Board Entrepreneurial Orientation, Board Guanxi and Firm Growth of Small Medium Enterprises in Malaysia

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Abstract
This conceptual paper is based on a study that predicts the overall Small Medium Enterprises firm growth based on board entrepreneurial orientation and board guanxi in Malaysia context. Previous studies on board of directors’ attributes tend to consider financial performance in its analysis only. The inclusion of the growth indicators such as sales figures, employee number, introduction of new product and new market broaden the research scope to fill the previous research gap. This study also aims to examine the relationship between board entrepreneurial and guanxi in relations with SMEs firm growth. One of the most significant theoretical implications is the introduction of a conceptual model on SMEs firm growth, board entrepreneurial orientation and board guanxi based on Malaysia context. From the practitioners’ perspectives, this paper suggests improvement of existing approaches to the governance and growth of SMEs. There is a dearth of exploratory endeavors in the context of SMEs firm growth and board of directors’ attributes for developing nations. Thus, empirical study in this area merits critical attention.

Keywords: Board entrepreneurial orientation, board guanxi, SMEs firm growth

1. Introduction
The boards of directors play a vital role to maintain effective corporate governance, particularly in firms held by many shareholders including the Small Medium Enterprises firms (Johannisson and Huse, 2000). When a firm is held by many shareholders with the separation of ownership and control, there is a possibility of an agency problem (Fama and Jensen, 1983). Generally, the firms’ management team is given the responsibility to implement major firms’ strategies and policies. The agency problem occurs due to the majority shareholders who own the firms do not involve in the daily operations of the firms (Fama and Jensen, 1983). Most of these firms’ daily operations are run by a management team who does not hold a single share in the firms. In this situation, the board of directors is regarded as a crucial mechanism to moderate and reduce the conflicts between the shareholders and the management team (Fama and Jensen, 1983).

The board of directors is regarded as a crucial mechanism in the corporate governance which can have an impact on the companies’ performance (Pearce and Zahra, 1992; Johnson et al., 1996; Forbes and Milliken, 1999). Previous studies on boards of directors mainly focus on larger firms’ contexts (Abdullah, 2006; Hashim and Devi, 2008; Kor and Sundaramurthy, 2009). Few studies on corporate governance have acknowledged the importance of well-functioning boards of directors in small and medium-sized firms in relation with firms’ performance (Zahra and Pearce, 1989; Borch and Huse, 1993; Johannisson and Huse, 2000; Abor and Adjasi, 2007). In relation to research on boards of directors’ variables, previous studies commonly investigate the attributes such as board independence, board ownership and board size (Pass, 2004; Fauzi and Locke, 2012; Awan, 2012).

A good relationship among the business partners is vital to grow the business. Nevertheless, the nature of relationships may differ across cultural due to difference in conceptions and expectations. The networking among individuals is vital to develop relationships with others and can stimulate emotional ties for a certain purpose. To further understand this phenomenon, Forret and Dougherty (2004) suggest few networking behaviors, comprising of joining professional associations, taking high-visibility work assignments, and attending social functions. In addition, Geddie et al. (2005) compare the constructs between relationship marketing and guanxi. They identified four constructs attached with guanxi, including: 1) bonding; 2) empathy; 3) reciprocity and 4) trust. On the other hand, the relationship marketing commonly relates to: 1) satisfaction, and 2) customer loyalty (Geddie et al., 2005). In other words, guanxi creates the relationship before the transaction, while the relationship marketing deals with the transaction in advance and creates the relationship later. Across the literature review, the studies to examine guanxi as one of the board of directors’ attribute is very rare in relationship with SMEs firm growth. Thus, the present study aims to fill this gap.

