TITLE - SMALL ENTERPRISE GROWTH THROUGH INTERNAL MARKETING AND EMPLOYEE SATISFACTION

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SUMMARY

Formulating and implementing internal marketing strategies for employee satisfaction will be more productive to small businesses than to pursue the Holy Grail of becoming the number one or two in the industry. Internal marketing is about treating those with whom you work as clients. Treating co-workers as your clients will make them feel special, and staff who feel special are more likely to make clients feel the same way. A small business firm without an internal marketing philosophy may overlook countless opportunities to derive true value from their staff.

Internal marketing is essentially an intra-organisational activity that transcends all functional boundaries to integrate the activities of the organisation. There are internal marketing gaps in small businesses and many approaches are available to close these gaps. These approaches that address the employee related issues are at heart of success of small business enterprises that compete with giant multinationals in the same markets to maintain their competitive edge. For small business enterprises internal marketing is a management tool that helps to achieve sustainable competitive advantage in a highly competitive business environment.

The key aspects of the internal marketing domain are the maintenance of organisational internal service culture and climate, the notion of the internal customer, the impact of employee satisfaction on customer satisfaction, the hiring of right employees with service inclination, the retention of employees and the value of long term employees. Attention to these aspects will enable small business companies to harness their resources and compete more effectively to satisfy their customers both internal and external, in the long term. A continuing commitment to the above beliefs of internal marketing will enable small business enterprises to face future challenges with confidence.

INTRODUCTION

Small business can win the battle for market share gradually by pleasing their customers one at a time rather than devoting time to analysing demographic trends, ratings points or other global measures. Businesses cannot afford to lose their customer because it costs five times more to replace a customer than to retain one. This makes it necessary especially for small business enterprises to take appropriate steps to ensure that all employees in the organisation have the necessary skills, motivation and authority to please everyone in their limited customer base.

Customers have core expectations. What they expect from a business firm is that they deliver what was promised. From small business enterprises customers may also expect greater personal attention and a decent apology when there are performance breakdowns. By meeting such fundamental requirements small businesses could please their customers one at a time and gradually win the battle for market share. Therefore small business companies do not need rare resources such as exceptional individuals to create goodwill and develop loyal customers.

The impact of dissatisfied customers goes beyond the loss of a single customer. They do not simply go away but take every possible opportunity to tell anyone who will listen to them about the rotten treatment they endured at the hands of the company. The worst is that as many as 96% of the dissatisfied customers who do not complain to the offending company on the average tell 9-10 friends, acquaintances and colleagues about the poor treatment they received [5]. Such bad word-of-mouth publicity could produce disastrous results in small business enterprises.

In small business enterprises employees occupy positions which make them psychologically and physically close to their customers as they are to their fellow employees. Their skills, behaviour and attitudes are therefore critical to the customer perception of the organisation and their future loyalty.

Customer loyalty is an important determinant of the business profit. A 5% increase in customer loyalty can produce a profit increase from 25% to 85% [11]. In order to build customer loyalty small business enterprises thus need to focus on the goals of employee satisfaction, adopt an employee focus attitude, develop skills

required in the employees to please customers and to recover when mistakes are made. In essence small business enterprises have to adopt the philosophy of internal marketing.

Employees and customers are important economies of small business enterprises. Small business firms need to pay attention to this new paradigm to drive their growth and profitability. They should enable the employees to deliver results to their customers. Loyal, satisfied and productive employees create value for customers and customer satisfaction primarily results from employee satisfaction. Small business firms therefore should invest in their people, the technologies that support people and have compensation linked to the performance of employees at all levels. This means adapting the philosophy of internal marketing.

THE IMPORTANCE OF THE EMPLOYEE

Employees are important because they are the service, they are the organisation in the customer's eyes and they are the marketers. In many cases the contact employee is the service – there is nothing else [14]. The contact employee in some cases provides the entire service single-handedly. The offering is the employee. Therefore, investing in the employee to improve the service parallels making a direct investment in the improvement of a manufactured product [14]. Even if the contact employee doesn't perform the service entirely, he or she may still personify the firm in the customer's eyes. Because contact employees particularly in small business enterprises represent the organisation and can directly influence customer satisfaction, they perform the role of marketers. They physically embody the product and are walking billboards from a promotional standpoint.

Employees of small businesses who often directly interact with customers influence customer perceptions of organisational responsiveness through their personal willingness to help and their promptness in serving customers. Additionally the assurance dimension of service quality is highly dependent on employees' ability to communicate their credibility and to inspire trust and confidence [14].

Most service problems are people problems. The inseparability of service from staff, the heterogeneity and difficulty in standardising the service all mean that most firms find it difficult to exercise control over how well customers are treated. McDonalds attempts to control as much as possible the quality of service delivered by its staff by setting precise standards even on how customers are greeted, served, and thanked. The large firms which

are best at customer service such as McDonalds, Xerox, Disney, and Westin, treat employee relations very seriously, knowing that good employee relations leads to good customer relations [2]. Small business firms who compete with giant multinationals in their home markets will have to out do these firms in their employee relations to gain competitive advantage.

THE INTERNAL MARKETING PHILOSOPHY

Internal marketing uses a marketing perspective for managing an organisation's human resources [1]. Internal marketing is concerned with creating, developing and maintaining an internal service culture and orientation, which in turn assist and support the organisation in the achievement of its goals [8]. It involves meeting the needs of employees so they can meet the needs of customers. It is a strategic weapon that helps to retain customers through increased employee satisfaction. For this strategy to be successful top level management must fully embrace it, and therefore the idea of internal marketing must originate at the top and be communicated down to the very bottom of the firm.

Despite its name, internal marketing is a management strategy rather than a marketing function [12]. Effective managers recognise the importance of serving their internal customers—the employees—as a prerequisite to providing satisfaction to external customers. They do a great job with their employees for them to do a great job with their customers.

Stershic (1994) has identified two separate but integrated aspects of internal marketing: attitude management and communications management. Attitude management is the process of motivating employees to be customer-focused; that is, getting them to "buy-in" to management's service strategy. Communications management involves managing the information that employees need to perform effectively.

Every person working within an organisation play the roles of both a supplier and a customer and this has given rise to the notion of "internal customer". All employees are part of the process that connects the organisation with the customer at the point of sale or "moment of truth". Thus for customer satisfaction there must be effective coordination of activities between front-line and back-office staff. The ability of the front-line staff to perform effectively depends to a great extent on the support they get from the other employees of the

organisation. Internal marketing enables the integration of various functions and allows employees across functional boundaries to work together to meet the needs and expectations of external customers. Through internal marketing all employees, even those who do not come into direct contact with customers, begin to understand how they could contribute to customer satisfaction.

CHALLENGE OF INTERNAL MARKETING

Internal marketing is about treating those with whom you work as clients [7]. Evaluation of internal marketing, communications and staff commitment of unsuccessful small business enterprises offers the clues as to why things go wrong in many of them. Managers of unsuccessful organisations fail to give a clear sense of direction to their people, they do not begin to communicate early enough, and they use the wrong tools. Their failure lies in the fact that they do not get their employees to "buy-in" to the process. They are ignoring the very people needed to deliver the results that guarantee success.

According to Taylor and Consenza (1997), the overall objective of internal marketing is to develop and retain motivated personnel within the organisational environment to reduce fluctuations in service quality and increase customer consciousness. A satisfied customer will remain loyal to the company or brand, but the creation of satisfaction depends on the co-operation and commitment of employees. Barnes (1994) states that getting them to "buy-in" is the challenge of internal marketing.

Job satisfaction and performance are correlated [9]. Satisfied employees besides performing functions that are formally required in their job descriptions, positively relate to other facets of employment such as helping co-workers, volunteering for extra work and so forth. There is also a linkage between employee satisfaction and retention and customer satisfaction and retention [4]. A strong linkage also exists between these two variables. Treating co-workers as your clients will make them feel special, and the staff who feel special are more likely to make clients feel the same way. Satisfied employees are a critical determinant of long-term customer satisfaction in an organisation. Similarly satisfied customers lead to employee satisfaction and retention, as employees find it much easier to deal with satisfied customers rather than the dissatisfied ones. Thus employers who implement internal marketing programes to develop and retain satisfied employees increase their profitability when these

employees deliver high service quality at lower cost which results in creation and retention of satisfied customers.

THE INTERNAL MARKETING GAP

Piercy and Morgan (1991) said that a firm's marketing performance could be improved by the development of internal marketing strategies which parallel, reinforce and support external marketing strategies. An internal marketing gap however can exist where executives fail to promote and position their plans and strategies in the internal market place.

Attention to customers, competitors and markets in the world outside is insufficient to achieve growth in small business enterprises. While such an external focus is obviously important to organisational success it is not in itself sufficient for developing a marketing orientation within the firm. In most small businesses there exists an "internal marketing gap." It seems that in addition to developing marketing programs and strategies aimed at the external marketplace, it is also necessary to develop a process and a program for the internal marketplace within organisations in order to achieve the organisational change needed to achieve the growth targets [7]. Unfortunately there is no unified notion on what exactly internal marketing is and how it could be implemented within an organisation [8].

The Gaps Model of service quality [15] proposes that customer assessments of service quality result from a comparison of service expectations with actual performance. Zeithaml and Bitner (1996) said that even when customer expectations are well understood and services have been designed and specified to conform to those expectations, there may still be discontinuities in service quality when the service is not delivered as specified. Because employees frequently deliver or perform the service, human resource issues are a major cause of these discontinuities. Employee behavior and attitude has an impact on the relationship with external customers. By focusing on the central role of employees, and by developing strategies to enhance employee satisfaction, organisations will be able to achieve effective customer-oriented service delivery and customer satisfaction in the external markets. This is the basic premise behind the development of internal marketing.

STRATEGIES FOR CLOSING THE INTERNAL MARKETING GAP

A complex combination of strategies is needed to ensure that employees are willing and able to deliver quality services and that they stay motivated to perform in customer-oriented, service-minded ways. Zeithaml and Bitner (1996) said to build a customer-oriented, service-minded work force, an organisation must: (a) hire the right people, (b) develop people to deliver service quality, (c) provide the needed support systems, and (d) retain the best people. Within each of these basic strategies are a number of specific sub-strategies.

(a) Hire the Right People – One of the best ways to close the internal marketing gap is to start with the right people from the beginning. This implies that considerable attention should be focused on hiring and recruiting personnel. In the current volatile small business market, where the skills and experience of employees are no longer sufficient, organisations should search for competent employees who could contribute to organisational effectiveness and competitive advantage.

Significant costs are associated with employee turnover. Expenditure on advertising, staff time on interviewing, training a person, interview expenses paid to applicants and possible relocation expenses are some of the direct costs incurred when a new applicant is hired. There are additional opportunity costs that are incurred when either a situation is left vacant for some time, or when a new recruit takes over from an experienced employee. Given the high cost of recruitment it is important that small businesses manage the recruitment process, so that only applicants who are able to match the profile that the company endeavours to portray to their customers, are employed the first time. The approaches to improve recruitment efforts to get the right people are:

- **Compete for the Best People -** To get the best people, organisations need to identify who the best people are and compete with other organisations to hire them. Berry and Parasuraman (1997) refer to this as "competing for talent market share." They suggest that firms act like marketers in their pursuit of the best employees, just as they use their marketing expertise to compete for customers. This means using a variety of methods to recruit employees, beyond just advertising in the newspaper.

  A whole range of channels are available to small businesses trying to find the best employees. A good starting point is to look for competent employees from within the organisation. They are more likely to stay

than those recruited from outside as they already have a relationship with the company. Another channel worth pursuing is referrals from existing employees. Both these options are highly cost effective. Small business enterprises could also use third parties such as executive search consultants, commercial recruitment agencies, universities or other employers who have access to potential employees.

In spite of the availability of many sources, the reality however is that finding good staff is becoming increasingly difficult. For some jobs there are floods of applicants. But due to skill shortage it is hard to fill vacancies in certain key areas. Under these circumstance small business enterprises seeking to hire the right people, essentially need to follow good recruitment practices.

- **Hire for Service Competencies and Service Inclination -** Once potential employees have been identified, organisations need to be thorough in interviewing and screening to truly identify the best people. Management needs to assess both the service competencies and service inclinations of the candidates, as these are key complementary capacities that are essential to develop customer loyalty.

  Service competencies are the skills and knowledge necessary to do the job. But, given the multidimensional nature (reliability, responsiveness, empathy and assurance) of service quality, employees should be screened for more than just their service competencies. They must also be screened for service inclination – their interest in doing customer-related work – which is reflected in their attitudes toward customers and orientation toward serving customers and others on the job.

- **Be the Preferred Employer –** The best candidates for a job can be appointed only if they are interested and apply for it in the first place. One way to attract the best people is to be known as the preferred employer in a particular industry or in a particular location. Being a preferred employer involves a variety of strategies, many of which revolve around treating employees as whole people and addressing their personal needs as well as work needs, and creating environments where people want to work while recognising that "people have lives."

  A clearly defined recruitment strategy that adopts a relationship marketing focus and building a reputation as a first class employer is critical for a small business organisation to be an attractive potential employer.

Once recruited, to retain the good people, organisations must deliver what is promised to their prospective employees.

(b) <u>Develop People to Deliver Customer Expectations</u> - To grow and maintain a work force that is customer oriented and focused on delivering what customers expect, small business enterprises must develop their employees to deliver quality service. That is, once it has hired the right employees, the organisation must train and work with these individuals to ensure their performance meets the required standard.

- **Train for Technical and Interactive Skills -** To provide quality service to customers, employees need ongoing training in the necessary technical skills and interactive skills.

- **Empower Employees –** Empowerment, which is a key internal marketing activity, enables the employees to deliver better quality of service to their customers. Many organisations have discovered that to be truly responsive to customer needs, employees need to be empowered to accommodate customer requests and to resolve problems on the spot. Empowerment means giving employees the desire, skills, tools, and authority to serve the customer. The key to empowerment is giving employees authority to make decisions on the customer's behalf. But, giving authority alone is not enough. Employees need the knowledge and tools to be able to make these decisions, and they need incentives that will encourage them to make the right decisions.

  Empowerment pushes decision-making down into the organisation and encourages people to think and use judgement. It allows for faster and flexible responses for customers needs by well trained, knowledgeable and confident staff. Providing employees have abilities that can be utilized and developed in this way, empowerment can be an effective tool in the development of employees to deliver customer expectations in small business enterprises. However for some small business enterprises empowerment may not necessarily be the best choice. Therefore launching a full-blown empowerment strategy should be done only after careful consideration of its pros and cons.

- **Promote Teamwork -** The nature of many service jobs suggests that customer satisfaction will be enhanced when employees work as teams. Because most jobs at times may be frustrating, demanding and

challenging, those employees who feel supported and have a team backing them up will be better able to maintain their enthusiasm and provide quality service. Employees who provide each other with consideration, trust, warmth and support help to break down barriers and enhance internal communication. By promoting teamwork a small business enterprise can enhance the employees' abilities to deliver excellent service, while at the same time the camaraderie and support enhance their inclination to be excellent service providers.

One way of promoting teamwork is to encourage the attitude that "everyone has a customer." If each employee can see how he or she in some way integral in delivering quality to the final customer, and if each employee knows who he or she must support to enhance customer loyalty, teamwork will be enhanced. Team goals and rewards will also promote teamwork. When teams are given rewards, rather than having all rewards based on individual achievements and performance, team efforts and team spirit will be encouraged.

(c) <u>Provide Needed Support Systems</u> - To be efficient and effective in their jobs, workers require internal support systems that are aligned with their need to be customer focused. This point cannot be over-emphasised. Some strategies for ensuring customer-oriented internal support are as follows.

- **Provide Supportive Technology and Equipment -** When employees do not have the right equipment, or their equipment fails them, they can be easily frustrated in their desire to deliver quality service. To do their jobs effectively and efficiently, employees need the right equipment and technology.

- **Develop Customer-oriented Internal Processes -** An organisation's internal processes should be designed with customer value and customer satisfaction in mind. This will allow their personnel to deliver quality services to customers. In other words, internal procedures must support quality service performance.

(d) <u>Retain the Best People</u> – Small business organisations that hire the right people, train and develop them to deliver service quality, and provide the needed support, must also work to retain the best ones. Long-term employees often develop personal relationships with customers. They identify with the norms and values of the organisation and take better care of the customers. They transmit these service values and norms to the successive generations of new employees.

Employee turnover, especially when the best employees are the ones leaving, can be very detrimental to customer satisfaction, employee morale, and overall customer service. The poor employee morale that results from employee turnover can effect team performance when it dampens the morale of the employees who stay with the company. This could ultimately jeopardize the success of the organisation in the external markets. The following strategies will support the retention of the best employees in a small business enterprise:

- **Include Employees in the Company's Vision -** For employees to remain motivated and interested in the organisation and supporting its goals, they need to share an understanding of the organisation's vision. People who deliver service day in and day out need to understand how their work fits into the big picture of the organisation and its goals. They will be motivated to some extent by their paycheck and other benefits, but the best employees will be attracted away to the other opportunities if they are not committed to the vision of the organisation. They cannot be committed to the vision if that vision is kept a secret from them. What this means in practice to small businesses is that their vision is communicated to employees frequently by management and that all employees are encouraged to "buy into" the vision.

- **Treat Employees as Customers -** If employees feel valued and their needs are taken care of, they are more likely to stay with the organisation. Many companies have adopted the idea that employees are also customers of the organisation. The product that the organisation has to offer its employees is a job (with assorted benefits) and quality of work life. To determine whether job and work-life needs of employees are being met, organisations should conduct periodic internal marketing research to assess employee satisfaction and needs. The findings of the research and the actions taken should be communicated by the organisation to the employees.

- **Measure and Reward Strong Performers -** If a company wants the strongest performers to stay with the organisation, it must reward and promote them. This may seem obvious, but often the reward systems in organisations are not set up to reward excellence by individuals. This does not necessarily conflict with the development of team spirit.

(e) <u>Use Conducive Organisational Design</u> – The organisational design must facilitate the implementation of internal marketing concept and philosophies. The traditional hierarchically structured vertical organisations that

optimise individual functions are not fertile grounds to facilitate internal marketing. They help to achieve individual managerial goals at the expense of the whole company and the customers. The use of multidisciplinary teams which marshal the company resources efficiently and effectively to deliver market needs, is more conducive to achieve Internal marketing orientation in small business organisations.

(f) Conduct Staff Surveys – Regular staff surveys are recommended in small business orgnisations to assess the internal service culture and climate. These surveys will identify not only the positive activities that should be continued in the future, but also the obstacles to service quality improvements that require urgent remedial actions. However, much care is needed in handling these surveys. Often employees who are suspicious of the intents of surveys will report the way they think the organisation wants them to do. This could be overcome by telling the employee precisely why the survey is done and then showing them that action has been taken over any concerns raised in the survey.

