation respectively. Therefore, with the VAF of the current study standing at 35% it can be classified as partial mediation.

### **Evaluation of R<sup>2</sup>, effect-size (f<sup>2</sup>) and predictive relevance (Q<sup>2</sup>):**

Having determined the impact of the path coefficients and mediation effect for the model, then, we measured the level of the R-squared values, effect size and predictive relevance of the model. The coefficient of determination (R<sup>2</sup>) of the model 0.223 and adjusted is 0.43. The research model explained 22.3% of the total variance in organizational performance. This suggests that the two sets of exogenous latent variables (i.e., competitive advantage and entrepreneurial orientation) collectively explained 22.3% of the variance in SMEs performance. Falk and Miller (1992) proposed an R-squared value of 0.10 as a minimum acceptable level. Following Falk and Miller (1992)'s approval, it can be said that the endogenous latent variable had an adequate level of R<sup>2</sup> values. Also, as classified by Chin (1998) R<sup>2</sup> of 0.19, 0.33 and 0.67 as weak, moderate and substantial respectively, the R<sup>2</sup> of the present study can be recognize as weak.

Chin (1998) Effect size shows the relative effect of a specific exogenous latent variable on endogenous latent variable(s) by means of changes in the R<sup>2</sup>. It is calculated as the increase in R<sup>2</sup> of the latent variable to which the path is connected, relative to the latent variable's proportion of unexplained variance (Chin, 1998). Thus, the effect size could be expressed using the following equation:

$$\text{Effect size: } f^2 = \frac{R^2 \text{ included} - R^2 \text{ Excluded}}{1 - R^2 \text{ included}}$$

Cohen (1988) defined f<sup>2</sup> values of 0.02, 0.15 and 0.35 as having small, medium and large effects, respectively. The result in this study disclosed that the effect size for entrepreneurial orientation was 0.025 and 0.076 for competitive advantage. Consequently, the effect size for both entrepreneurial orientation and competitive advantage is considered as small. The current study used Stone-Geisser test of predictive relevance of the research model by applying blindfolding techniques (Geisser, 1974; Stone, 1974). Specially, a cross-validated redundancy measure (Q<sup>2</sup>) was used to evaluate the predictive relevance of the research model (Chin, 2010; Geisser, 1974; Hair *et al.*, 2013a, b; Ringle *et al.*, 2012; Stone, 1974). The Q<sup>2</sup> is a standard use to a measure how well a model predicts the data of omitted cases (Hair *et al.*, 2013a, b). Henseler *et al.* (2009) recommend that, a research model with Q<sup>2</sup> statistic(s) larger than zero is considered to have predictive relevance. Result revealed Q<sup>2</sup> statistic of 0.23 for the endogenous latent variable which is beyond zero, signifying predictive relevance of the model (Chin, 1998; Henseler *et al.*, 2009).

### **CONCLUSION**

As stated in the objectives, the study examined the direct effect of entrepreneurial orientation, competitive advantage on the performance of SMEs in Kano, Nigeria. It also examine the mediating effect of Competitive advantage on relationship between Entrepreneurial orientation and SMEs performance.

Consequently, the Findings of the study stress the importance of Entrepreneurial orientation and Competitive advantage in increasing the performance of SMEs. Also, SMEs performance is positively affected by Entrepreneurial orientation and competitive advantage. In addition, the current study indicates that Competitive advantage mediate the relationship between Entrepreneurial orientation and SMEs performance.

The current study contributes to the existing literature by adding evidence from Nigeria on the influence of entrepreneurial orientation and competitive advantage on SMEs performance. Theoretically the integration of competitive advantage as a mediator into entrepreneurial orientation and SMEs performance has contributed to the theory of RVB.

### **IMPLICATIONS**

The finding could have policy implication for Nigerian Entrepreneurship regulatory agencies such as SMEDAN as it suggests a strategy toward increasing the performance of SMEs through Entrepreneurial orientation and competitive advantage.

### **LIMITATIONS**

This study is connected with a number of number of limitations which comprise the following: the coefficient of determination is measured to be weak in consistent with Chin (1998) which implied that entrepreneurial orientation and competitive advantage explain only 22.3% of the variations in SMEs performance in Nigeria. Nevertheless, this can be improved through assimilation of additional variables not included in the current study. The sample used in this study are concentrated in Kano state only. The future research should use other samples from other part of the country. Even though, the sample is sufficient for the purpose of this study, future studies should consider the enlargement of samples relative to the number of predictors to be used in their studies, finally.

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