Generally, firms that operate entrepreneurially perform better than those firms that are more conservative. Entrepreneurial firms usually involve in specific strategic actions including innovation, proactiveness, and risk-taking (Lumpkin and Dess, 1996). With the relationship between entrepreneurial orientation (EO) and firm performance are widely accepted by scholars, researchers are now increasingly focus on the contextual factors that change the nature of the relationship between EO and various manifestations of organizational performance. In this vein, this study adopts EO into board of directors construct to investigate...
SMEs firm growth. As such, this study also investigates the potential boundary conditions on the relationship between board EO and SMEs firm growth.

There is a dearth of exploratory endeavors in the context of SMEs firm growth and board of directors’ attributes for developing nations. Thus, empirical study in this area merits critical attention. We attempt to explore a model for overall SMEs firm growth based on board of directors’ attributes. We aspire to examine the relationship between board entrepreneurial orientations, board guanxi, and SMEs firm growth in Malaysia context.

2. Firm Growth

According to Penrose’s (1959), firm growth comprising of an increase in firm resource and expansion of firm organization structure. On another literature, Huse (2005) demonstrated that growth of a firm covered a wider set of parameter such as product and process innovation as well as venturing into new marketplaces. Subsequently, Davidsson, (2005) presented the idea of entrepreneurial growth which consisting of the launch of new products or services. Entrepreneurial growth as presented by Davidsson (2005) also taking into consideration of looking for new domestic and international market. Although, some prior studies have adopted firm growth as a proxy of firm performance (Aaboen et al., 2006; Shepherd and Wiklund, 2009; Bradley et al., 2011), but relatively few of the previous studies had investigated the issues on board of directors’ and SMEs firm growth.

Previous research on board of directors’ attributes mainly focused on financial performance, namely ROA and ROE (Haron et al., 2008; Awan, 2012; Yusoff and Alhaji, 2012). However, through extensive literature review, the researcher found that firm growth (sales figure and employee number) as performance indicators having been largely ignored the study on the board of directors attributes. Besides financial performance, firm growth performance has been recognized as an important aspect for business to perform (Wiklund and Shepherd, 2005; Coad and Rao, 2008; Bradley et al., 2011). The inclusion of the growth indicators including sales figures, employee number, introduction of new product and new market broaden the research scope to fill the previous research gap.

Wiklund and Shepherd (2005) refuted that growth as a measurement for firm performance is better than accounting ratio or financial performance indicators. The suggestion of Wiklund and Shepherd (2005) is in line with the change-in-amount perspective as mentioned by Penrose (1959). Penrose (1959) proposed that growth can be measured with a broad range of indicators such as sales and employment measures. In a recent study, Aaboen et al. (2006) also supported the notion of Penrose that firm growth can be measured with multiple measurement including sales number, employment figure and other appropriate measurement. Although, various measurement pertaining to growth are suggested by different researchers, the sales figure is the most preferred indicator to measure growth (Ardishvili et al., 1998; Park and Bae, 2004; Shepherd and Wiklund, 2009; Bradley et al., 2011).

3. Small and Medium Enterprises firm Growth

The existence of a broad range of internal and external factors affecting firm growth has established a challenge for full explanation of the phenomenon studies and the growth of SMEs is a complex phenomenon. For example, Davidsson (1991) theoretical model consists of three main constructs namely, ability, need and opportunity. A cross-sectional research method was used to investigate three variables to relate with small medium sized firms growth and the results revealed that all three factors affect growth with at stable effects across the industries. Research reviews have concluded that firm growth is not a homogeneous phenomenon, but firms grow in many different ways for different reasons with different consequences (Shepherd and Wiklund, 2009; McKelvie and Wiklund, 2010).

In the process of firm expansion, entrepreneurship is vital on identifying business opportunities by entrepreneurial managers. This is consistent with the notion of “entrepreneurial growth” as demonstrated by Davidsson (2005), which refers to the introduction of new products or services, and venturing into new geographic markets. Therefore, SMEs firm growth study needs to focus more on specific forms of growth rather than on an undifferentiated notion of total growth (Davidsson et al., 2002; Davidsson et al., 2010; Clarysse et al., 2011; Naldi et al., 2013). Thus, SMEs firm growth study via the introduction of new products or services, and penetration into new geographic markets, locally and internationally is crucial.