(g) Promote Internal communications and Networking – Internal communication and networking are the critical competencies managers in small business enterprises must develop to implement effective internal marketing programs. Internal communications, which manifest in the form of company newsletters, brochures, video conferencing, and meetings and announcements, is a mechanism to develop knowledge, experience and expertise in an organisation. It is a valuable method to ensure that everyone in the organisation is aware of their roles in cross functional activities. Achieving coordination and leadership are the other advantages of internal communication and net working.

CONCLUSION

Internal marketing should be viewed as a management philosophy for both motivation and support rather than as a short-lived exhortation program or campaign to boost attention to customers. Much of the work done so far on internal marketing has been embryonic and descriptive or prescriptive. It is evident that there is as yet some confusion over what internal marketing actually is, its role, and how it can be implemented. Essentially, internal marketing is a way of doing business. For small business enterprises it is a management tool that helps to achieve sustainable competitive advantage in a highly competitive business environment.

For internal marketing to play a prominent part in improving customer satisfaction it is obvious firstly that top management needs to be committed to internal marketing. Secondly, the small business enterprise must be prepared to invest resources in nurturing a 'team' environment in the workplace and have both an internal and external marketing plans complement each other in line with the firms business strategy. Finally they should hire the right people, develop them, support them and retain them to create a true business culture where everyone in the organisation will consider good service to internal and external customers a natural way of life.

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An Internal Conceptual Model of the Sustainable Firm

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Abstract

The dynamics of the proactive firm can only be discovered through a conceptual model. This observation is demonstrated in recent strategic literature focusing on dynamic elements to explore the firm's strategic processes and requirements. At no time is a dynamic model more critical to business than in periods of instability and uncertainty evident in the present times. This paper consolidates earlier papers, by this author into a comprehensive internal model of the firm. The paper demonstrates firm dynamics and identifies two elements, marketing and liquidity as central to sustainability in dynamic environments, furthermore the model appears to apply to organisations universally. The paper initiates the concept of the sustainable firm for dynamic environments.

Introduction

Two concepts at the core of accounting, corporation law and much of management literature concerning the firm are that of the "going concern" and "periodic measurement". Economic also has, in recent times, questioned the traditional technological and the transactionally based models of the firm. Whether these concepts are still appropriate to the present dynamic environment is open to question. Furthermore, recent management, entrepreneurship and marketing literature increasingly reflect new concepts which do not fit comfortably with these foundational views of the firm. The purpose of this paper is to present a conceptual framework model of the sustainable firm attuned to proactive and dynamic environments. This model is dynamic and indicates consequence and relationships enabling the understanding of the consequences of decision in the firm.

Ingram's (1996) discussion of the going concern identifies the central issues in the concept as stability for a sufficiently long period to allow meaningful performance measurements to be taken. Financial accounting standards internationally stipulate that "material" short term or "abnormal changes" are identified and separately commented on in financial accounts so that the reader can form a view of what constitutes a "normalised" point in time situation for that firm. Economics has the technological (see Maurice & Phillips 1986; Baumol et al. 1988;) and transactional models of the firm which are also static (see Yang 1997; Shi & Yang 1995; and Yang & Ng 1993; Cheung 1983; Coarse 1937). These models provide insights into the horizontal and vertical relationships in the firm but they are static and, whilst useful to equilibrium economic theory, are of limited use in dynamic situations. As noted by Kirchhoff & Green (1995), dynamic approaches are required to model proactive non-equilibrium economic situations, especially in the entrepreneurial context.

Strategic literature, on the other hand, has since 1990 substantially focused on the dynamic elements of the internal and external business environment in order to develop a better understanding of a firms strategic processes and management decision requirements. Significant analytical discussion on strategy (for example

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Mintzberg 1994 or Quinn 1992) and entrepreneurship (Lumpkin and Dess 1996), no longer accepts a static, pre-emptive or fixed view of the processes but emphasises the ability of management and other stakeholders to interface in a productive and proactive manner.

Strategy has been articulated as consisting of predictable and unpredictable components (Mintzberg 1987). Managers can react by developing "deliberate strategies" to capitalise on foreseeable situations but not for the unpredictable factors which constitute a substantial component of realised strategy (Mintzberg 1994, 1989). Implemented business strategies are thus strongly influenced by "emergent elements" and are often a substantially modified version of the original strategy plan (Mintzberg 1987; Quinn 1992) if such a plan exists. Hofer (1986) identifies turnaround strategy evaluation in terms of cash flow effects. Yet the role of cash flow and liquidity and its effects on the strategic process and behaviour of management, appears to have been largely ignored in published literature and its value underestimated (Geursen 1997). This is especially so in the area of entrepreneurship and small business where research emphasis has been on firm startup activity, venture capital acquisition, entrepreneurial characteristics and behaviours rather than the dynamic ongoing business post startup.

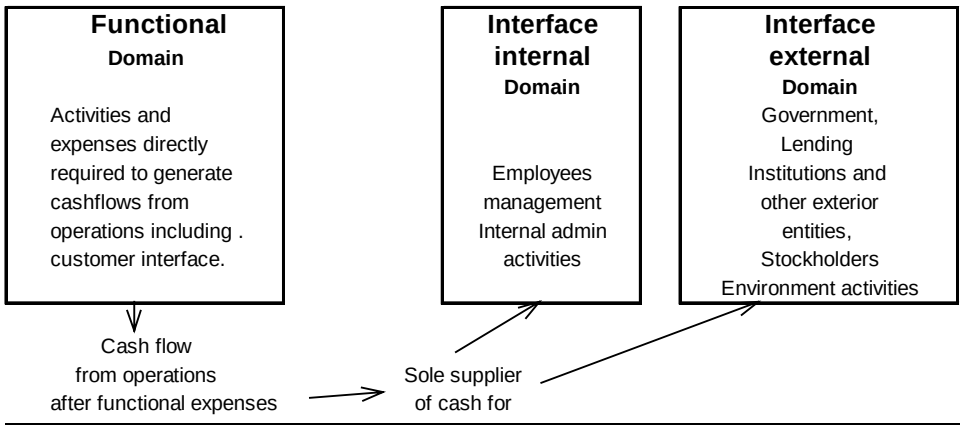
The Component Models

Geursen (1997, 1998, 1998a) presented three models for conceptualising the three critical elements in the internal dynamics of the firm. The first model addresses activity and power, the second, cashflow dynamics, incorporating liquidity implications and the third identifies proactive market and firm interface mechanisms and how these function. The contribution of this paper is to summarise and consolidate the components into an overall conceptual model of the firm. Empirical substance is provided demonstrating that the overall model works in small firms. The organisation of the paper is to present the three components models and consolidate them into an overall model. It then present research from a random sample of small entrepreneurial firms supporting the working of the model and concludes with a discussion of the implications the model has for the study of organisations generally.

The firm as a generative and extractive phenomenon

The first component model identifies how the fundamental relationships of the firm are organised. It identifies a split in the activities in the firm between those concerned with the generation of cashflows from operations and those necessary to service the interfaces demanded of the firm. The interface domain can be further divided to reflect this activity internally and externally. Thus the model extends the technological view of the firm beyond productivity by recognising that, in contemporary times, the firm is subject to "social" costs (for example taxes, environmental charges) over which it has no control. The description in the diagram below reflects these factors and their power implications as follows:

(Figure 1) The Three Domain model



This model provides a framework for classification of focus and its purposes in the organisation. Furthermore it permits distinction between generative and distributive initiatives and recognises that the interface groups are directly dependent on the performance of the functional domain if the organisation is to survive. Agency theory, on which much of accounting and finance literature is based, is thus limited because it restricts analysis to the relationship between the two interface groups and ignores the critical generative initiatives in the organisation. As this model recognises all aspects of strategic activity in the firm it provides a tool for classification of strategic activities hitherto missing from business literature and necessary for a comprehensive discussion of the firm.

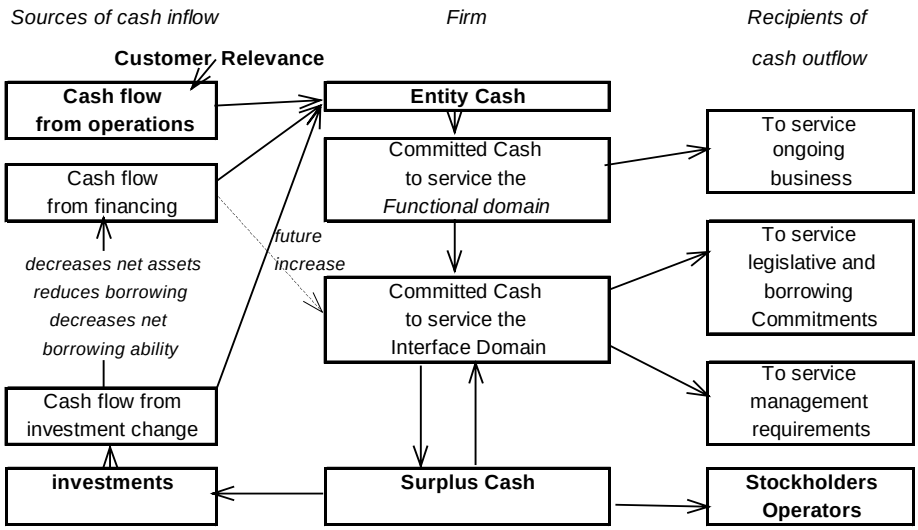
The theoretical roots of the three-domain model come from orientation literature. Orientations adopted by an organisation determine its culture and in turn the information system it selects. Geursen (1998) recognised that different orientations serve different purposes in organisations, but that a number of orientations were required to co-exist if the total requirements of the firm were to be satisfied, even when their cultural drivers were in conflict. Conflict between orientations is resolved by dividing them into two fundamental groups, orientations, such as marketing and entrepreneurship perform generative tasks, supplying the organisation with its cashflows from operations, and others, such as accounting focus on control facilitating the interface requirements of the firm. Geursen (1998) empirically demonstrated that it was valid to conceptualise the small firm as consisting of the functional and interface domains. Furthermore, managers of sustainable firms, especially entrepreneurs, concentrating their efforts on functional cash-generating activities. These managers recognised the existence of interface requirements but delegated as much as possible of this area and its servicing away from them. Furthermore he demonstrated that in the large organisation the Interface domain was split between internal and external demands, thus covering the three stakeholder groups in the organisation

The dynamic cashflow model

The second component model is the cashflow model which identified the dynamics of cashflow in the firm. The model retains the structure of the three domain model described the role of the functional domain as the generator of net cashflows and the interface domain as a distributive function of those net cash flows. The model takes the three sources of cashflow recognised in accounting (cashflows from operations, changes in investments and financing) to reflect the paths, consequences and

outcomes of cashflows through an organisation. The paths reflect the dynamics, interrelationships and consequences of management actions and the implications of these in financial structural terms. The model is as follows:

(figure 2) The dynamics of cashflows and liquidity



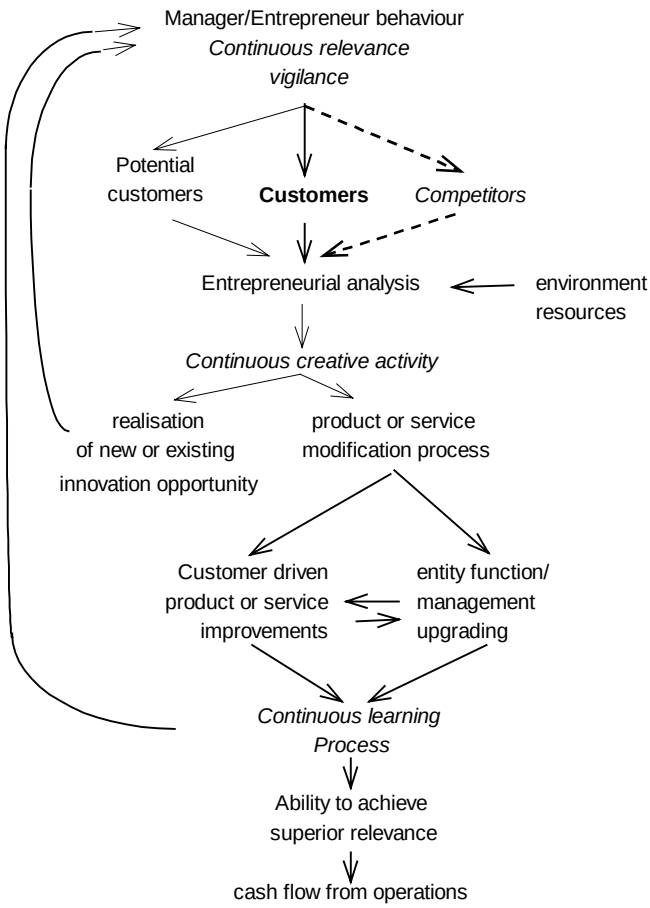
The model in figure 2 goes beyond traditional accounting cashflow models (for example Ingram 1996) in that it portrays cashflow and leveraging structures from the point cash enters the firm till it departs and does the within the three domain structure of the previous model. Furthermore it identifies *surplus cash* as a new aspect in cashflow and liquidity models thus distinguishing between cash to service ongoing requirements and cash over which there is discretionary managerial power. Geursen (1997) identified the presence of this cash as a critical determinant of realised strategic directions in the firm and of its health. Furthermore he demonstrated that the presence of continued *surplus cash* triggered new expansionary strategic initiatives whilst very low levels or the absence of *surplus cash* initiated urgent consolidating strategic activity. A firm's strategic activity thus, fundamentally functions through management's perception of present and future cashflows. The paper identifies that cashflows are fragile and not very predictable when new strategic activities are implementation, hence the importance of existing surplus cashflows from other activities or strong liquidity reserves to maintain liquidity during these periods.

The generative component of the firm and its dynamics

In the third component model Geursen (1998) explored the links between customers and the firm in the entrepreneurial situation. This research indicates that the marketing orientation practiced in the small the entrepreneurial firm is fundamentally different from other firms. It does not conform to the formalised structures identified in marketing literature (see Despande and Farley 1998; Sinkula 1994; Slater and Narver 1995; Narver and Slater 1990; Jaworski and Kohli1993) but functions as a direct relationship between customer and the firm's prime decision-maker. The most critical aspect of the model is the method used to achieve market orientation. Small firm managers and entrepreneurs use direct and two ways communication to proactively interact in a dynamic relationship which is to the benefit of both parties. The customer benefits by having the supplier focused directly on his/her most current

needs. The owner/ entrepreneur benefits by constantly knowing what output will generate operational cash inflows. The system promotes dynamic internal adjustment throughout the firm. Wastage resulting from activity that is not directly relevant to customers becomes noticeable and can be avoided, controlled or reduced. The cash flow or liquidity situation acts as the control, providing the critical reference point for sustainability information. The process can be modelled as follows:

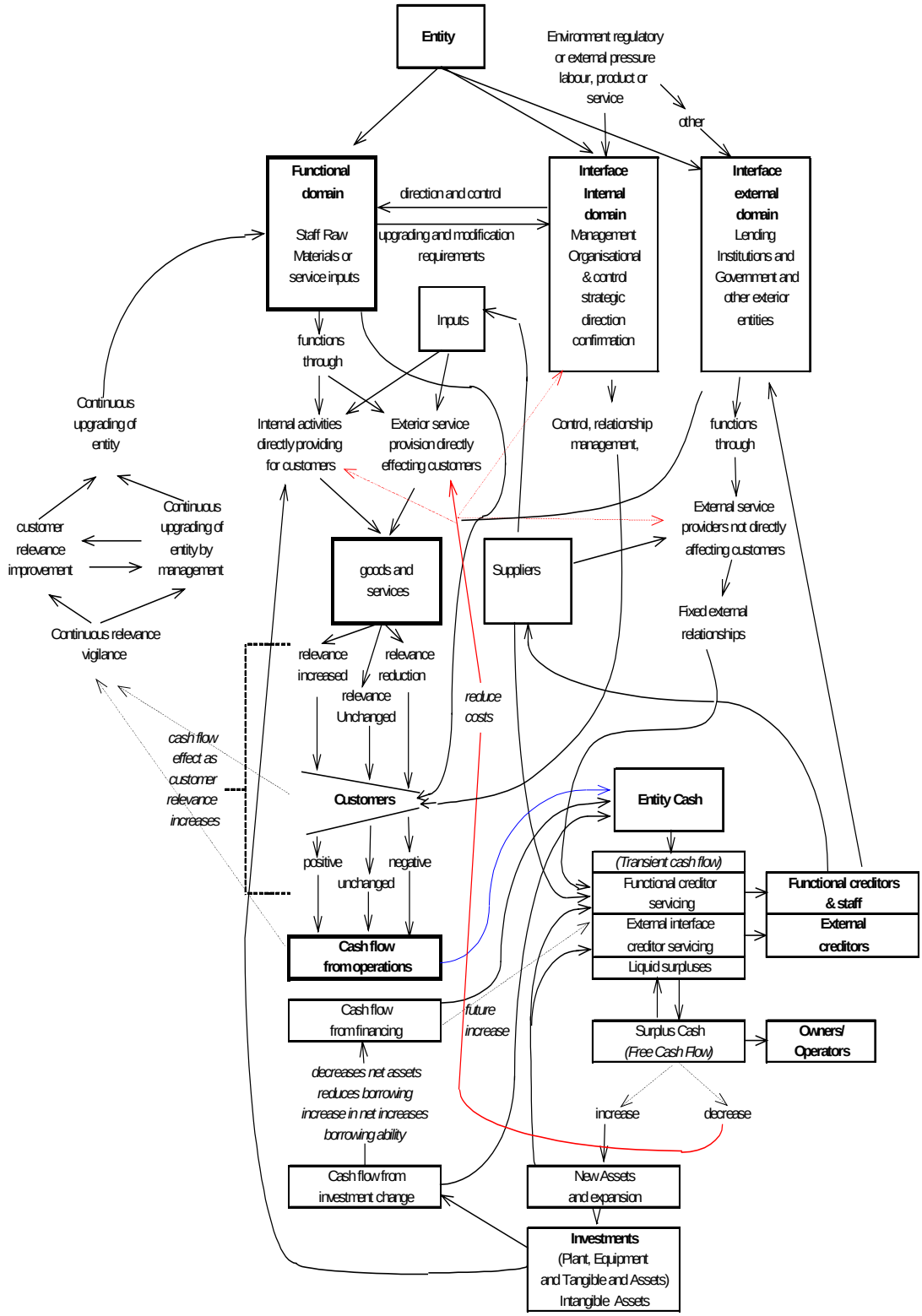
(figure 3) Entrepreneur Market Relevance Model



An Internal Conceptual Model of the Small Firm

The remaining modelling task of this paper is to bring the component models together into an integrated whole. The model in Figure 4 displays the conceptual model of the small business, the purpose of this paper and unites components follows.