Moreover, Delmar (1996) conducted a study to find out the relationship between the behavior of the SMEs entrepreneurs and business performance. A theoretical perspectives based on the modern psychology and entrepreneurship research was developed (Delmar, 1996). The variables in Delmar SMEs study consists of business performance, entrepreneurial performance, the motivation and ability of the individual, and the environment. Delmar (1996) demonstrates that the motivation theories have a different perspective than performance theories. For instance, motivation theories focus on why people behave the way they do, but performance theories aim to assess the behavior of the individual. The main findings of Delmar’s study are: 1) job interest of the entrepreneur associated significantly to the firm performance; 2) intellectual ability of the
entrepreneur has no correlation to the firm’s performance; 3) values of the entrepreneur had little explanatory value in relation to the firm’s performance, but could differentiate moderately between entrepreneurs and non-entrepreneurs; 4) entrepreneurs’ prediction of future firm performance was dependent on the perceived causes of their present situation; 5) growth motivation of the entrepreneur was explained by previous growth, interests, attitudes and opportunity recognition.

A further analysis of behavioral differences between more successful entrepreneurs and less successful ones showed that successful entrepreneurs are more cautious, employed long-term planning and used external competence to overcome for their own shortcomings (Delmar, 1996). On the other hand, the non-successful entrepreneurs preferred control over their firm to business expansion and are not willing to delegate authority. Moreover, the non-successful entrepreneurs have a less well-developed personal network (Delmar, 1996).

Based on an extensive review of literature on small firm growth or performance, Wiklund (1998) develops a theoretical model that comprises of four theoretical attributes namely, environment, resources, motivation and strategy of entrepreneurial firms as exhibited in Figure 2.1. Wiklund (1998) demonstrates that the effects of attitudes, resources and capabilities, industry and perceived environment on growth or performance mediated through entrepreneurial orientation (EO). Wiklund (1998) explains EO as the small business manager’s self-perception of the firm’s strategic orientation which consists of three main variables, namely, risk taking, proactiveness and innovation. Moreover, the strategic orientation of the CEO in small firms is very likely to be the strategic orientation of the firm. Therefore, the strategic orientation of the CEO reflects the willingness of a firm to engage in entrepreneurial behavior (Wiklund, 1998).

The study of Wiklund (1998) focuses on the strategic dimension of small firm growth and reveals that growing firms have a strategic orientation similar to entrepreneurial. In other words, entrepreneurial strategic orientation influences small firm growth and performance. Wiklund (1998) empirical study shows that firms which focus on growing market niches seem to grow better than firms adopting other strategic in stable market. It implies that growing firms are better in detecting and exploiting opportunities.

Among Wiklund (1998) findings are younger firms grow faster than older firms, and larger management teams are existed in well-performing firms than low-performing firms.

4. Entrepreneurial Orientation

The initial conceptualization of EO dimensions are suggested by Miller (1983) and includes only three dimensions: 1) innovativeness; 2) risk taking, and 3) proactiveness. However, two additional dimensions of EO are proposed by Lumpkin and Dess (1996), namely: 1) competitive aggressiveness and 2) autonomy. Across the entrepreneurialship literature, most of studies in entrepreneurial orientation adopt Miller (1983) approach to operationalize entrepreneurial orientation with three EO dimensions (Wiklund, 1999; Wiklund and Shepherd, 2003; Zahra and Covin, 1995). According to Miller (1983), a so called entrepreneurial firm usually engages in product and market innovation, takes risky ventures, and adopts proactive measures to defeat its competitors.