(figure 4) A Internal Conceptual Model of the Small Firm



The functional entity produces goods and services. Its relevance to customer's needs essentially determines how the firm's cashflow from operations changes. As customer relevance increases, cashflow from operations increases. As customer

relevance decreases, cashflow from operations is reduced. The dynamics of cashflow are thus evident in the model.

The consequences of changes in different parts and activities are also evident in the model. Research for dynamic cash flow component model indicated that management decisions are fundamentally cashflow perception based. Thus, from the cash accounting perspective, providing expenses are controlled and functional and the interface expenses are less than cash inflows, surplus cash is generated. This cash is identified in the model as "surplus" because it is uncommitted. After subtracting tax requirements an amount is available for discretionary strategic purposes and dynamics of the opportunities presented are indicated in the model.

Consequences come into play when cashflow into the firm is derived from cash changes in investments as asset reductions reduce future borrowing ability and cashflow from financing initiate a future increase for cash requirements to service the additional borrowing. The model therefore reflects a dynamic situation with cashflow from operations as the critical component of free cashflow. It is also evident from the model, and the discussion earlier in this paper, that cashflow based on operational achievement can be used as a surrogate measure of market relevance performance in a firm. It further follows that surplus cashflow status or the expectation of it, acts as a control on strategic activity. When cashflow is positive, growth is encouraged and when it is negative, frugality is encouraged. A side observation about the model is that whilst surplus cashflow generation is strong there is little pressure on the entity for control expenses. But as soon as the situation changes control behaviour is activated and a defined path of reaction is initiated to bring the entity back into balance. The model thus presents a dynamic and proactive view of the internal functions of the small firm.

Evidence of model validity

The final research task in this paper is to provide data that supports or refutes the validity of the model. An instrument was used from which a six-year directional balance sheet could be constructed. Instrument development and testing revealed that respondents were able to recall with reasonable accuracy financial information which provided a directional indication of their balance sheets. Respondents could recall whether sales (revenue) had increased, remained stable or decreased. They could recall this same information for expenses and financing. After piloting, experimentation with the instrument wording and sequence arrangement, it was found respondents could recall the same information for the last five years. It was thus possible to provide longitudinal evidence supporting assessment of how well the system, from which this model is derived, functioned as a dynamic system. The research hypothesis was thus:

> H1. Can it be demonstrated that small entrepreneurial firms who exhibit the behavioural characteristics on which the component models are based survive in the business environment?

Research method

Empirical substance was derived from a random sample (final respondents n=220) representative of Australian small firms. Warrnambool was selected at random from a list reflecting non-urban centres and Melbourne was selected at random from a list of

the major urban cities. The final sample was selected from a listing of all business phone numbers in the Warrnambool and Melbourne regional telephone directories. The sample then selected by the Computer Assisted Telephone Interviewing (CATI) sampling methods and telephone interviewing was used to achieve sample integrity. For example an unanswered number was redialled five times over the next two weeks before being discarded and replaced, thus conforming to CATI procedures (Malhotra 1994). The sample achieved a sampling efficiency of 87.3% of the target sample. A structured questionnaire was administered by telephone to respondents by two trained independent interviewers.

A screening question was included to filter out businesses not conforming to the Australian Bureau of Statistics definition of a small business. The key characteristics of this definition are that manufacturing businesses must have fewer than 100 employees and non-manufacturing fewer than 20. The instrument was administered only to conforming businesses. Characteristics suggested by Beddall (1990) relating to management, ownership and decision-making functions resting with the owners/ managers were recorded and all respondents conformed to these management and ownership criterion. Franchise owners/operators, retailers operating under a banner, or belonging to a group, or any businesses with affiliations that provide it with a market position were excluded. Management in such businesses might not be fully responsible for strategic all key decisions and were excluded from the sample.

A comparison between Australian Bureau of Statistics small business profile and the sample indicate good representation of Australian small business types and structures. The only group not represented in the sample was mining businesses. A detailed correlation study could not be undertaken because comparative data was unavailable on a regional or state basis.

Respondent definition

All respondents in this study were identified as possessing or having demonstrated innovation, autonomy of action and market exposure to qualify them as entrepreneurs. Whilst there is no clear and generally agreed definition of what constitutes an entrepreneur some notable scholars indicate that entrepreneurship requires five behaviours including innovation, autonomy of action and market exposure, competitive aggression and acceptance of personal risk (for example Lumpkin and Dess 1996; Miller 1983; Covin and Slevin 1991). However as Lumpkin and Dess (1996) have argued, not all of these characteristics need to be present for a person to be classified as an entrepreneur.

It should be noted that the sample for this study was strongly skewed towards business survivors. Most respondents (96.4%) had been in business for more than two years; nearly half of them (47%) for more than 10 years. The sample thus reflects a group of small businesses that, by virtue of their length of time in business, can be considered as successful (Beddall 1990; Williams 1989; Storey et al 1990). Most respondents operated businesses which were mainly domestic but a small percentage (3.18%) were both domestic and international. The structure of most businesses (51.36%) was an incorporated structure. A further number (29.09%) operated as a partnership and the balance were unincorporated sole traders. Respondents in the sample indicated a cross section of turnovers, ranging from more than $A10 million (16.1%) too less than $A100,000 (22%). Some 50.2% of the sample had annual turnovers greater $A1 million.

Research findings

Figure 5 provides an insight into sales (revenue) performance of all respondent firms over the five preceding years and expectations for the current year.

Figure 5 Sales (revenue) change over a six year period

Number of years increase achieved over a six period (1990/6)	Probability of increase achievement	Cumulative
0	0.068	0.068
1	0.091	0.159
2	0.232	0.391
3	0.150	0.541
4	0.173	0.714
5	0.045	0.759
6	0.241	1.000

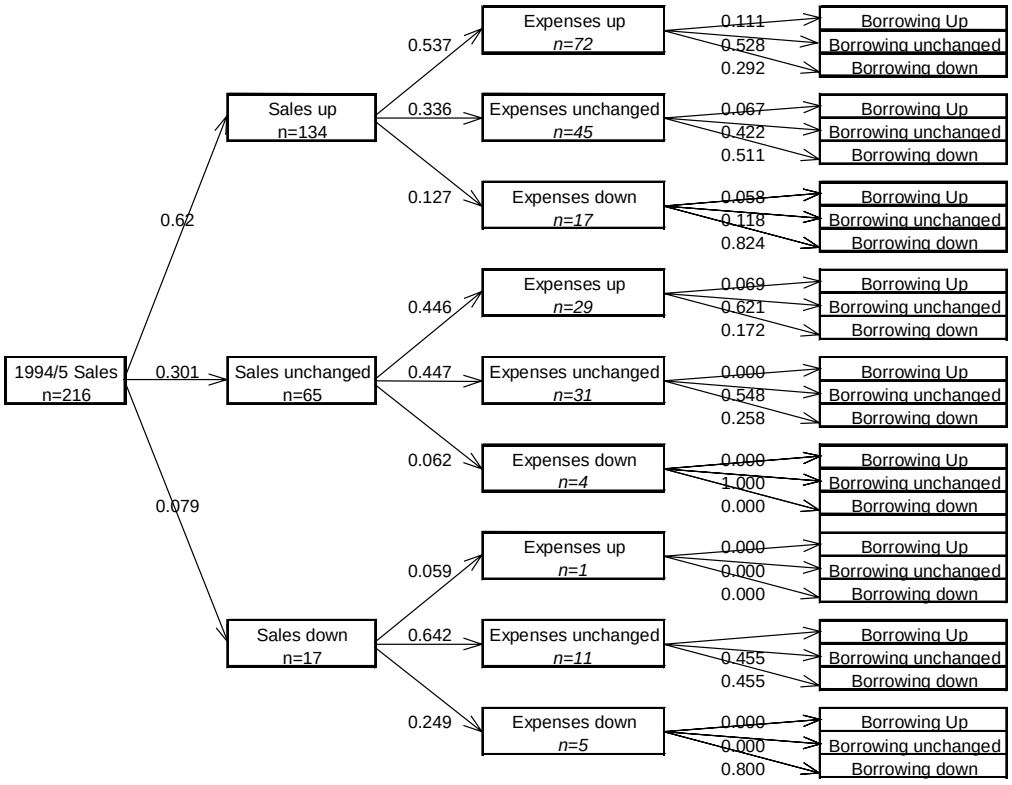
n=220

Figure 5 clearly indicates the achievement of sales growth, and thus, of revenue, by respondents. The sample indicates an active achievement of constant growth (pr uninterrupted pr=.241) with very few firms achieving less than two years of growth (pr=.159). Overall, the data indicates a normal growth achievement of between two and four years out of the six year period with one of the respondents (pr=.241) achieving continual growth.

Figure 5 provides an insight into the consequences of growth on the "health" of the business. Changes in the relationship between the three factors, revenue, expense and financing, were analysed in order to establish whether the financial situation had improved or deteriorated. This measure did not define the extent of the change ("by how much") as in testing and respondents were unable to answer this with sufficient accuracy, especially for the earlier years of the six year period. Data was constructed for one year but comparison with other years indicated a constancy of pattern between the years.

The data in figure 5 identifies that these firms were able to generate sufficient operational cash flows and manage their expenses in a manner that they could continue to meet their creditor commitments, hence achieve sustainability. The main point is that it indicates that small firms, which implemented the decision processes reflected in the models, maintained their viability.

(figure 6) Relationship of sales, expenses and financing for a given year



Note: Probabilities in each group do not add up to pr=1 because the few incomplete questionnaires were included in the data and treated as a "no response"for that section. This group is not seperatly identified but can be calculated by substracting the sumation of each group from 1.

The particular relationships achieved between sales, expenses and borrowing indicate a proactive management process. Growth in sales (pr =.609) can be achieved without increasing expenses (pr=.463) and even where expenses go up, it is unlikely financing increases (p r=.820). Unchanged sales leads to a loosening of expense control (pr<. 446, pr =.447) and sales decreases lead to consolidation behaviour (this last observation should be treated with caution because only seventeen respondents experienced negative sales' growth in the year of analysis).

The table in Figure 6 clearly demonstrates that the system used by the respondents to manage their firms was achieving sustainable business outcomes. The data collected for this question was completely independent and not used in any other piece of analysis. Since the sample conformed to robust random sampling methodologies it is a valid <u>indication</u> that the system the model portrays is indeed, an internal conceptual model of the small firm, hence the null hypothesis is rejected and H1 cannot be rejected.

<u>Some conclusions and implications.</u>

In essence the model presented in this paper is very compatible with extensions of Adam Smith's classic technological model of the firm, which is at the base of microeconomic rationality and entrepreneurship. Unlike Smith's model the research for the development of this model (Geursen 1999) indicates that owners of firms, in contemporary times, are not free agents able to structure a firm purely on production efficiency criteria. Today firms have "social costs" such as management, supporting staff and demands of society to service. The overall model in figure 4 provides a

framework for analysis of activity and their consequences in the firm. The model in figure 1 enables the classification of effort within the organisation and the understanding of the structural dynamics by differentiating between net revenue generating activity and its distribution. The model recognises that distribution cannot occur without the generation of net revenue. Furthermore it permits distinction in costs between those which directly relate to generation of wealth and those that distribute that wealth. Costs to service capital are considered as a social cost belonging to the external interface group. Servicing such costs is directly dependent on the performance of the functional domain for liquidity, hence stability only exists if the following is true:

$$\text{(Condition 1)} \qquad \Psi(f) \geq (CIi + CIe)$$

Where

Ψ = Net cash flow
f = Functional activity
C =Servicing costs
Ii = internal interface
Ie = external interface

Furthermore, there is a dichotomy in the structure of power between the domains. Despite the dependence of *Ii* and *Ie* on *f* on Ψ to fund these activities, power over the firm is held in the order of *Ie*, *Ii* and *f*, hence the power relationship is in reverse to the generative relationship. This dichotomy is responsible for the cyclical differences which can be observed in the history of firms. The explanation being that *Ie* and *Ii* commit expenditure on the basis of Ψ *expectations* of *f* and if these are not met *f* delivers Ψ at a level of:

$$\text{(Condition 2)} \qquad \Psi(f) < C(Ii) + C(Ie)$$

The firm is not in a sustainable mode in condition 2 and must return to equation 1. It can borrow to overcome its imbalance in the short term or it can restructure by cutting its costs. Firms attempting to achieve re-establishment of the equation 1 status by reduction of *Ii* or *Ie* either failed to recover or recovered only for a short period (Geursen1999). This was because the power structure encouraged that some savings be forced on *f* costs and these led to reduction in customer value leading to reduce cashflows from operations and a lower Ψ (Geursen (1997). The only exception to this observation is when the firm has a functional domain consisting of a multiple of product or service units and revenue of an individual unit is less than its *f costs*, in this situation Ψ is increased by cutting that product of service. Recovery from cycle troughs occurs only when action is taken which increases Ψ to a level that equation 1 is re-established (Geursen's 1998 and 1999). Furthermore the model in figure 2 indicates sustainability exists when a firm can maintain a positive balance between net revenues from the functional domain after servicing the expectations of the interface domains.

Implications of the model on entrepreneurship theory

From the model it might be argued that entrepreneurship is an activity concerned with activity of (*f*), the functional domain to achieve Ψ. Entrepreneurs concentrate their efforts in this area to achieve their net revenue effect by close dynamic customer

interface (Geursen 1998a), hence the relationship between marketing and entrepreneurship. Yet there is other entrepreneurial activity is clearly not part of (*f)* but focused on *Ii* and *Ie*. Burgelman (1984) identified the presence of such activity as intrapreneurship but a clear distinction between entrepreneurship and intrapreneurship has not been well articulated.

The model presents a new perspective which facilitates the differentiation between these two activities. It argues that intrapreneurship is activity which takes place in *Ii* or/and *Ie* and that whilst the outcomes might be the generation of wealth for individuals the effect on the future of the firm is entirely different to the effect of activity in the functional domain. In the long term sustainability is not achieved. For example a firm owner may at a particular stage not have any traditional tangible assets, for example an Internet company where the principal asset is the intellectual property of its software. It may be trade in condition 2 but it can continue to trade only as long as it can service its debts, which it does by cash generating activity in the *Ie* domain, in particular, by selling sufficient stock to support its inadequate Ψ or by increasing its borrowing. Hence such firms are only sustainable as long as investors believe the future underlying, but speculative, cash flows are perceived as sufficient to continue investment support. An important implication of such activity is that the firm will fail very quickly if cash flows from *Ie* cease to be available unless the firm can return to condition 1 immediately (as shown by the Australian "entrepreneur" collapses in the late 1980's such as Bond Corporation Ltd.). The firm can re-establish stability by activity in *Ii*, such as downsizing but as Geursen (1999) indicates with small firm research, recovery of sustainability depends on growth in Ψ. Hence it is argued that the model identifies the important fundamental difference and value between *intrapreneurship* and *entrepreneurship,* whilst accepting that both generate wealth. Furthermore, by articulating that entrepreneurship rests in the functional domain it establishes the clear and direct link between entrepreneurship and marketing because both are concerned with the generation of Ψ from *(f),* operating in the functional domain.

The final observation about the three-domain model of the sustainable firm is that it appears to apply across all economic structures and can thus be characterised as a general model of the sustainable economic unit. For example:

> *The individual*
>
> An individual needs income, spend income on themselves including immediate family/friends is required to contribute to societal costs- these are the three domains of the model and the individual is only sustainable as an economic unit as condition 1 prevails.
>
> *The firm*
>
> The fit with the model has been explained earlier in this paper where it was noted that it was sustainable in the longer term only as long as condition 1 is maintained.
>
> *A non-profit organisation (eg. Art museum or state operated University)*
>
> Fundamentally fits the model although if there is financial support by government this can be treated as positive cash inflows in *CIe*, hence the model still applies.

An economy

In an economy the model applies because there is governments need income which they use to fund themselves and support societal services, hence the model structure applies. Furthermore the model can also be used to evaluate economic dynamics by recognising that many industries are dependent on other industries for existence of cash flows. For example, Ψ in law firms comes from the advice to clients so the provision of advice is its functional domain. For the client the advice might be necessary to do business but it is a reaction to a factor in *Ii* or *Ie*. It thus follows that the law firm is dependent on Ψ *(f)* of the client for existence. Applying this logic to economic analysis the model appears to provide a basis for isolating the driver of economic activity by indicating that there independent and dependent structure in an economy which are identifiable.

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DEVELOPMENT AND STUDY OF A TAXONOMY OF STAGE CONFIGURATIONS OF THE LIFE-CYCLE, APPLIED TO THE SME OF THE BEIRA INTERIOR REGION

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ABSTRACT

Several theories and models have been proposed over the years, attempting to explain the organisational life-cycle phenomenon. However, not enough attention has been given to the basis of construction of a life-cycle stage. In this study it is proposed that each life-cycle stage is composed of unique configuration of variables related to the firm context and structure. A cluster analysis was applied to a sample of 65 firms belonging to the manufacturing industry of the Beira Interior region, in order to obtain a taxonomy of configurations of development stages. This study suggests a sequence of four growth stages: Birth, Expansion, Maturity and Diversification and one stage of Stagnation or Decline.

INTRODUCTION

Several researchers [1, 2, 3, 4, 5] have been suggest that structure, development and behaviour of the organisations can be predictable through life-cycle models. This models will may help to understand the growth phenomenon complexity and the effects that provoke in the firm [6, 7]. All the firms, in your development, travel all over stages distinct each one with the characteristics owners [2, 3, 8]. An understanding of life-cycle phenomenon firm and the associated management imperatives could aid entrepreneurial founders through the uncharted course of firm growth [9].

The most part of the life-cycle literature is based in static characteristics of the organisations. As suggest Kimberly and Miles [10], don't know many about the structure evolution and process or pattern of decision making that as organisations try progress in their life-cycle, since creation to maturity. The works made by Adizes [1],Greiner [2] and Lyden [5] indicate that occur changes in the organisations, following a predictable pattern that can be characterised by development stages. This stages follow a wide series of strategies, structures and organisational activities [4, 6]. While numerous theories and models have been proposed in an effort to explain the life-cycle process, there has been remarkably little effort to validate these empirically [11, 6].

We intended with this investigation, study the small and medium sized firm to light of the acquaintance of life cycle theory with the aim objective test the empirical existence of development (or patterns) stages. Thus this work represents a first effort in related at study and development of a empirical taxonomy of life cycle stages applied to small and medium sized firm of the Beira Interior region.

THEORETICAL CONSIDERATIONS

Attend this considerations, three important questions will be addressed.

1. LIFE-CYCLE CONCEPT

In spite of number of stage-based models of organisation growth which have been proposed over the years, there has been remarkably little attention paid to the basic construct of life-cycle stage. In review of the life-cycle literature, we found no explicit definition about life cycle concept. Several authors [1, 11, 6, 12] in their models talked explicitly of life-cycle stages, while others used terms such as growth stages [13, 14, 15] or development stages [16, 13, 6]. However it found no effort to distinguish between these terms in the literature.