When come to the small business managers, EO is regarded as the small firms’ strategic orientation which including risk taking, proactiveness and innovation (Wiklund, 1998). According to Wiklund (1998), the strategic orientation of the CEO in small firms is the also the strategic orientation of the firm. Therefore, the strategic orientation of the CEO exhibits the willingness of a firm to participate in entrepreneurial behavior (Wiklund, 1998). Moreover, Wiklund (1999) relates the positive influence of EO on performance to the first mover advantages and the tendency to take advantage of emerging opportunities implied by EO to sense weak signals and seize the opportunity. Wiklund (1999) also suggests that these firms monitor market changes and respond rapidly, thus capitalizing on emerging opportunities. Innovation keeps them ahead of their competitors, gaining a competitive advantage that leads to improved financial results. Proactiveness gives the firms the capacity to present new products or services to the market before their competitors, which gives them also a competitive advantage (Wiklund, 1999). Furthermore, Wiklund (1999) also states that there is a reason to believe that the relation between EO and performance may be especially strong in the context of small firms. Similarly, in the present study, the entrepreneurial orientation of the BOD demonstrates the willingness of a firm to involve in entrepreneurial activities to boost the SMEs firm’s growth.

From the discussion above, board EO is related with the strategy role of BOD to implement firms’ goals and policies as presented by Zahra and Pearce (1989), the strategy role of BOD transformed in terms of EO is link to also the stewardship theory. The empirical studies of EO in Malaysia SMEs context are still rare. However, Omar and Rejab (2011) reveal that many Malaysian SMEs entrepreneurs in information communication technology (ICT) have steered their organizations from humble start-ups to professional ventures. Hence, in this present study, the board Entrepreneurial Orientations (EO) refers to the strategies, decisions and actions making processes adopted by the board of directors. In addition, one of the aims of the present study is investigate the relationship between SMEs board EO and firm growth in Malaysia context. In the present study, the board of directors of SMEs are the key driver of SMEs firm growth. Thus, the researcher
proposes the following hypothesis;

H1: Board Entrepreneurial Orientation has a positive relationship with SMEs firm growth.

5. Guanxi Network

According to Mizruchi (1996), an interlocking directorship refers to a director whom sits on multiple boards of several firms. Therefore, an interlocking directorship is one type of board network which creates an important link among firms (Hung, 1998). In other words, an interlocking directorship refers to the social connection which is built between few firms as one person holding positions as boards of director for at least two or more than two firms.

With regard to the resource dependency perspective, the interlocking directorships can help the firms to secure critical resources (Pfeffer and Salancik, 1978). Generally, the board of directors’ roles included to assist the firms in dealing with its environment, to enhance its legitimacy and to achieve better firms’ performances. Thus, the boards of directors are regarded as an important linking vehicle to the firms with the external environment (Hung, 1998). Moreover, the boards can easily access to the firms’ finance information and operations as well as knowing more about the needed resources to be allocated among the interlocking firms (Hung, 1998). Thus, resource dependence theory is the most appropriate approach to describe the board of directors interlocking issues compares to other theoretical approaches (Zahra and Pearce, 1989).

Besides the approach of interlocking directorships, board network may be investigated from another point of view, namely guanxi approach. Guanxi can be defined as personal connection, close and good relationships, as well as one’s social network (Tsang, 1998). In fact, guanxi plays a vital role in the Chinese daily social and business life and it is crucial factor to build a long term personal relationships (Stanifird and Marshall, 2000). Many researcher have realized the potential of guanxi to facilitate business transactions (Lee et al., 2001; Zhuang et al., 2010; Sheng, et al., 2011). To date, however, no empirical research has integrated guanxi into board network as an important element similar to interlocking directorships. Therefore, the researcher draws on vital role of guanxi to propose a conceptual model that links guanxi as a board of directors attribute and SMEs firm growth in present empirical study.