Table 1 presents a comparison of authors' statements regarding the nature of life-cycle stages and the specific dimensions utilised to describe stages and to differentiate between various stages of development.

The life-cycle stage construct appears to be a multidimensional phenomenon. In each of the life-cycle models reviewed, authors described stages in multidimensional terms. While there is considerable variability between models, all included some dimensions related to organisation context and organisation structure. Common contextual dimension include: organisation age, size, growth rate, and focal tasks or challenges faced by the firms. Common structural dimensions include: structural form, formalisation, centralisation and vertical differentiation, the number of organisation levels. It seems to exist an interrelation through descriptive dimensions used in the stages characterisation. For example, Miller and Friesen [11] referred to "integral complementaries" among stages dimensions. Galbraith [13] noticed that each one of these dimensions is connected to the other. In this way, the life cycle stages can best be characterised in terms of what Hanks et al. [9] call configurations: organisational structures, production systems, information processing, strategies and

environments, all tend to influence each others, of such manner that they gives rise to a small number of extremely common configurations.

TABLE 1- DESCRIPTIVE DIMENSIONS OF SELECTED LIFE-CYCLE

Model/Nature of stages	Contextual Dimensions	Structural Dimensions
Adizes (1991) Organisations have life-cycle just as living organisms do; they go through the normal struggles and difficulties accompanying each stage of the organisational life-cycle and are faced with the transition problems of moving to the next stage of development. Organisations learn to deal with these problems by themselves or they develop abnormal diseases which stymie growth – patterns that usually cannot be resolved without external professional intervention.	Age; size; normal problems and transitions.	Structural form; formalisation of policies and procedures; leadership characteristics; depth of management; diversity and complexity.
Churchill e Lewis (1983) Delineates five stages of development. Each stage is characterised by an index of size, diversity and complexity and described by five management factors: managerial styles organisational structure, extent of formal systems, major strategic goals and the owners involvement in the business.	Age; size; growth rate; major strategies	Management style; organisation (form and levels) extent of normal systems and business/owner relationship.
Galbraith (1982) The stage of development and the business idea determine the basic task to be performed. For different tasks, different structures, decision processes, reward systems and people are needed in order to execute that task. Each of these dimensions is connected to the others.	Age; size; growth rate; task	Structural form; specialisation level; reward system; formalisation; centralisation leadership style.
Greiner (1972) Growing organisations move through five distinguishable stages of development, each of which contains a relatively calm period of growth that ends with a management crisis. Each evolutionary period is characterised by the dominant management style used to achieve growth, while each revolutionary period is characterised by the dominant management problem that can be continued.	Age; Size; industry growth rate.	Organisational structure; formalisation level; top management style; control system; management reward emphasis.
Kazanjian (1988) The firms faced strategic operational problems from the time of product conceptualisation through organisational maturity. Further, some of these problems seem to have been more dominance seemed to exist. The particular problems faced at a given time appeared to be strongly associated with a firm's position in a particular stage of the growth.	Age; size; growth rate; dominate management problems.	Structural form; formalisation; centralisation; top management composition.

(continue)

Models/Nature of Stages	Contextual Dimensions	Structural Dimensions
Miller e Friesen (1984) A review of literature on the organisational life-cycle disclosed five common stages: birth, growth, maturity, revival and decline. Each stage would manifest integral complementarities among variables of environment ("situation"), strategy and structure and decision making methods; that organisation growth and increasing environmental complexity would cause each stage to exhibit certain significant differences from all other stages along these four classes of variables.	Age; number of employees; size (relative to competitors) concentration of ownership; stakeholder influence; environmental dynamics, hostility and heterogeneity; strategy variables reflecting: - extent and frequency of product innovation; - diversification; - geographical expansion; - marketing orientation.	Basis of organisation; participate management sophistication of information systems; performance controls; action planning; environmental scanning; formal controls; internal communications; centralisation of power; delegation for routine decisions; technocratisation; resource availability; differentiation; decision-making style.
Quinn e Cameron (1983) Changes that occur in organisations follow a predictable pattern that can be characterised by developmental stages. Theses stages are (1) sequential in nature; (2) occur as a hierarchical progression that is not easily reversed; and (3) involve a broad range of organisational activities and structures. A variety of bases of organisation members to organisational structures and environment relations.	Age; size; criteria of organisational effectiveness.	Structural form; formalisation; centralisation; leadership; culture.
Scott e Bruce (1987) As a small business develops it moves through five growth stages, each with its own distinctive characteristics. Because the transition from one stage to the crisis or another. Crises tend to be disruptive and the problems of change can be minimised if managers are proactive rather than reactive.	Age; size; growth rate; industry stages; key issues: - source of finance; - cash generation; - major investments; - products/market scope.	Structural form; formalisation of systems and controls; top management role/style (centralisation).
Smith et al. (1985) Models of life cycle stages presuppose that there are regularities in organisational development and that these regularities occur in such away that the organisations developmental processes lend themselves to segmentation into stages or periods of time.	Age; size (sales); size (employees); growth rate; top management priorities.	Structural form; reward system (formalisation); centralisation; top management composition.

SOURCE: Hanks et al. (1994: 38)

These configurations may represent common organisation structures, scenes of strategy, and even common developmental or transitional sequences. In this context, it was defined life cycle stage as an unique pattern of relative variable to the context and structure organisational. This definition is also supported by [13] who used the term reconfiguration to characterise the transition from one stage to the next.

2. LIFE-CYCLE MODELS

The different cycle life models presented (Table1), are supported in a set of factors to explain the alterations of the organisations characteristics. Each one from nine models can be organised on a " Summary Model " (Table 2) with five stages: Birth, Expansion, Maturity, Diversification and Decline.

As illustrated in Table 2, there is a fairly broad range in the number of stages specified as the organisation emerges from birth, trough maturity and eventually decline. Smith et al. [12] suggest a three stage model. Kazanjian [14] and Quinn and Cameron [6] consider a four stage model. Churchill and Lewis [16], Galbraith [13], Greiner 2], Miller and Friesen [11] and Scott and Bruce [15] theorised a five-stage model. Finally, Adizes [1] proposed the most complex model, suggesting ten life-cycle stages.

TABLE 2 - COMPARISON OF LIFE CYCLE MODELS: NAME AND NUMBER OF STAGES

.

MODELS	Start-Up Stage	Expansion Stage	Maturity Stage	Diversification Stage	Decline Stage
Adizes (1991)	1. Courtship 2. Infancy	3. Go-Go 4. Adolescence	5. Prime 6. Stable		7. Aristocracy 8. Early Bureaucracy 9.Bureaucracy 10. Death
Churchill e Lewis (1983)	1. Existence 2. Survival 3.Success-Disengagement	3. Success-Growth 4. Take-Off	5. Resources Maturity		
Galbraith (1982)	1. Prototype 2. Model Shop	3. Start-Up/Volume Production	4. Natural Growth	5. Strategic Maneuvering	
Greiner (1972)	1. Creativity	2. Direction	3. Delegation	4. Coordination 5.Colaboration	
Kazanjian (1988)	1. Conception & Development 2. Commercialisation	3. Growth	4. Stability		
Miller e Friesen (1984)	1. Birth	2. Growth	3. Maturity	4. Revival	5. Decline
Quinn e Cameron (1983)	1. Entrepreneurial	2. Collectivity	3. Formalisation	4. Elaboration of structure	
Scott e Bruce (1987)	1. Inception 2. Survival	3. Growth 4. Expansion	5. Maturity		
Smith et al (1985)	1. Inception	2.Alto -Growth	3. Maturity		

SOURCE: Hanks et al. (1994: 40)

The selection of five stages in Table 2, was made in the interest of parsimony and ease of comparison. All models include one or more stages related to organisation birth, expansion and maturity.

All except four models [1, 16, 14, 12] include one or more diversification or revival stages. Only two investigators [1, 11] include a decline stage or stages in their life cycle model. Exclusion of decline stages in the majority models, can be attributed, likely to two inherent characteristics of decline organisation. First one, refers to the impact of decline organisation structure and systems is far less predictable than changes associated with growth [9]. Second, the onset of organisation decline may actually occur at any stage of the organisation life cycle [11].

While the models suggest a fairly consistent pattern of organisation growth, there is wide variance as to the specific number of stages.

3. CHARACTERISTICS OF LIFE-CYCLE STAGES

Several investigators have emphasised, for only times, sets of organisational characteristics and life-cycle models [6].Table 3 presents a synthesis of the nine models by dimension and stage.

As illustrated in Table, the organisations are theorised to evolve through five general stages: Birth, Expansion, Maturity, Diversification, and Decline. As the organisations evolve through various life-cycle stages, they are theorised to increase in age and size.

Growth is theorise to be highest during the growth stage slow during the maturity stage and decline during decline stage. The structural forma goes from simple, to functional to divisional. The organisation becomes increasingly more formal and specialised, and the decision making becomes less centralised as the organisation grows.

TABLE 3 – LIFE-CYCLE STAGE CHARACTERISTICS: COMMON PATTERNS

DIMENSION	Start –Up Stage	Expansion Stage	Maturity Stage	Diversification Stage	Decline Stage
Age	Young.....	.....	.....	Older	Any age
Size	Small.....	.....	Large.....	LArgest..... .	Declining
Growth Rate	Inconsistent	Rapid positive	Slow growth	Rapid positive	Declining
Structural Form	Undifferentiated; Simple	Departmentalised; Functional	Departmentalised and Functional	Divisional	Mostly Functional
Formalisation	Very informal, personal, flexible; Few policies	Formal systems begin to emerge, but enforcement is lax.	Formal; Bureaucratic; Planning & Control systems are enforced.	Formal, Bureaucratic	Excessive Bereaucratisation
Centralisation	Highly centralised in founder	Centralised: Limited delegation	Moderately centralised.	Decentralised.	Moderately centralised
Business Tasks	Identify niche; Obtain resources; Build prototype; Set up task structure	Volume production & distribution; Capacity expansion; Set up operating systems.	Make business profitable; Expense control; Establish management systems.	Diversification ; Expansion of product market scope	Revitalisation; Redefinition of mission and strategy

SOURCE: Adapted from Hanks et al. (1994), p. 42.

TAXONOMY STUDY OF ORGANISATIONAL LIFE-CYCLE: BEIRA INTERIOR REGION

OBJECTIVES AND METHODOLOGY

Much has been written through the years, about organisational life cycle. However little attention has been given to the foundations of life cycle stages.

As illustrated in the preceding section, there is a high level of similarity among life-cycle models, particularity when viewed at a very general level. However upon close examination, a number of incongruities emerge. For example, models do range from three to ten theorised stages (Table1). This tends to create some disparity in stages descriptions between models. Differences between models can be traced to two methodological problems. First, most models of the organisation life cycle are conceptually rather than empirically based. In the absence of empirical analysis, a plethora of conceptually based models have emerged. Which of these models best depicts organisational growth? Lacking systematic empirical study, this questions remains unanswered.

Hanks et al. [9] suggests that a form to exceed the limitations of the conceptual studies and to get greater empirical severity is the use of taxonomies. It is proposed in this study that each life-cycle stages consists of a unique configuration of variables related to organisation context and structure. If organisations evolve through a sequence of stages, as theorised, then in a cross section of organisations, several stages should be represented.

Identification of these stages should therefore be possible by empirically clustering organisations based on common configurations of these dimensions. Thus, fundamental issue explored in this study is the validity of this configurational definition of life-cycle stages. Do distinct configurations emerge in the analysis? Does the general pattern of configurations reflect a sequence of developmental stages? Affirmative answers to these questions will lend support to the configurational definition of life-cycle stage.

Sample

The population studded was SME (Small and Medium sized Enterprise) of the Beira Interior Region from Portugal. Data were collected by questionnaire during Spring and Summer of 1996. Questionnaire were mailed to the presidents of 300 firms. Completed questionnaire were received from 65.

Variables Definition

Two types of measures were used in the analysis. The first type, designed as "clustering variables" includes eight measures of organisation which were used to derive the growth stage taxonomy. Each of these dimensions had been identified in the literature as a relevant descriptions life cycle stages (Table1). The second type includes four additional "descriptive variables" used to aid in interpreting the derived taxonomic stage configurations [18, 9]. To prove the statistics and significance of the results, an analysis of variance ONEWAY was used (ANOVA). Discriminate analysis was used to verify if the firms were classified well.

Clustering Variables

In the clusters analysis were used structural variables. The *contextual variables* included: the *age*, the *size* and *rate growth* . Organisational Age (*Age*) was calculated by subtracting the year the firm was founded, which was self reported by respondents, from 1996, the year data were collected. Organisation Size (*Size*) was measured by the logarithm of the organisation's reported total employment at the end of the 1995 fiscal year. The Growth Rate

measure (*Employee Growth2*) reflects organisation growth for the firm's most recent year of performance. It was calculated, utilising self-reported employment data, based on the following formula:

$$\text{Employee Growth2} = \frac{\text{(Total Employees 1995 - Total Employees 1994)}}{\text{Total Employees 1995}}$$

This measure of growth, was used because it allowed us to overcome a limitation associated with traditional growth measures, and thus retain new firms in the analysis[1]

Structural Variables, used to derive the taxonomy included measures of *vertical differentiation*, *structural form*, *formalisation*, *specialisation*, and *centralisation*. Vertical differentiation (*Levels*) consists of the total number of organisation levels. Respondents were asked to count the number of levels in the longest line between direct workers and the organisation chief executive, including both of these levels.

Structural Form, was self reported by respondents based on brief descriptions. The structure variable was coded as follows: simple structure, 1; by function, 2; by divisions, 3; and other, 4.

Formalisation was operationalised using scale of eleven items. The first tem items used a 7-point Likert-type scale, ranging from strongly agree to strongly disagree. The eleventh item measured the formalisation of the decision-making process in the organisation based on Mintzberg's [19] entrepreneurial/professional dichotomy of the decision making.

The *Specialisation* is adapted from Hanks et al. [9] Respondents were given a list of 20 functional areas and were asked to check those in which they had at least one full-time Employee. The item is scored by counting the number of functions checked.

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[1] The more tradicional growth formula, designated in this article as Employee Growth1, and presented later as a "descriptive variable" is as follows:

$$\text{Employee Growth1} = \frac{\text{(Total Employees 1994 - Total Employees 1995)}}{\text{Total Employees 1995}}$$

Centralisation was measured through an adapted from Hanks et al. [9]. Respondents were given a list of five decision issues. They were then asked to indicate the level of management that must approve the decision before legitimate actions may be taken. The scale is scored by adding up the total of all five responses. A high score on this scale indicates high level of centralisation in the firm.

Descriptive Variables

While not used in the derivation of the taxonomy, four additional variables are subsequently profiled to aid in interpretation of the derived cluster set. These include *Total Sales*, *Sales Growth*, *Total Employment*, and *Employee Growth1*. *Total Sales* consist of annual revenues for fiscal year 1995. *Sales Growth* was calculated, using self-reported data, based on the following formula:

$$\text{Sales Growth} = \frac{\text{(Total Sales 1995} - \text{Total Sales 1994)}}{\text{Total Sales 1994}}$$

Total Employment consists of the total number employed by the firm at the end of 1995. The fourth descriptive variable is the Employee Growth1, measure which was explained above.

PRESENTATION AND DESCUSSION OF THE RESULTS

Exploratory cluster analysis was utilised to determine if life-cycle stage configurations could be identified based upon underlying patterns in the data.

An aglomerative hierarchical method that used Ward's [19] criterion was employed in the analysis. The appropriate number of clusters was determined based on the following criteria. First we examined the results of the Ward's [9] method application on the dendrogram form. Second, we compered the number of the clusters with fusion coefficient. It was observed that six groups were relativity small and aid little additional information to five groups solution. Thus, it was selected the five groups solution as optima.

To verify differences in the clusters mean to each of the eight individual variables multivariate analysis of variance was conducted. Dependent variables included the contextual an structural variables utilised to form the cluster groups. Independent variables in the analysis were the derived life-cycle stages clusters. An F-test was performed to verify that group centroids were significantly different. This followed by a series of multivariate

analyses of variance with the life-cycle stage cluster as dependent variables. Duncan test was applied to determine the statistical significance of differences between cluster mean values for each variable.

TABLE 4 – CLUSTER ANALYSIS RESULTS AND DESCRIPTIVE VARIABLES - ONEWAY*

	CLUSTER 1 (N = 24)		CLUSTER 2 (N=13)		CLUSTER 3 (N=15)		CLUSTER 4 (N= 7)		CLUSTER 5 (N=5)		ONE-WAY	
	Mean	S.D.	Mean	S.D.	Mean	S.D.	Mean	S. D.	Mean	S. D.	F Value	P<
CLUSTERING VAR.												
Size (log.)	1,21	0,42	1,44	0,33	2,20	0,38	1,48	0,33	1,26	0,42	13,88	0,0000
Age	6,67	0,45	12,46	6,53	16,0	8,56	44,86	17,09	16,2	8,81	18,74	0,0000
Employee$_2$ Growth	0,05	0,25	-0,04	0,18	0,22	0,10	-0,15	0,19	-0,77	0,43	14,70	0,0000
Structural Form	1,08	0,28	2,15	0,38	2,13	0,64	2,71	0,95	2,0	0,0	21,76	0,0000
Levels	2,33	0,76	4,0	1,41	4,27	1,03	4,71	1,49	3,4	1,14	10,98	0,0000
Specialisation	2,04	1,55	4,69	2,36	6,0	2,94	8,8	3,34	4,8	1,10	19,06	0,0000
Centralisation	20,17	1,01	15,46	2,5	14,4	1,3	12,29	2,81	19,4	1,95	15,82	0,0000
Formalisation	26,92	10,06	32,78	8,16	33,57	9,73	39,2	11,35	40,0	8,19	2,86	0,0310
DESCRIPTIVE VAR.												
Sales (10^6 Esc.)	157,6	185,3	143,3	151,6	627,9	565,2	187,3	143,1	123,7	202,5	N.A	N.A
Total Employees	16,33	11,29	27,62	20,49	159,6	124,44	30,6	18,92	18,29	12,96	N.A	N.A
Growth$_1$ Employee	0,05	0,22	-0,01	0,17	0,03	0,10	-0,11	0,14	-0,41	0,13	N.A	N.A
Sales Growth	0,04	0,23	0,09	0,3	0,15	0,31	0,18	0,18	-0,19	0,19	N.A	N.A

Nº of firms in the sample: 64
* P < 0,05
N.A = Not Applicable

Canonical discriminant analysis was performed to examine the specific differences between clusters. A number of canonical discriminant functions can be identified, and differences between clusters can be analysed based on loadings on the canonical discriminant functions. To aid in interpretation of clusters and assess their validity, clusters were plotted along the first two discriminant functions [9].

Canonical discriminant analysis of the five groups and eight variables was conducted. Four canonical discriminant functions were significant in differentiating among the clusters ($p<0.05$). Variables with the highest absolute loadings on the first discriminant function were age and structural form with loadings of 0.39876 and 0.58637 respectively.

TABLE 5 CANONICAL DISCRIMINANT FUNCTION LOADINGS

VARIÁVEIS DE CLUSTERS	Function 1 (Organisation)	Function 2 (Complexity)	Function 3 (Maturity)	Function 4 (Dynamism)
Size (log.)	0,03617	**0,62313**	0,14468	-0,28315
Age	**0,39876**	-0,24372	**0,53841**	0,15774

Employee Growth2	-0,18323	0,29341	0,07120	**0,89845**
Structural Form	**0,58637**	0,13402	0,05927	-0,08628
Levels	0,34550	0,32586	-0,08585	-0,10511
Specialisation	0,35735	**0,54083**	0,21118	-0,27365
Centralisation	-0,28246	-0,04141	**0,64868**	-0,28263
Formalisation	-0,2049	-0,02528	0,10100	-0,05191

Based upon these loadings, this function can be labelled “organisation” . High-loading variables on the second function include size and specialisation, with respective 0.62313 and 0. 54083. This discriminant function appears to reflect “complexity”. Variables with high loadings on third canonical discriminant function include age and centralisation with loadings of 0.53841 and 0.64868. We label this function “maturity”. The last one function was labelled “dynamism” because presents as high loading the Employee growth variable with 0.89845.

Cluster centroids were computed and are plotted along the first two discriminant functions in Figure 1.

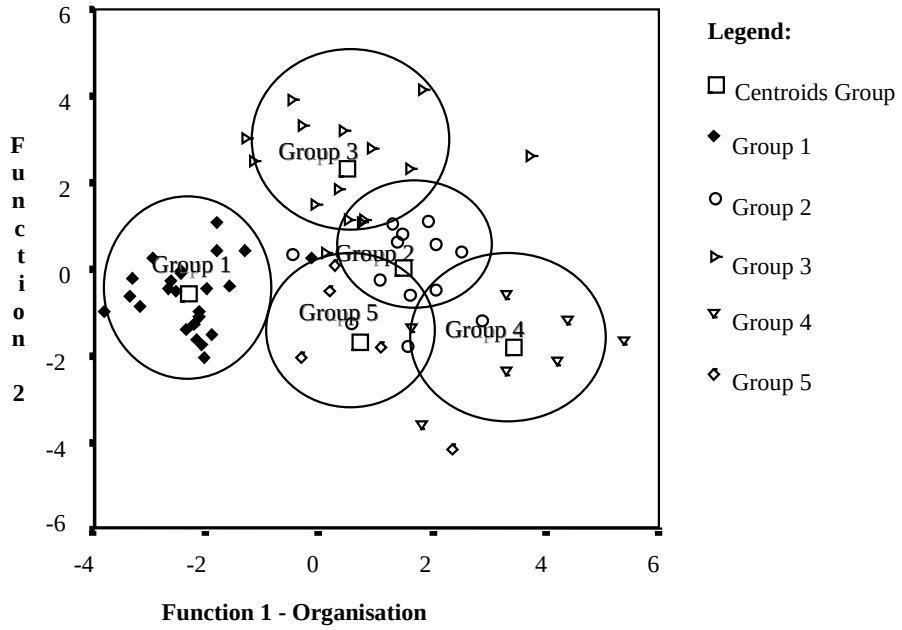

FIGURE 1- PLOT OF CLUSTERAND GROUP OVERLAPS: LUSTERING VARIABLES

This plot illustrates differences between cluster groups. The five cluster groups are generally tight and well separated, with some overlap. Clusters 1, 2, 3 and 4 portray four levels of organisation (discriminant function 1), Cluster 1 being the most young (age) and least complex (structure), and Cluster 4 being the most older. Clusters 3 and 5, while comparable in organisation, differ in complexity (Discriminant function 2). This one tend to be more specialised and more complex (in size) than Cluster 5.

RESULTS DISCUSSION

It was proposed in this study that life-cycle stages could be defined and operationalised as unique configurations of organisation context and structure. The results of the study provide general support for this proposition. Five distinct configurations were identified in the cluster analysis. While the cross-sectional nature of this study limits our ability to reach definitive conclusions as to the sequencing of stages, the derived taxonomy suggests a sequence of five developmental stages, characterised by clusters 1, 2, 3, 4 and 5.

As illustrated in Table 4, annual revenues and organisation size increase incrementally across clusters 1 through 4. Structure changes from primarily simple (cluster 1) to functional (cluster 2 and 3) to partially divisional (cluster 4). The number of organisation levels (Levels) increases incrementally across the growth stages ranging from 2,33 (cluster 1) to 4,71 (cluster 4). Formalisation and specialisation increase across the stages, while centralisation displays a declining pattern. A brief discussion of each of these configurations is presented below.

Cluster 1: Stage I

Cluster 1 consists of young, small firms. The mean age is just over six years, annual sales average near $ 157.600, and mean employment is 16,33 employees. The basis of organisation structure is simple (1,08) with a mean of 2,33 organisation levels. The organisation is highly centralised (20,17) and quite informal (formalisation = 26,92). Firms at this stage employ a mean of 2,04 specialised functions. Based upon these characteristics, this configuration to represent a Birth stage of development (see Table 3). The firms are relatively young, small, highly centralised and informal.

Cluster 2: Stage II

Stage II consists of firms that are slightly older and larger than firms in Stage I (Table 4). The mean age is 12,46 years, mean employment is 27,62 employees, and mean sales are approximately $ 143.000. Firms in this stage have generally adopted a functional basis of organisation (structure =2,15). Organisation decision making is still very centralised (15,46), but less so than in Stage I, and organisation systems are a little more formal than in

Stage I (Formalisation = 32,78). Compared to Stage I firms, they have an additional organisation levels (Levels = 4,0) and 5 specialised functions. When compared with stage descriptions identified in Table 3, this configuration appears to represent an expansion stage of development.

Cluster 3: Stage III

Stage III firms have a mean age and size more high than clusters I and II. Employ a mean of 159,6 employees, and have average annual sales of over $627.000. Firms in this stage are still growing, but not quite as fast as firms in Stage II. Mean sales growth is 15% and mean employment growth is 22%. Firms in this adopted a functional structure and reduced level of centralisation. Formalisation is high (33,57). Firms at this stage employ a mean of 6 specialised functions. When compared with characteristics identified in Table 3, this cluster appears to represent a maturity stage of development.

Cluster 4: Stage IV

Observing the results of the cluster analysis (table 4) we verify that cluster 4, have age mean of 44,86 years, employing 30,6 employed and the annual revenue is $187.300. Sales growth is 18%. This firms present 4,71 organisation levels and 8,8 specialised functions. While the mostly of the firms employ a functional structure, at this cluster emerge a divisional structure (structure form = 2,71). Centralisation is low and the level of formalisation (39,2) is the most largest. This cluster present a large number of specialised functions (specialisation = 8,8). When compared with stages descriptions identified in Table 3, this configuration appears to represent an Diversification stage of development.

Cluster 5: Stage V

The firms of cluster 5, while similar in size to firms of the Clusters 1 and 2, are significantly older than their counterparts (Table 4). These firms fail to fit the traditional life-cycle model summarised in Table 3, and are thus more difficult to interpret and classify. The firms at this group average 16,3 years of age, employ an mean of 18,29 employed. Growth employment is declining (employment growth1 = -0,41; employment Growth2 =-0,77), and sales are declining too with a rate of –19%. These firms present a specialisation level similar to cluster II firms (specialisation = 4,8) and structure form (2,0). Present organisation levels of 3,4. This group present the formalisation level more heighted of whole groups (40,0). While present also high centralised level, against in

part the life cycle model that characteristics are present in the systematised model (table 3). While this firm groups are similar in size and structure with firms of the expansion stage (cluster II) are different in context. They are significantly more older (age = 16,2) and they not present any growth. Those firms present small size but with some advanced age.

Returning to the life-cycle literature, we identified a few possible scenarios that might help explain this configuration. Hanks et al. [9] noted that firms may go through cycles of stagnation or decline, interspersed among stages of growth. Empirical support of this notion may be found in Miller and Friesen's [11] longitudinal study of the organisation life cycle, they may skip stages or revert back to certain stages. Perhaps this configuration includes firms that are undergoing a cycle of stagnated growth. Or may be to present firms of life style where their entrepreneurs opted to maintain their firms small or may be to reflect, still firms that growth is limited because thus firms are operate in niches of market very small. This question can only be answered through future longitudinal analysis.

CONCLUSIONS

In our opinion this study makes two important contributions to the literature. First, it presents a methodology for empirically operationalising the organisation life-cycle. To know deeply models of life cycle stages permits increase knowledge of the complexity of growth phenomena and the effect that has into the firms [6]. While the literature abounds in theoretical models, very little attention has been paid to the critical construct of life-cycles stage. The empirical identification of configurations reflecting developmental stages represents a key building block for future analysis of the organisations life-cycle [9]. By employing this methodology to multiple samples, patterns of life-cycle stages can be systematically explored and important hypotheses generated.

The second contribution of the study is the derived taxonomy itself. The taxonomy presents a picture of growth stages in manufacturing industry firms of Beira Interior Region and provides a baseline for comparison with future taxonomic studies. The taxonomy portrays four configurational stages which appear to reflect Birth, Expansion, Maturity and Diversification stages. One additional configuration reflective of older small firms are also identified as stagnation or decline stage. The identification and verification of the development patterns

obtained in this study applied in different and more extensive contexts will better the utility and validation of the life cycle paradigm.

SUGGESTIONS FOR FURTHER RESEARCH

Empirical analysis of the organisation life-cycle remains in its early stages. Preliminary validation of the configurational approach to studying life-cycle characteristics presents an important building block, but a significant amount of work remains to be done. First, longitudinal studies of the organisation life-cycle that trace changing organisational configurations over time are needed. Although the cross-sectional approach taken in this study is suggestive of live-cycle stages, it is impossible to differentiate between configurations representative of life-cycle stages and those suggestive of firms simply choosing to do business in different ways. Both historical and repeated measures designs would provide important insights into patterns of organisation growth [9, 11, 6].

Second, there is the need for rich qualitative studies which capture the nuances of change within individual organisations. Such studies may provide additional insight into the choice of appropriate variables to form the clusters. Eight variables were used to form the clusters in this study. Might comparable configurations be identified with fewer variables? Are there additional variables which, if included, would yield more revealing configurations? Such studies might also lend insight into the process of configurational change.

Finally, there is a need to test the predictive utility of the derived cluster model. How are the taxonomy clusters related to focal problems or strategic priorities?

In conclusion, a valid life-cycle model could be of great value to those managing emerging growth firms. It could provide a road map, identifying critical organisational transitions as well as pitfalls the organisations should seek to avoid as it grows in size and complexity. This study provides a promising building block toward achieving these objectives.

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Electronic Commerce and the use of Website Design Consultants in Western Australian SMEs: factors affecting the success of online small enterprises

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Summary

Electronic commerce is often considered too expensive, technologically complicated and unsuitable for the small business environment and is not seen as a core activity for most small enterprises. In spite of these inhibitors, there are a growing number of small organizations developing websites to market their products and an increasing number of enterprises conducting online transactions and selling their products directly to customers via the Internet. In Australia there are more than 1000 website design consultants having a strong impact on the Small and Medium Enterprise (SME) sector, particularly in their efforts to enter the world of online commerce.

The majority of SMEs have neither the internal expertise nor financial resources to enable in-house development of electronic commerce and therefore turn to the services of website design consultants to assist them. As this appears to be a necessary strategy, given the operational and financial limitations of SMEs, the efficacy of this option is investigated in this paper.

The aims of this paper are firstly, to identify the extent to which SMEs feel their individual business needs are understood by website design consultants. Secondly, to investigate whether SMEs have clear goals and strategies before engaging in electronic commerce.

The paper incorporates a case study of two Western Australian online SMEs who contracted website design consultants to produce their sites. The SMEs chosen were established retail businesses and both utilized the services of different website design consultants.

The results of the study indicated that the case SMEs did not have an understanding of the need for business planning or developing an Internet strategy. Instead, both SMEs had entered the world of online retailing in a relatively adhoc manner. It was found that neither SME felt that their individual business needs were understood or met by the website design consultant. In fact, the case SMEs themselves appeared unable to articulate their own business needs in order to ensure a successful relationship with the consultants.

Introduction

Electronic Commerce[1] is not seen as a core activity for most small enterprises in Australia and it is quite often considered too expensive, technologically complicated and unsuitable for the small business environment [1, 2]. It appears that Australian Small and Medium Enterprises (SME)[2] are hesitant in their approach to electronic commerce [2, 3], unlike the United States where electronic commerce is growing at an exponential rate [4, 5].

In spite of the reluctance of Australian SMEs to enter the online world, there are a growing number of small organisations developing websites to market their products and an increasing number of enterprises conducting online transactions and selling their products directly to customers via the Internet. Therefore, SMEs appear to be slowly overcoming their reluctance to enter the online world. Whilst this is considered a positive step in increasing the presence of SMEs in the online environment, most SMEs lack IS expertise [6, 7], and turn to the services of website design consultants to assist them in developing an online presence.

In Australia there are more than 1000 website design consultants [1] having a strong impact on the Small and Medium Enterprise sector, particularly in their efforts to enter the world of online commerce.

[1] The definitions of electronic commerce range from the very simple and straightforward concept found in the Yellow Pages Small Business Index as "the use of the Internet to buy and sell products [2]. To the far more complex definition offered by the Monash Centre for Electronic Commerce:"as the process of conducting all forms of business activity between entities using appropriate electronic methodologies and procedures in order to achieve the organisation's objectives [3].

[2] There is no definitive model of a small or medium enterprise in Australia. The Yellow Pages Small Business Index defines a small business as having up to 19 full-time employees and a medium business as having between 20 and 200 employees, these figures do not include agricultural businesses (Small Business Index, 1998). The Small Business Development Corporation (SBDC) of Western Australia definition of small business is less than 5 employees in a micro-business, less than 20 employees in the non-manufacturing sector and less than 100 employees in the manufacturing sector. For the purpose of this paper two small enterprieses were chosen for case analysis in the micro and small business category.

The question asked by this paper is as follows: To what extent do SMEs feel their individual business needs are understood by website design consultants in order to ensure a successful venture into the world of online electronic commerce?

In an attempt to answer this question, this paper incorporates a case study of two Western Australian online SMEs who contracted website design consultants to produce their sites. The SMEs chosen were established retail businesses rather than start-ups as it was felt that established businesses would already have a general business plan or strategy. Different website design consultants were used in each case.

A review of the literature shows that an important factor in the success of online enterprises is their ability to align business processes with website strategy [8,9,10,11]. Further, several important issues have been identified in the literature regarding SME use of external consultants in the management of Information Systems. These include a clear understanding of the client/consultant role and the importance of SME involvement in the consultation process [6,12,13,14]

SMEs and the Internet

Research shows [15, 2, 1, 8] that most SMEs accessing the Internet tend to use it primarily for communication and information gathering with a small percentage actually using the Internet to conduct electronic transactions.

The findings of the Institute of Small Business Research (ISBR) 1998 Small Business Opinion Survey of Western Australian SMEs indicated that the majority of SMEs surveyed used the Internet for communication purposes and that electronic transactions only formed a small proportion of Internet usage (see figure 1):

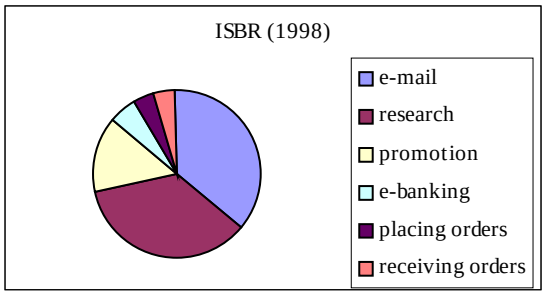

Figure 1 W.A. SME use of the Internet [15]

The Institute of Small Business Research estimates that 18% of Western Australian online SMEs surveyed conduct electronic transactions and only 9% are capable of receiving orders via their websites. If higher proportions of SMEs are to venture into the online world, the infrastructures of existent online retailers need to be examined in order to identify successful strategies for electronic commerce. Factors examined in this paper are the decision by a SME to contract a website design consultant, and the influence of the design consultant on the SMEs Internet strategy.

Website Design Consultants and SMEs

The majority of SMEs do not have either the internal expertise or financial resources to enable the in-house development of Information Systems (IS), including electronic commerce [1, ,6, 7, 12, 13]. It is anticipated that this lack of internal IS expertise also impacts on the SME sector's ability to design, develop and promote websites. Therefore, it is suggested that SMEs tend to rely on external consultants to design and implement websites.

The success or failure of a SME engaging a website design consultant involves a number of issues. Firstly, it may be the SMEs first attempt at engaging an external consultant and the SME may lack the relevant knowledge and experience required for successful engagement. Secondly, website design consultants are often SMEs themselves, and in the current climate of accelerating growth in the electronic commerce area, website design consultants are often business start-ups and consequently, may lack experience in negotiating successful contracts. Finally, consultants tend to view SMEs as one-off jobs and may consequently lack commitment to the project, "small firms were viewed as one-shot opportunities, offering no potential for establishing a long-term relationship. Consultants…would sell the small firms software and hardware, put together a network, and move on to the next company" [17].

Gable, [12,13] identified a number of issues that SMEs need to consider when engaging the services of a consultant. These included the amount of time and effort the SME contributes to the project and the maintenance of a clear understanding of the role of the SME and the role of the consultant. Gable, [12] developed a twelve phase model of consultant engagement to clarify the role of a SME in selecting a consultant (see Figure 2) :

1. define the problem;
2. evaluate internal resources available for the project;
3. canvass the market for prospective consulting firms;
4. develop a request for proposal (RFP);
5. check references;
6. evaluate proposals;
7. select a firm;
8. negotiate the contract;
9. announce the selection;
10. continuing review and refinement of mutual and individual responsibilities;
11. continuing monitoring and control of progress and
12. post-engagement evaluation of the service.

Figure 2: Gable's 12-phase model [12]

Gable applied the 12-phase model to a study of a case SME, 'Singapore Graphic Designs', in an attempt to identify the problems and issues SMEs encounter when engaging external consultants [12]. His findings indicate that the consultant engaged for the project did not adequately meet several of the steps in the model (see Table 1):

Problem	**Phase of Model**
1. consultant lack of commitment	5. check references 8. negotiate contract
2. consultant lacks experience	10. & 11. continuing review
3. no methodical approach	6. evaluate proposals 10 & 11. continuing review
4. inadequate vendor appraisal	6. evaluate proposals 10 & 11. continuing review

Table 1: SME problems and issues [12]

Gable, in a later study, introduced the concept of the 'pro-active client role in small business' [13]. This concept, in conjunction with the 12-phase model, was used in a study of five Singaporean SMEs attempting first time computerization. In his findings, Gable identifies areas where consultants failed to adequately meet key steps in the 12-phase model. In conjunction with this, Gable assesses the impact of client involvement in consultant engagement finding that "effective engagement requires that the problem is well defined and an appropriate consultant is selected with the problem in mind" [Gable, 1991 #66, p.89]. He then identifies three areas where SMEs can improve their consultant engagement process:

- assess client and consultant compatibility (phases 5, 6, 7 & 8);
- identify and address specific organizational roles (phases 1,2, 11 & 12) and
- accommodate evolving project objectives (phases 11 & 12) [13].