When come to the academic research, guanxi usually refers to the social connections or interactive behaviors between individuals (Chadee and Zhang, 2000; Lee and Dawes, 2005; Leung, et. al. 2005). This multi-faceted nature of guanxi concept is considered complex and confusing (Ambler 1994; Lee & Dawes 2005; Lee, et al. 2001). In a more recent literature, Zhuang et al. (2010) define guanxi in a more details form into; 1) guanxi states; 2) guanxi behaviors; and 3) guanxi norms. Firstly, the “guanxi states” demonstrate the qualities of a relationship between individuals. Secondly, the “guanxi behaviors” indicate the activities involved by an individual to develop and maintain good relationship. Finally, the “guanxi norm” explains guanxi behavior including the actions of renqing and mianzi (Zhuang et al. 2010). The renqing is the assistance or favor that one gives to others (Zhuang et al., 2010). For instance, when a member in the association or group gets into difficulty, one should give assistance, and after it has been received, the recipient should return it as soon as the opportunity arises (Hwang, 1987). Those who do not repay assistance or renqing are considered people who cannot be trusted or losing face. On the other hand, mianzi or face is also seen as an individual’s image in a social context (Bond, 1991). One is given face by others in society when he or she is respected or having face. One’s face may be lost by an inappropriate behavior and losing face can bring shame to an individual (Zhuang et al. 2010). Moreover, making others to lose face is considered an aggressive action (Tung and Yeung, 1996).

In regard to SMEs and guanxi, Krittakorn, S. (2007) conducts a study using data from 298 Bangkok based Sino-Thai SMEs provide a number of interesting results. Krittakorn, S. (2007) discovers that the strength of ties in the guanxi or network for the family relationship is stronger than the friend and stranger relationship, while the strength of ties in the network for the friend relationship is stronger than the stranger relationship. The result of the study also shows that guanxi has a positive impact on Sino-Thai SMEs and business performance (Krittakorn, 2007).

In another recent empirical study, Cao et al. (2014) conduct a study on the impact of guanxi on the bullwhip effect and firm performance with survey data of 205 samples. The result shows that that guanxi has a positive impact on firm performance and the bullwhip effect. In regard to that study, Cao et al. (2014) also define guanxi as the ideas of a relationship covers reciprocity, and ongoing long-term commitment and personal networks.

Despite the prominence of the guanxi perspective, little research examines guanxi’s function in the process of board of directors attributes. The interlock directorship explains how board of director who sit on various firms’ board can secure critical resources for the firms. While through board guanxi, members in the board of directors do not necessary have to sit in several boards in various firms in order to obtain crucial resources, but the connections of the board of directors itself play a vital role to get important resources for the firms. To address this gap in literature, this study examines how guanxi may be linked to
board of directors attributes to improve SMEs firm growth. Through extensive literature review a hypothesis is formulated as below;

H2: Board guanxi has a positive relationship with SMEs firm growth.

6. Conceptual Framework and Conclusion

Based on the thread of discussion, we develop a conceptual model (Figure1) that proposes relationships between board EO, board Guanxi and SMEs’ firm growth.

![Conceptual Framework](image)

Figure 1. Conceptual Framework

We foresee that a positive correlation between board entrepreneurial orientations and SMEs firm growth as well as board guanxi and SMEs firm growth. The newly developed board of directors’ attributes assumed to be significantly explained the variance in SMEs firm growth. This study intend to adopt PLS approach to analyze the data since predicting the relationship is the main concern, rather than theory testing (Hair et al., 2014). Smart PLS M3 Version 2.0 software will be employed in this regard with the application of a bootstrapping technique to determine the significance levels for loadings and path coefficients. Following the general convention, a two steps approach is considered to assess the conceptual model, namely the measurement model and the structural model (Hair et al., 2014). This paper also initiates the need to consider the measurement of SMEs firm growth based on sales, employment, new product, and new market as performance indicators. Regarding the managerial implication, this paper provides some opportunities for the improvement of existing approaches to the governance of SMEs. Thus, this preliminary conceptual work actually opens door for further empirical work to consider the effects of board EO and board guanxi towards SME’s governance and growth.

References


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