Although Gable's studies focus on first time computerization, it is felt that his model is applicable to Australian SMEs engagement of website design consultants. For the purpose of this research, it was decided to utilize Gable's 12-phase model of consultant engagement as a framework for analysing SME involvement in selecting a website design consultant.

Internet Strategy and SMEs

Prior to consultant engagement a SME should have a clearly defined Internet strategy. Current research shows that an important factor in the success of online enterprises is their ability to align business processes with website strategy. [8, 9, 10, 11].

Cragg, [9] identified four components of Internet strategy that may be useful for SMEs to consider when engaging in online commerce (see Table 2). The four components are *goals, content, process and functional.*

The *goals* component of an Internet strategy is sub-categorised into primary and secondary goals. A SME should incorporate both primary and secondary goals within the overall Internet strategy, in order to identify exactly what they expect from an online presence. Cragg indicated that the benefit of incorporating primary and secondary goals would be a method for SMEs to recognise potential economic benefits, and to indicate "…that increased sales can only be considered as one indicator of success." [9].

The *content* dimension of an Internet strategy identifies the main uses of a SMEs website. This component enables a SME to clarify what the site started with; it's current major uses, what the site is for and future plans for the site.

The *process* component is basically a method to identify whether the initiation and leadership of the strategy was from the CEO level or further down the chain of command and whether the site was built utilising internal or external expertise.

Finally, the *functional* component of Internet strategy examines the functions of the website. This could incorporate business-to-business electronic commerce, business-to-consumer electronic commerce, or the implementation of a method for increasing and retaining customers [9].

Goal	Example
primary	to reach an international market
secondary	to market site to potential customers
Content	
started with	email, catalogue, order form
major use	marketing/promotion
WWW site for	product distribution
future plans	introduce new functions
Process	
led by	owner/manager
whose initiative	internal
built	external
Function	
functions of site	business-business, business-to-consumer

Table 2: Cragg's Internet Strategy [Cragg, 1998 #32]

Whilst all four components of Internet strategy identified by Cragg, *goals, content, process and function* are useful in understanding the development of Internet strategy, the case study for this paper incorporated two of Cragg's strategies: the *goals* strategy, which identifies the main goals of the SME and the *content* strategy.

The above models Gable [12] and Cragg [9] were applied to the two case studies to evaluate the level of SME involvement in the selection of a website design consultant, development of an Internet Strategy and how these elements may have impacted on the success of the SME venture into business-consumer electronic commerce.

Research Design

As Internet commerce, particularly in Western Australia, is still in an emergent phase it was felt that case studies involving in-depth interviews would be most appropriate.[3] A review of the literature into research methodologies highlighted the usefulness of the case methodology in new and relatively new fields [16, 17, 18, 20].

Sample

The case studies were chosen via a deliberate theoretical sampling plan. Initially the researcher scanned the client pages of five Western Australian website design consultants. From this, several online SMEs were identified and their websites assessed based on the following model of website activities (see Table 3). The model was synthesised from Internet usage surveys and interviews conducted by several researchers [15, 18, 2].

Use of Site	SME One Educational products supplier	SME Two Lingerie retailer
Communication	email for client queries	email for client queries
Promotion	site promoted for local, national & international customers.	site promoted flor local, national & international customers.
E-transactions	can order products online via email order form – products available in a variety of languages. Pre-payment is a requirement.	can order products via email order form, Prices are not included in catalogue.

Table 3 Website activity model.

The SMEs were chosen based on the following criteria:

- Less than 5 employees (micro-business category);
- Retail business;
- Websites capable of electronic transactions;
- Website designed by an external consultant and
- Business located in Western Australia.

[3] "Case research is best utilized when the goals of the researcher and the nature of the research topic influence the selection of a strategy. Case research is particularly appropriate for certain types of problems: those in which research and theory are at their early, formative stages". (Benbasat et al., 1987 p360)

Background Information

SME #1 was a supplier of educational products and had been in business for four years. The website was designed and implemented by an external consultant and went "live" in November 1998. Since May 1999 the website has been developed and maintained in-house.

SME #2 was a lingerie retailer and had been in business for two years. The site was designed and implemented by an external consultant and went "live" in May 1999 (a delay of three months from the expected date due to copyright errors). The Owner/Manager intends to undertake a short course in HTML editing and then further develop and maintain the site in-house. Table 4 summarizes the background information of the two SMEs.

SME	Founded	Staffing	Annual Turnover	Date website started
SME #1 Educational products supplier	1995	2 full-time 2 part-time	$200,000	November 1998
SME #2 Lingerie retailer	1997	1 full-time 2 part-time	not stated	May 1999

Table 4 Background Information of case SMEs

Results and Analysis

The data was analysed using a matrix as proposed by Miles and Huberman [21]. A matrix is "…the 'crossing' of two lists, set up as rows and columns." [21]. The purpose of this method of analysis is to enable the data to be analysed visually and the data from both cases to be easily compared and contrasted and themes and patterns identified [21]. The data was then further analysed using Gable's 12-phase model for consultant engagement [12] and Cragg's Internet Strategy [9].

Gable's 12-phase model

Table 5 illustrates how closely the two SME case studies adhered to the guiding principals of Gable's 12-phase model for consultant engagement:

Gable's 12-phase model	SME #1	SME #2
define the problem	♦	♦

evaluate internal resources available for the project	♦	♦
canvass the market for prospective consulting firms		
develop a request for proposal (RFP)		
check references	partially	
evaluate proposals		
select a firm	♦	♦
negotiate the contract	partially	
announce the selection		
continuing review and refinement of mutual and individual responsibilities	♦	
continuing monitoring and control of progress	♦	
post-engagement evaluation of the service	♦	♦

Table 5 SMEs and Gables 12 phase model [12]

Consultant Engagement

Neither of the case SMEs utilized each of the steps in Gable's model (see Table 5). SME #1 completed six steps and partially completed two and SME #2 only completed four of the steps. Neither SME canvassed the market nor did they develop a request for proposal, although interestingly both SMEs stated that in hindsight they would have canvassed the market and asked for full quotations "…in hindsight I would have looked around more and found someone more capable and experienced…" (SME #1). Both SMEs relied on the recommendation of their Internet Service Provider (ISP), trusting that the ISP would know the market and make an appropriate recommendation.

SME #1 viewed the refereed sites suggested by the consultant, but did not contact either of the sites for a verbal or a written reference. SME #2 did not consider asking for references. Again, both SMEs stated that in hindsight they would have requested either verbal or written references from the consultants' client sites.

Neither SME had a formal written contract with their consultants although SME #1 had negotiated a verbal contract in relation to pricing for the design of their site. A written contract outlining the roles of both parties, requirements for the sites, pricing, timeframes and contract variations would have been useful for both SMEs when engaging a website design consultant and this will be expanded on in the following discussion on pricing, service and consultant experience.

Pricing and Service

In the analysis of the data, pricing and service were recurrent themes for both case SMEs and the importance of clarifying the role of consultant and client was very clearly highlighted. In both cases, it appeared that the SMEs passively trusted the consultant to produce results at minimal cost. Gable stated that the "misconceived view of the client role" [13] is one of the prime reasons for the breakdown of the client/consultant relationship.

Both SMEs felt that they had been overcharged and that they did not receive value for money from their website design consultants. SME #1 had discussed a budget with the consultant and was unaware that changes to the site would incur additional charges "..but that's when the money came into it and it ended up costing for every little tiny change and that's until we got the bill and said 'hey this is much more than what you said', I told him we had a really strict budget and it was just blown right out…"

SME #2 linked pricing and service provision several times throughout the interview "…if I've got to constantly be telling them what to do I think paying $90 an hour is a bit ludicrous" and "I don't think I got value for money…basically I think they charged me an hourly rate for the work that they did, the fact that they had no ideas of their own should have been taken into account when billing me".

Interestingly, neither SME voiced their concerns with the consultants and, as can be seen from the comment of SME #2 above, assumptions regarding billing were made but not explicitly drawn to the consultant's attention to enable any potential rectification.

This lack of feedback from the client to the design consultant confirms Gable's (1991) statement. This is further highlighted in comments made by both SMEs in regard to a perceived lack of follow-up service provision. SME #1 "It was me contacting him rather than him coming out at the end and going through it and saying right this is it it's final and saying are you happy? It didn't close up at all." SME #2 "I haven't heard from them since May and it's now July..if it was me, you know, a week or two later I would have phoned and said 'how's it all going'."

Consultant Experience

One of the client concerns identified by Gable in his analysis of consultant engagement is that consultants often appear to have minimal relevant experience. He stated that this could be overcome if selection of a consultant were guided by his 12-phase model. The two case SMEs in this study lend support to this statement as they did not adhere strongly to the guidelines of Gable's model and very clearly felt that their consultants lacked essential experience.

For example, SME #2 believed their consultant was technically competent, but lacking in original ideas. "I don't think they have any ideas of their own. I think they are very good technically, but I don't think either artistically or marketing wise that they are particularly well clued up". SME #1 stated "We gave them our catalogue, we thought they'd come up with something wizzbang but they copied exactly what we had done. We could have done that ourselves…they gave us the basis but that was all, there wasn't any extras...we fed them the ideas."

The development and evaluation of a Request for Proposal (RFP), steps 4 and 6 in Gable's model, may have clarified for the SMEs exactly what they were seeking from a website design consultant. In conjunction with the RFP, the preparation of a firm contract (step 8) may have assisted in circumventing these problems.

Cragg's Internet Strategy

Table 6 indicates how both SMEs fit within the Internet strategy model adapted from Cragg [9].

Goal	SME #1	SME #2
primary	To reach an International market	To establish mail order.
secondary	To increase profits	To market site to potential customers
Content	**SME #1**	**SME #2**
started with	email, catalogue, order form, promotion	email, catalogue, order form, promotion
major use	promotion	marketing/promotion
WWW site for	product distribution	increase customer base
future plans	electronic shopping cart	To control site internally, to initiate ideas that will increase the profitability of the site

Table 6 SME Internet strategy adapted from Cragg [9]

Neither of the SME's had a formal written business plan or Internet strategy as suggested by Cragg [9]. Instead, both SMEs had entered the world of online retailing in a relatively adhoc manner. Both SMEs relied on ideas, memory and hopes for

the future success of their sites. SME #1 had ongoing discussions between the partners of the firm to generate ideas and future plans based on their original goals of reaching an International market and increasing overall profits. SME #2 stated that they did not have a written plan "just ideas, obviously I'd like to develop it to other things".

When interviewed, both cases SMEs could verbally identify their primary and secondary goals, but were less clear in regard to content strategy. Both SMEs had future goals for their sites but had not formulated a structure for ensuring their ideas were captured, that plans and timeframes developed, or that future costs were identified.

SME #1 felt that they had achieved their first goal of reaching an International marketplace "We're pleased with the response we're getting from people all over the world". Although they did not feel that they had achieved the second goal of increased profits. "…the fact that we're not getting any follow up is really disheartening, at the moment I wouldn't rate it an economic success." The procedure for ordering is complex, an initial inquiry has to be sent via email, a catalogue will be posted and at this point most queries halt. One of the company's future goals is to incorporate shopping cart technology, an online catalogue and credit card ordering. SME #1 felt this improvement in the websites capabilities would increase actual orders from the site and lead to greater economic success. However, SME #1 also stated that the major use for content strategy was for promotion and they considered this an intangible measure of success.

SME #2 on the other hand felt strongly that they had not achieved their primary goal of establishing mail order, "sales off that have been minimal". Yet their secondary goal of reaching a wider audience was seen as quite successful "we've had about 200 requests for catalogues off the site in two months which is pretty good, people are walking around with our catalogues." SME #2 also stated that they had achieved the content strategy of marketing/promotion of the website. This was seen by SME #2 as an intangible measure of success and that economic success would follow once the website had been reassessed and redesigned internally.

Conclusion

There are many factors affecting the success of SMEs entering the world of online commerce and this paper focused on two possible factors. Firstly, consultant engagement for web design was investigated using Gable's 12 phase model for consultant engagement, and secondly Internet strategies were explored, specifically the *goals* strategy, which identifies the

main goals of the SME, and the *content* strategy, which identifies the main uses of the website adapted from Cragg's Internet strategy models.

Prior to consultant engagement, a SME needs to have a clear idea of their Internet goals and the strategies required for achieving those goals as suggested by Cragg [9]. However, neither of the case SMEs appeared aware of this concept. Although both cases SMEs could identify their primary, secondary and content goals verbally, both relied on ideas, memory and hopes for the future success of their online venture. Neither SME had allocated an ongoing budget for future maintenance and development of the sites nor had they clearly articulated or formalized future aims, identified time-frames or developed clear strategies for achieving any of these objectives.

The analysis of the interview data showed that Gable's 12 phase model for consultant engagement is a worthwhile tool for evaluating SME involvement in engaging external consultants to design their website. One aspect of this model that is particularly useful is its potential for clarifying the mutual roles and obligations of the client/consultant relationship. The model could be used in order to guide negotiations and relations between the client and the website design consultant to achieve a more successful outcome.

The question asked by this paper was: To what extent do SMEs feel their individual business needs are understood by website design consultants in order to ensure a successful venture into the world of online electronic commerce.

The data from the two case studies indicates that neither case SME felt that their individual business needs were understood or met by the website design consultants. In fact, the case SMEs themselves appeared unable to articulate their own business needs. Therefore, further research in this area would be valuable in order to clarify the issue, namely are online SMEs, in general, able to define and articulate their business needs to ensure a successful relationship with website design consultants. Ongoing research for this project will include an Australia-wide cross-case analysis of SMEs and website design consultants with the following anticipated outcomes:

1. Guidelines will be developed to enhance negotiations between website design consultants and Australian SMEs to achieve a more effective outcome;
2. A set of critical development factors will be designed, in relation to Internet strategy and consultant engagement, that may be used by Australian SMEs and consultants to facilitate the implementation of the online organization

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Organizational Life Cycles in Small Enterprises

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Summary

Despite the proliferation of a number of models of organizational lifecycle there remains little support empirically for their validity. Few studies have been conducted utilizing an inductive case based theory building methodology. Fewer studies have looked at lifecycles of small firms, despite claims by some authors that many life cycle models do not take into account the unique characteristics of small business. This study builds a 4 stage model of organizational life cycle in the New Zealand wine industry. Findings indicate the existence of patterns in organizational growth in small businesses similar to those of traditional life cycle theories. Unlike traditional theories, these cycles are dependent upon strategy and market orientation rather than due to the intrinsic nature of the firm.

Introduction

One of the most common (and perplexing) research questions asked by researchers is "what causes organizational growth? And, What happens to organizations as they grow?" In answer to these questions several organizational theorists have suggested that organizations go through a series of necessary and predictable life cycles much in the same way that an organism does [13]; [15]; [16]; [20]; [24]). Central to this theory is the idea that organizations move through a series of phases [31]. These phases may be as a result of internal crises [11], a search for new opportunities [5], a response to changes in the industry structure over the product life cycle, or in response to the changing nature of problems confronting an organization [15].

Typically small businesses fail more often than they succeed. Following a period of dramatic growth in domestic and export sales in the last decade a number of new investors have been attracted to the wine industry in New Zealand [32]. Many of these investors are small start-up wineries attracted by images of romance, high returns and a seemingly unlimited growth. Recently, a number of industry spokespeople have commented that the number of wineries will decrease in the years to come [2]. A recent study indicated that wineries in New Zealand were predominantly driven by the desire for increased growth and profit [2]. As such any business models that can identify how firms grow over time can assist small and medium sized wineries as they age and provide strategies that will enable them to insure against failure.

One popular growth model is organizational life cycles. However some doubts arise over the validity of life cycle models [17]. [17] argued that at best life cycle models can account for some of the explanation of growth at an industry level, however the existence of a general theory is unlikely. Life cycle models have also been criticized by small business writers for not taking into account the motives of many small business people who may be motivated by factors other than economic or growth based motivations assumed by life cycle theories [22], [19]. Life cycle models do traditionally assume that growth is desired and therefore it may be more appropriate to examine whether life cycles occur in growth oriented firms. The purpose of this paper is to examine whether profit driven wineries progress through a series of distinct life cycle stages.

Literature

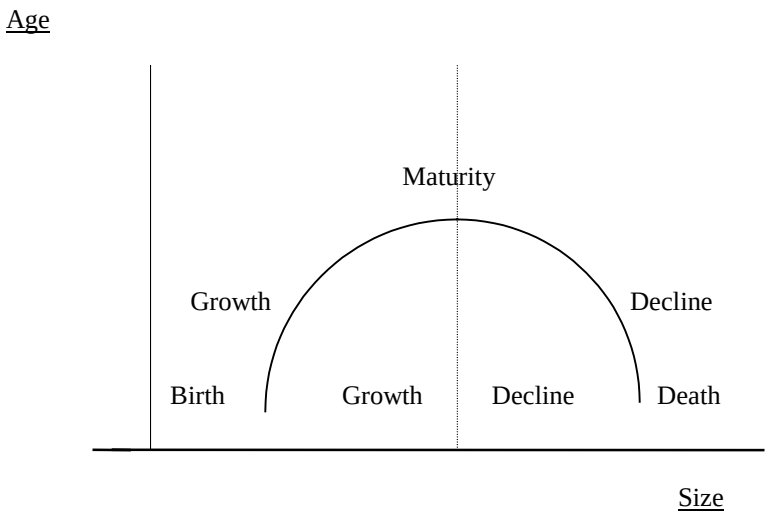
[12] noted that the life cycle analogy was developed in order to explain the development of organizations over time. Traditional management theories had failed to take into account issues such as an organizations age, size, and complexity when they attempted to explain organizational effectiveness [16], [24], and [20]. Early studies of organizations typically used a cross sectional perspective which more often than not resulted in a static view of the firm, telling us little about how firms are designed or develop over time [6], [24]. [20] concluded that these studies were too narrow and only looked at one specific interval of organizational evolution.

In reaction, many theorists designed models which argued that organizations go through predictable lifecycles ([1]; [5]; [6]; [7]; [8]; [24]; [11]; [16]; [18]; [20]; [27]). In these models, organizations are born, they grow, mature, decline, and ultimately die [24].

The aim of these life cycle models has been twofold. Some authors have used the life cycle metaphor as a means of explaining the emergence and development of whole industries [5], [27]. Primarily life cycle models have been developed to diagnose when an organization will get into trouble and then offer advice to management on how to encourage growth and prevent crises [11], [1]. [24] argued that given the high failure rate of new organizations it would be valuable to gain a greater understanding of how organizations develop and change over time. Life cycles have also been used to provide an early warning system for managers - to forewarn them of future crises, there causes, there consequences, and the way around them (for example see [1]). [30] described organizational change as largely reactive and triggered by organizational declines. A life cycle theory of the firm would enable managers to predict crises, and therefore plan for needed change prior to the event as opposed to waiting for decline to occur [11].

[20] argued that in general most theories held that firms develop in a sequential manner: "the *birth* phase led to a *growth* phase which in turn resulted in a period of *maturity*. Eventually product-market diversification and divisionalization could move the firm from *maturity* to the *revival* phase, while sometimes a *decline* phase followed maturity or revival." (339) The general idea is presented below as Figure 1. As organizations develop, they go through a series of stages, deal with a number of different challenges, conflicts and problems and adopt different strategies and skills.

Figure One: Organizational Life Cycles



In several literature reviews on organizational life cycle [13], [20], [24] a number of similarities between competing life cycle theories have emerged. [31] argued that common to all life cycle models was the idea that all firms develop or change in a unitary sequence that is both cumulative and conjunctive. Common to all theories was also the idea that there is some underlying logic or 'genetic code' that drives the organization through its life-cycle - with external events being mediated by the "immanent logic, rules, or programs that govern the entity's development." [31 p.37].

Despite the proliferation of models, a number of problems arise. Firstly, there is little empirical evidence for the existence of life cycles [19], [24]. Secondly, the sheer number of different models makes integration difficult [12]. Thirdly, the models are deterministic and do not allow for choices made by managers to pursue different strategies, including strategies that do not aim for growth [22], [7], [23]. Lastly, many of the studies rely on subjective data, limited samples and utilize cross sectional research designs which fail to show the long-term development of a firm [19].

Despite these problems, the model remains popular. A review of organizational development theories described it as one of the dominant models in describing organizational growth [31]. There is also some evidence that does support the theory [12], [14], [20]. Studies by [5], [23], and [21] all identified structured patterns in corporate history. Finally, a proven model of life cycle does have many advantages both for academics and for managers. [12] argued that a valid life cycle model would be of great value to those managing growing firms. He argued that:

> "It could provide a road map, identifying critical organizational transitions, as well as pitfalls the organisation should seek to avoid as it grows in size and complexity. An accurate life cycle model could provide a timetable for adding levels of management, formalizing organisation procedures and systems, and revising organisation priorities. It could help management know when to "let go" of cherished past strategies or practices that will only hinder future growth. Recruitment of critical skills could be timed to coincide with organizational needs." [12, p.1]

[13] defined a life cycle stage as "a unique configuration of variables related to organization context or structure." (7). The number of stages of development varies widely from three to ten [19], [12]. [19] argued that the [12] model was possibly the best way forward for life cycle theory, and his definition of a life cycle stage not only answered many criticisms of life cycle models (i.e. that they are difficult to test, vary in the number of stages and have little empirical backing); it is also sympathetic to other models such as [15] idea of organizational gestalts. For the purposes of this study, [12] definition of a life cycle stage will be provisionally adopted. A life cycle model would therefore be defined as a model that identifies a number of discreet stages that a firm goes through as it develops over time following a growth strategy.

Comparing ten models across five theorized stages, [12] and [13] argued that a valid life cycle model must address the following three questions:

1. What constitutes a life cycle stage?
2. Through how many life cycle stages do organizations grow?

3. What are the characteristics of each stage?

The New Zealand wine industry

In the last fifteen years the New Zealand Wine industry has achieved a great deal of success both at home and abroad. The Wine Institute of New Zealand reported that exports grew 15% in volume and 40% in value for the six months to 31 December 1998. This surge in recent success has attracted a lot of domestic investment to the wine industry. At present there are now 268 small category one[i] wineries in New Zealand. There are 297 registered wineries in New Zealand. However, the market is dominated by the 'big four' producers (Montana, Corbans, Villa Maria and Nobilo) who account for 78% of the domestic market. The other 285 wineries are therefore competing for just 10% of the local market, with imports accounting for 12%. With a static domestic market, and an increasingly competitive export market, these 285 wineries face significant challenges if they are to survive [2], [25].

Recent studies [2], [25] also lend weight to the concerns that many of these small wineries will struggle in the future. A report by agricultural bank Rabobank [25] on the world wine trade found that the traditional supply chain of wine through supermarkets and liquor wholesalers was consolidating through a number of mergers and acquisitions. As a result of the increased number of wine producing nations and wineries, many retailers were looking to rationalize their product lines and form relationships with a few key, large suppliers who could guarantee supply, product range, quality and delivery, and most importantly had strong brands that would sell themselves to an increasingly knowledgeable wine consuming public. [2]'s (1999) study found some acceptance for the idea that branding and marketing were highly important for future business success in the New Zealand wine industry, however this result was not uniform across small producers who were typically more production oriented.

These pressures and others, such as increased competition, increased wine quality and mergers between large wine companies are threatening the existence of small wine producers. Identifying a life cycle model for small wineries in New Zealand has many advantages as these organizations grapple with the challenges and pressures of growth and survival in the global market place. Some of these advantages are listed below.

1. A life cycle model could identify critical transitions points as organisations grow. This would enable wineries to plan in advance for the necessary changes that would need to be made to their strategy and structure to cope with the pressures of growth.

2. It could help management know when to "let go" of cherished past strategies or practices that will only hinder future growth.

3. Recruitment of critical skills could be timed to coincide with organizational needs.

4. Wineries could be provided with a template that would identify how they should develop, what pitfalls they may come across, what skills employees need, and what management practices should be used to spur future growth.

5. A large number of wineries are family owned. Family owned business are often subject to internal and political pressures that many traditional businesses are not. Previous research by Beverland and Bretherton (1998) found that many family owned wineries did benefit from using life cycle models to identify new opportunities and structural changes particularly in the area of staff rewards, succession planning and capital injections from non-family members.

6. Growth is a result of good management practice. A model of organizational lifecycle is essentially a model explaining the growth patterns of successful firms. As such, any model would identify best management practice for new entrants and struggling companies.

Methodology

Data for this paper was collected from interviews with 68 Category One (sales of less than 200,000 litres per year) wineries in New Zealand. This represented 33% of the total number of small wineries in New Zealand. Only wineries with a conscious growth strategy were selected. Wineries were then selected on the basis of their age, size, location, ownership structure, market share, brand profile and performance. Finally, any wineries that had gone through periods of revival (as reported in industry journals or the local press), formed strategic alliances, listed on the secondary stock exchange or had undergone a change in management were also selected on the basis that they could represent a particular stage of growth.

The data collection followed the multiple case study method of [9]. This approach was adopted as their was a lack of any grounded or inductive studies in the life cycle literature. Traditional life cycle studies have either assumed the existence of a theory in advance (e.g. [24]) or utilized cross sectional research designs that don't allow for an examination of how a firm develops over time (e.g. [12]). There has also been a call for more qualitative studies to occur in this area, particularly for inductive theories of life cycle [13]. For each case, secondary data was sought and written up in the form of a 'mini-memo' [29] that would form the basis for the case study and would drive discussion in the interview. In general data was gained via industry sources such as [32] and [4]. These sources would usually include information on start-up date, number of vintages, product range, levels of production, export markets served and some company and performance related information. From there, wineries were contacted and interviews scheduled. Interviews generally lasted for one hour although they ranged between 45 minutes to 3 hours depending on the willingness of the owners to divulge information and the amount of historical information to cover. Secondary data on such issues as product range, price range, number of employees, organizational charts, performance and objectives was also sought at this time.

Following the interviews, data was transcribed from tape, edited and summarized into memos. The data analysis generally followed the grounded theory approach of [29]. This method involved one of constant cross comparative analysis between each site. Following the writing up of an individual memo based upon the interview data and any historical or secondary data, the memo was returned to the interviewees for review and alteration. This helped ensure objectivity and internal validity. Once this was done, theoretical memos were written up around key themes such as strategy, evolution, structure, functions and specialization. Following this, the data was integrated with literature on life cycles, organizational development and strategy in order to assist with the emergence of a life cycle model. The result of this process forms the basis for the findings and discussion below.

Findings

As an overview, within 8 vintages from start-up, wineries tended to grow very quickly. Initial production averaged around 11 tons, but within 8 vintages had grown to 76 tons. Most wineries argued that this was natural for grape production, but also distributors would demand more production once the brand became established. Through the initial years growth tended to be financed through retained earnings. Interestingly wineries argued that there were several thresholds of production, and that being caught in the middle was dangerous. For example if you wanted to remain a niche focused winery you should keep production very low. From this initial level, your next step would be around 60,000 cases of wine. From there 120,000-150,000 cases was seen as a good level of production. This allowed a wider niche focus, but still avoided competition with large wineries that competed on cost. After this, growth should be much greater and aim for a production size of a large winery (1,000,000 litres sales per year).

The majority of the wineries were relatively new. On average these wineries employed 2.65 full time staff, 5.1 part time staff and 10 seasonal staff. When wineries started up they would utilize external consultants for wine making, viticultural advice, accounting and finance and vineyard management. Most wineries did their own marketing. As firms grew older, they tended to internalize the wine making, viticulture and marketing functions. As organizations grew older, the successful ones tended to move away from reliance on cellar door sales and develop wider distribution channels such as exports, liquor chains, supermarkets and wine shops. As organizations grew older (from 1 to 8 vintages), the successful ones tended to increase production, focus on key varieties (as opposed to offering a wide range of wines) and become more sophisticated marketers.

In general, the effect of founding was limited. Despite their being differences in the sample between firms that had purchased a winery from a former owner, started a vineyard from scratch and built a winery when vines were producing (generally in the 5th year of growth), or wineries who planted vineyards, built a winery at start-up and brought in grapes from outside to provide for cash flow, there was little difference between the patterns of growth of these firms.

Prior to start-up, there was evidence of a lot of action on behalf of prospective winery owners. Typically they attempted to gather resources, secure financial backing, gain key employees such as wine-makers, and acquire

finance and basic business skills. There was no time limit to this 'stage' but the participants all felt that they had to convince themselves and others that starting a company was a 'good idea' and that they needed the right level of resources and timing in the market to begin a business. Once prospective owners had the resources and the confidence the business was usually started within 6 months. During this period, prospective owners may still be working for other wineries or have other careers and may not give up these positions until the winery was established and enjoyed a level of financial security.

In the first 5 years, wineries were typically production focused. Those entrepreneurs that brought a vineyard as a going concern would typically focus on re-planting vineyards with key varietals, investing in oak barrels, new plant, and new viticultural practices. As these vineyards may have been planted with poor performing varietals many of these may be pulled out. Wineries that were new had to establish a cash flow. They may do this by using up capital, or they may buy in grapes from independent grape growers and make low priced wines that contributed to cash flow but didn't impact negatively on the choice to produce high quality branded wines (often these cheap wines would be dropped when their own grapes started producing). Another key strategy for gaining cash flow was to use plant to produce wine for other wineries. These wineries undertook little marketing and employees were often on short-term contracts or hired as independent consultants.

After the first five years, many vineyards would have their own grapes coming into production and would focus on establishing their own brands from their own vineyards. Wineries that revitalized an old vineyard would start focusing on marketing and building brands at an earlier date, usually within the first two years following purchase. Between year 5 and year 8, wineries would hire their own wine-makers and production staff but still use consultants for business related activities, although marketing was usually done in-house, often by the owner. As wineries became established, marketing would become the prime business focus, although production would still remain important. Production wise, wineries would often increase their storage space, expand plant and may build their own bottling lines. Marketing wise, due to their small size, most wineries would focus on public relations type activities. In the wine trade this consists of entering wine shows, sending wine to the press and wine writers, building a cellar door and holding tasting evenings for wine clubs. There was little advertising or mass marketing done at this stage.

Wineries typically relied on positive show results and press write-ups to sell their wine. Wineries also relied heavily upon cellar door sales (average sales through cellar door or mailing lists were 85%) at this point in time, although quickly moved away from this (usually within 3 years) and expanded into traditional channels such as supermarkets, wine retailers, restaurants and exports.

Towards the end of this period, providing the winery was successful (most made their first profits by year 5), most business functions would be performed in-house, whilst professional functions such as accountancy, law and some scientific functions would still be outsourced. Marketing plans were also developed at this time and accountancy systems tended to become more sophisticated during this period. During this time, wineries would tend to either expand their product range by offering more varietals and wines at different price points or focus very narrowly around 3-4 varietals. The strategy depended on production levels and upon geographic location. Being a cool climate region, New Zealand can grow some grapes better than others. In particular late ripening grapes such as Cabernet do not perform well or consistently well in New Zealand. Some wineries would remove these varietals as they understood more about their particular micro-climate, or 'terroir'[1].

After 8 years wineries went in one of three directions. Some wineries would settle at a certain level of production and grow no further. Some owners commented that this level of production allowed them to retain control over the company without having to hire line managers and supervisors. At this level owners were content, and therefore didn't choose to grow further. This sometimes lead to a decline period as the level of production was too low to meet the demand of key distribution channels like retailers or export markets. These wineries may also lose key people who felt stifled and therefore quality and market activeness would slip. Other wineries would consolidate for a period (on average 2 years or 2 quality vintages) and then go through a period of further expansion. These wineries often concentrated on improving debt to equity ratios or return to shareholders before moving ahead with further expansion. Finally other wineries simply continued to expand.

[1] Terroir roughly translates from French to "the relationship between soil, climate, and vineyard site." These factors generally impact upon the ability of a winery to gain the best out of a particular grape variety and controls to some extent the grapes that one can plant in a particular location.

Consolidation consisted of reducing product lines, deleting poorly performing labels or brands, reducing debt, bringing the winery up to full production and gaining key staff. Cash was often also sought from equity partners at this time to fund further expansion. Other wineries often sought new equity partners. Wineries that grew without consolidating continued to focus on increasing the production of key varietals whilst adding wines that were popular in the market. The focus of these wineries was predominately upon branding, brand reinforcement, building and expanding distribution channels, forming strong relationships with growers (if they used them), distributors and agents, building links with the media, and entering wine into international wine shows whilst moving away from domestic shows. Companies at this level also continued to develop sophisticated financial and monitoring systems that enabled improvements in quality as well as financial performance. A number of new staff were hired, typically in the marketing and sales area, although viticulturalists and wine-makers were also added. This often consisted of making part time staff full time. Wineries also relied very little on cellar door sales (which were now less than 10% of total sales), although they used the cellar door for brand building and enhancement. At this stage at least 50% of production tended to be exported, with wineries struggling to ration wine to key export markets. Wineries also focused upon return to shareholders at this stage and invested less of their profits back into the vineyards.

The age of many of the wineries made it difficult to establish any patterns beyond eight years, however the trend that is emerging is that many wineries are seeking to grow further through equity offerings on the secondary share exchange, or by gaining new equity partners or through the formation of alliances or joint ventures with local and overseas wineries. Family firms tended to differ in this respect in that they were more reticent to seek outside shareholders and funds for fear of losing control of the business. Although many did eventually elect to appoint non-family managers and seek outside equity capital most did so whilst still retaining a majority shareholding in the business.

Some wineries also went through periods of decline and renewal (no winery had ‘died’). In terms of performance 66.2% of wineries were projecting a profit for this year (1999). Those wineries that had been successful in the last five years of operation (success is defined as ‘profit in all of the last 5 years’ or ‘loss to break even or profit in the last 5 years’) tended to be more market oriented than those that had suffered losses. Market orientation strategies

involved: a focus on product quality, a focus on profitability, the development of strong brands, entering wine into wines shows, sending wines to media and providing product support. Forming relationships with suppliers and exporters was also important. When wineries went through a renewal period they typically returned to strategies of earlier periods.

Discussion

The general model that emerged from the data is presented below as Table 1. The evidence for a pre-birth stage supports a common criticism of life cycle models by small business writers [22] who argued that life cycle models typically ignore this stage. Once a winery has been started, several wineries sought a survival threshold [8]. Following pre-birth, a start-up stage can be identified from those wineries that gained market success. This generally comes from a successful wine review or wine show result. Once this result is gained, a small winery typically sells out of product overnight. From this stage, firms go through a expansion stage. This stage involves increased production, increased numbers of skilled staff, the development of a strong brand and a large amount of marketing activity. This activity involves the establishment of relationships with distributors, press, exporters and loyal customers (through mailing lists). Firms at this stage can risk overheating by developing too many product lines. Successful firms at this stage typically develop a strong focus around a few products such as Pinot Noir, Chardonnay and Sauvignon Blanc, although the product line will be partly driven by the geographic location of the vineyard. This stage is characterized by strong growth, a clear focus [1] and focusing on attaining human capital.

Following this, successful companies increased production, gained control over the supply of grapes, and developed strong brands that made them less dependent upon show results for demand. Successful wineries also developed secondary labels to use when the harvest was poor. As organizations aged they also grew in number of employees. There was some initial evidence to suggest that wineries that are older also started to seek new sources of capital via share offerings on the secondary exchange, or new equity partners. Less successful companies tended to use debt financing to cover expenses.

It is difficult to identify characteristics of any stages past the expansion as most wineries are still expanding. Some wineries are diversifying through increased share-holdings and equity capital. This seems to be becoming a trend and may identify a new stage of growth. Many wineries also consolidate at this stage and develop a back catalogue of aged wines before seeking further growth. Firms that declined are those that lose market focus by failing to develop strong brands. They also become over-reliant on a great vintage or wine show result. They fail to develop distribution channels over and above their cellar door operations. They also fail to rationalize product lines and increase supply of sought after wines. Finally, these wineries also fail to secure key assets such as staff, grape supplies and supermarket shelf space. All of this is well supported in the literature on life cycles [13] and organizational decline.

Table 1 Proposed model of organizational lifecycle for small New Zealand wineries.

Stage	Pre-birth	Start-up	Expansion	Growth
Time period	6 months once resources gathered	0-5 years	5-8 years	8 years +
Key focus	Resource gathering	Production Cash flow	Brand building Production growth Market expansion	Focus ROI Market orientation Debt reduction
Production	none	Replanting Vineyard focus Some winery development	Winery development Vineyard expansion Bottling lines Storage	Winery expansion Further vineyard expansion Quality control systems
Marketing	none	Public relations, wine shows and press, cellar door sales	Wine shows, press, in store marketing and limited advertising	International wine shows and press, public relations, cellar door and advertising
Distribution	none	Cellar door	Cellar door to traditional retail	Export Retail Little cellar door
Staff functions	owner and wine-maker	Production, generally part time	Production, marketing, generally full time	Some management staff
Challenge	Gain resources	Survival	Gaining distribution channels	Systems and planning

The data shows support for a life cycle theory or model existing within the New Zealand wine industry, however further testing would need to be done to establish if this model was true for different industries or even other wine

industries. What has emerged is a mid range theory of small firm development in the New Zealand wine industry that may add support to the large body of literature on organizational lifecycles. However, there are some significant differences. The range of options confronting wineries suggests that lifecycles or stage patterns of growth are not deterministic but are strategy dependent. For example, to focus on a niche in the wine market, wineries had to go through similar stages to companies with higher aspirations in their initial start-up period, but beyond that they had a range of options and success depended on maintaining quality and good links with customers and influencer markets. The similarity within an industry grouping of organizational development and growth offers support for a resource dependence model of organizational life cycle that does allow room for strategic choice and variation within an organizational population. Ownership structure also plays little role in life cycle development. Family firms often took a little longer to move from start-up to growth to further development as they were traditionally more risk averse and less likely to seek outside capital.. What was common was that the decision to seek outside capital took longer, but once it was made, the developmental pattern was similar to those of non family firms. Finally, the model seems strikingly similar to many of the life cycle models developed from large firms. Whilst it deliberately doesn't account for lifestyle or non-economic motivation of small firm owners, it does seem that lifecycle models within small firms are merely a variation of large firm models with the main difference being one of scope.

Finally this pattern of lifecycle development represent one of growth. It is by no means a necessary pattern of development. Several of the wineries in the sample have gone through periods of decline and renewal. As mentioned earlier, decline sets in when firms lose their market focus and fail to maintain a quality product. To renew, firms typically return to earlier stages of the lifecycle, refocusing on grape and vineyard quality, branding and developing relationships with key distributors. This is typically financed by outside capital and may include a change in management.

Conclusions

Despite wide spread theoretical support, organizational life cycles have little empirical backing. This research adds to the few studies that have found the existence of life cycles across firms in similar industries. There was some

initial evidence for a number of stages. The number of stages should not be seen as an exhaustive list. The young age of the sample did not allow for identification of later stages. Also the development was not guaranteed, but had to be earnt by consistent market action and the development of a market orientation. Failure to do so would result in decline and ultimately death. Firms that did successfully develop the right strategies went through the standard developmental pattern as highlighted in table 1. Renewal required a return to earlier stages of development and consisted of regaining a market focus. Interestingly there was little variation between family firms and non-family firms in the sample.

One limitation that needs to be borne in mind is that the sample did not allow for identification of what happens when small firms move to much larger levels of production. Most wineries in the sample were still relatively small after eight years, and any further expansion to reach a level of 1,000,000 litres of annual sales may require very large capital injections. This is yet to occur in the New Zealand wine market but has occurred overseas and it may be that further growth will have to come from outside investors rather than be generated internally. Finally, the development of a firm may be explained with reference to more than one model of organizational development. The findings provide support for models of organizational life cycle and for strategic choice models. Integrating strategic choice or teleology into a model of organizational life cycle may capture more of the complexity of firm development than the deterministic models of the past.

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[i] Annual wine grape sales not exceeding 200,000 litres

‘I Want to Make A Difference”
Women Small Business Owners: Their Businesses, Dreams, Lifestyles, and Measures of Success.

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SUMMARY

This paper reports the results of a series of focus group discussions with 63 women small business operators in Western Australia, one of the largest states for self-employment in Australia. The focus groups were the final part of a much wider study into women’s self-employment in Australia, which included an interviewing program of government agencies and other bodies interested in, or involved in, the small business sector, and a questionnaire study of 313 male and 264 female small business operators on a range of issues involving both start-up and continuing operations. The 63 respondents who participated in the focus groups represented 23.9% of the 264 female questionnaire population.

The results revealed that women tend to pursue small business as a lifestyle choice. Although different women seek different lifestyles, ultimately the question of growth of the business is pinned to lifestyle issues such as balance and flexibility. The question of values, and the way a person conducts business, is also significant.

The study also revealed a number of interesting features concerning women’s motivation and satisfaction in owning a business; the type of ‘contribution’ they believe they are making; their definitions of ‘success’; how they integrate time for themselves, their relationships and family; attitudes towards business growth; and what it was like being a woman in business. The results give a greater understanding of why women are entering small business in greater numbers, and why women, on the whole, prefer to keep their businesses small.

INTRODUCTION

Many different and diverse types of women enter self-employment. Two recent Australian studies (Flinders University of South Australia, 1995; Still & Timms, 1997) have found that the types include those who do so from necessity (the need to create or ‘buy’ a job, especially if the woman is unemployed or endeavouring to re-enter the workforce), those who cannot find certain opportunities in the salaried employment sector (encompasses ‘escapees’ from the corporate and public sectors; women who have encountered the ‘glass ceiling’; professional women; and women with a particular skill or creative drive); those who enter into partnership arrangements with other small business owners, those in family businesses, and finally those women who

become involved in multi-businesses (either as portfolio or serial founders [Westhead & Wright, 1999].

The types of businesses that these women run are also many and varied (Still & Timms, 1997, 1998). They include businesses operating in the informal sector of the economy (such as self-employed domestic workers), marginal home-based workers, home-based professionals and para-professionals, home-based cottage businesses; solo operations; micro-businesses (employing up to 5 employees); small enterprises (employing between 6 to 20 people); and multiple-business ownership (Scott & Rosa, 1996).

Just as there are different types of women entering small business, and considerable differences between the types of businesses that they operate, so there are differences in women's motivations and aspirations regarding their small business activities. Still & Timms (1997) and Cliff (1998) found that a woman's life cycle and that of her business may be intricately entwined, with a number of complex interrelationships developing according to the stage of life cycle (either life or business, or both) being pre-eminent. Put in practical terms, this means that as a woman passes through her own life-cycle she may pursue different goals in relation to her business and different business strategies depending on the life-cycle of the business.

Pursuing this further, Still & Timms (1997) found a number of important business development stages amongst women-owned businesses, based primarily on growth parameters. These were necessity (the business endeavour is undertaken through necessity); interest (growth is not pursued beyond a point where the owner must delegate responsibility); organic growth orientation (growth is self-financed, and undertaken in a manner which ensures that work/life integration is manageable); 'fire in the belly' (growth is fast and fuelled by entrepreneurial vision); and rapid growth (growth is a principal business goal, is financed through external sources and requires the employment of staff).

Interesting though these developments are in understanding women owners and their business operating methods, however, they do not present a total picture of why women become involved in self-employment. Another dimension begins to emerge when comparisons are made of the differences and similarities between men and women small business owners. Previous research has revealed that many women owners enter self-employment 'to make a difference', while also desiring greater autonomy, independence and flexibility, an opportunity to earn more money and other allied reasons. (Buttner & Moore, 1995; Still & Timms, 1997; Envick & Langford, 1998). Male small business operators, in contrast, tend to choose economic reasons such as the capacity to create wealth and the opportunity to pass something on to their family (Birley & Westhead, 1994; Fagenson, 1993).

While much research has been conducted into the reasons behind start-up for both genders, there has been no investigation to date on what is meant by women's self-professed goal of 'wanting to make a difference'. This is probably because most previous studies have adopted a quantitative methodology rather than a qualitative one where the answers to such questions could be delineated. What does 'wanting to make a difference' mean? Does it mean carving out some significant market share or other such economic method of measurement? Or does it mean being able to conduct business using a different philosophy or objectives to the traditional paradigm?

In an endeavour to solve this question, and thus round out the perspective on why women enter self-employment, this paper reports the findings of a series of focus group discussions held with 63 women small business operators in Perth, Australia. Whilst considerable research has been conducted into why women enter self-employment (Flinders University of South Australia, 1995; Still & Timms, 1997; Buttner & Moore, 1997; Chaganti & Parasuraman, 1999; Ahl & Samuelsson, 1999; Mallette & McGuiness, 1999), and Envick and Langford (1998), amongst others, have explored gender differences in the behaviours of entrepreneurs, little is known of women's perspective on the type of 'contribution' they make by owning a small business; their definitions of business 'success'; how they integrate time for themselves, their relationships and family; and their attitudes towards business growth. It is well known that women prefer to keep their businesses small (Still & Timms, 1999a; Flinders University of South Australia, 1995).

However, the views of women themselves on this matter have been rarely explored. The inclusion of the focus group discussions as stage 3 of the wider study, then, was designed to give a greater understanding of why women are entering small business in greater numbers than men, and why, on the whole, they prefer to keep their businesses small.

THE STUDY

The findings reported in this paper represented stage 3 of a much wider study into women's self-employment in Australia. Stage 1 was an interviewing program of 57 government agencies, educational and research institutions, and private enterprise sources such as business associations who were either interested in, or involved with, the small business sector. The prime purpose of that stage was to uncover particular barriers which prevented women from 'growing' their businesses (Still & Timms, 1997; 1999a). Stage 2 was a questionnaire survey of 313 male and 264 female small business operators on a range of issues involving both start-up and continuing operations (Still & Timms, 1999b), to ascertain if gender differences applied to these issues and whether women faced any particular or unique circumstances as compared to men. Finally, Stage 3 comprised a series of focus group discussions with 63 self-selected women small-business operators who represented 23.9% of the original 264 women who had participated in the questionnaire study. The purpose of the focus groups was to explore in more detail the experiences of women across the whole gamut of small business ownership as well as women's personal experiences in being a small business operator.

The sample represented a broad cross section of women in small business ownership (Australian Bureau of Statistics, 1998a,b). That is, their businesses were predominantly either solo operations or micro-businesses. There were no small enterprise owners in the sample. The women also either worked from home or from rented premises, while the type of businesses they were engaged in ranged from home-based cottage-style businesses to portfolio founder operations (Still & Timms, 1998; Westhead & Wright, 1999). Motivations for starting the business ranged from 'buying a job', 'requiring flexibility', 'escaping the corporate and private sector' through to 'wanting to make a difference' (Still & Timms, 1998). The women discussed a series of issues

covering business growth, the interaction between the business and life cycles, aspirations and success, balance and flexibility, and contribution to the economy. The particular format for the focus groups discussions was influenced by the results of Stages 1 and 2 of the wider study. For ease of analysis and consistency, the results of the focus groups were categorised into a number of themes following the format of the interview.

RESULTS

Making a Difference

Generally the women defined 'making a difference' as a fundamental shift in the goals and outcomes of their businesses as compared to male-owned businesses. That is, they were not primarily governed by economic goals. Rather they combined social with economic goals in their businesses. . In addition, they were not so concerned with making money. Contributions by way of making a difference to a community, by treating staff in a fair and friendly manner, by building good working environments for employees, by treating clients in a particular way, were very important to these women. As most had had unpleasant experiences of working in the male managerial culture prevalent in larger organisations, they were determined to set some new value paradigms and operating environments to reveal that there were other 'ways of doing business and still being successful'. Various dimensions of 'making a difference' were explored by the women in the focus groups. The following categories explain how they felt in more detail. While the women may not have been fully articulate in defining the 'difference', the sentiments they expressed give ample evidence of a different underlying orientation towards business and its eventual outcomes for both the owner and others.

Motivations and Satisfactions

Basically, the women followed Still and Timms (1998) paradigm as to why they entered self-employment. Apart from the basic reason of 'finding a job', there was a mixture of 'escapees from the corporate world', those who wanted to have 'independence and control' (also linked to a dislike of working in a large organisation), those who wanted 'flexibility or balance in their life', those who wanted more 'hands-on' experience with service to customers or the community, and

those who had a ‘dream or a creative vision’ they wished to fulfill (also defined as ‘making a difference’)

Four women were unemployed when they commenced their businesses. Despite having various skills, they were unsuccessful in gaining employment in the labour market. Two had been out of the workforce for too long (marriage and child-rearing), while for the other two no suitable jobs were available at their time of need. Start-up was thus an economic necessity, one which they had pursued quite successfully because their businesses had operated for over a year. As two women expressed it: “I have a nice stable income. I am quite satisfied”.

Another group of women were unhappy with working environments of large organisations, either public or private. Interestingly, their responses covered not only unsatisfying work situations and the ‘glass ceiling’ syndrome, but also revealed a new interpretation on what ‘independence and control’ meant to them. Some typical responses were as follows:

> *I was dreading going to work to-morrow. I had never been like that in my life before. I thought I had to do something about this. It was getting to be a health hazard. It was getting more and more stressful. I was getting sick all the time, but not sick enough to take time off work.*
>
> *I had been working for the government for some years, and had a position of reasonable responsibility and some promotion. I was asked why I didn’t go for higher jobs: I just couldn’t imagine anything worse. I kept saying: “Why would I do that?” I asked myself: “Do I want to be here until I retire at 65?” The answer was ‘no’.*
>
> *Professionally I was sick and tired of hitting the glass ceiling. A lot of promises were made, but never fulfilled. I was working harder than my male colleagues. I was earning a good income, but I was struggling all the time to get recognition. I wanted to be my own boss, have a real go at it myself, to see what I could achieve. You get to the situation where you think: “Is it me, or is it them? Is it the system?” I think last year I demonstrated that it was really the system.*
>
> *I just got fed up with trying to convince other people that I had a good idea before I could try it. That was a very strong motivator in me in starting my business.*
>
> *I put ‘independence and control’ over your working life as being very important. Being an accountant you have to have certain experience etc. before you can become a member of one of the professional bodies. When you are in an employment situation you have to be at work from 8.30 a.m. and you might be there until five, or six, seven or eight o’clock depending on the season. If you are not there you are seen as not performing or at least come under suspicion. I got really fed up with having no independence and control as I perceive it.*

> *I also wanted independence and control over my working life. What I've found frustrating is when you're working for someone else you're sitting there and you are double guessing their decisions. You're sitting there thinking: "I wouldn't have done that". With me, when I make a decision I do it by consensus.*

The remainder of the women's reasons were divided between having 'flexibility and balance', wanting to put something back into the community, and having a 'creative vision' that would 'make a difference'. For example:

> *My biggest motivation for starting my business was creative vision. I've committed my lifetime to taking my therapy into the 21st century, beyond 2000. I want to contribute to the world. You have to have someone who has enough vision to take it into the next era and that's what gives me a warm fuzzy feeling – that's what keeps me going. Knowing that I've got the power to do that and the skills, the knowledge and all that.*

No one volunteered 'making money' as a prime motivator. In fact, there was general agreement that money was not a driving force for these women:

> *….it's something else. Its job satisfaction, giving extra service, things like that. It's having people come back, and liking you, and having time with your friends and your family.*

These sentiments are confirmed by previous stages in the study (Still & Timms, 1997; 1999) and other research into the motivations of women entering small business (Ahl & Samuelsson, 1999; Buttner & Moore, 1997; Mallette & McGuiness, 1999).

Values

Closely entwined with the motivations regarding start-up were the particular values, both personal and business, that guided the individuals. The majority of the women spoke very directly about values, mainly because they had all come from male dominated industries or had worked within the male managerial culture. 'Integrity' was a word that featured prominently in the focus group discussions.

> *I saw an industry that smelt, that had no integrity…However, everyone that I had seen with no integrity was wildly successful. This just pissed me off to the nth degree. I was determined to prove that you could have total integrity, because you can't have just a little bit of integrity. You could make money, you could do well, and you could hold your head up high. When you didn't have to cheat, you didn't have to have hidden mark-ups*

and hidden commissions, then I could actually say that my business was successful. I told you it could work and I have not cheated anyone.

This integrity thing is really important. When my mentor first came and saw me, the first thing he said when he looked at my books and saw what I was doing was "You're not going to succeed". I said: "Why not?" And he said: "Because you are not taking a percentage off the top". And that was before I'd even really begun the business. I said: "I need to sleep at night".

Other values expoused by the women were the need to have control over quality; being able to practice their own business philosophies and principles in their business; being honest, moral and ethical in business; having concern for customers; and treating people like people – both customers and employees. Values were also valued for themselves:

Being your own boss means that you can set a value system that you are very comfortable with. I've worked in organisations where I haven't been comfortable. There are value statements on the wall, but what really happens within the organisation is totally contrary to that. The way people behave in an organisation is not about what I would call respecting others. It's important to have those fundamental values and ethical behaviour. The way we work in the consortium is good because there's certainly support of values, it's about supporting each other. We're still competitive, but we're honest and upfront about it. I think female value systems are very, very different to male values.

I don't know about other businesses, but certainly from the beginning a big part of my business has been looking after people who are less fortunate than I am. I just feel like it's time I paid a little back. One of the statements in my business plan is that I give a percentage of my turnover to charity, which is probably why I don't make any money! It's the sort of thing that a guy would not dream of doing; they might do it to get a tax deduction but not as a set thing.

What we are saying is that we have more human values, social related values rather than what we perceive to be men's values.

This type of driving force has also been found in research conducted by Olson & Currie (1992) and Still & Timms (1997).

Definitions of Success

Only four women identified money, or the amount of dollars they achieved in business, as their measure of success. The remainder were concerned with non-financial aspects, although some recognised that if they were successful, or gave satisfaction, in what they were doing then

success (in terms of dollars) would follow. The measures of success enunciated by the women were many and varied, and represented an eclectic choice. They included: having the 'opportunity to prove to myself that I can be successful in something'; helping communities; maintaining the freedom from doing what somebody else believes should be done; living a 'successful' life (successful not defined); being in control of decisions; expanding one's professional experience; being able to use and test creative abilities; being self-sufficient; having freedom of choice; successfully helping clients; balancing your life; and being 'happy with yourself'. Typical comments were:

> *I started my business to give myself a job and from what I perceived to be a threatened position financially. Therefore I decided not to bother about finances, which might sound silly, but I did not want to make that the focus of what I do. I've found that that works very well for me. Since I've put it out of my mind, it's actually taken care of itself quite successfully. So success is, to me, the way that you live your life.*
>
> *Success to me is that next Wednesday I'm going to do something else, I'm not working. It's that control of the book. You don't have to book yourself out. Or you take a week off. There's a price to pay for that, of course, but then you reach a certain level where you can charge a little bit more and give more, become more selective with your clientele so that you stay in control of A to Z….Success to me is freedom of choice.*
>
> *I have a guy who helps me do marketing plans. We have these amazing discussions that go a bit like this: 'What do you really want? Do you want a bigger car? How about a Porsche? What about a boat? Do you want to move into a bigger house? Wouldn't it be nice to be able to fly to Paris for a weekend?" Isn't that a male thing? Measuring success by the amount of toys you have. Who has the most toys wins?*
>
> *You read about Kerry Packer and how his measure of success if how many billions of dollars he's got. But it doesn't really matter, he might be a success in business, but is he a success in life?*

It is not known whether the above comments came from married women who were only in their business part-time or from women fully committed to running a full-time business. Nevertheless, an element of not having to worry too much about being the 'provider', the main bearer of the family income, is evident in the responses. Interestingly, the women who did nominate money as a measure of success were either divorced or widowed and needed to make a living for themselves. Money was thus important to them as a matter of survival for both themselves and their families. Despite this, however, other research has shown that women primarily measure success in terms of self-fulfillment or non-financial factors, and secondarily in

terms of profit (Buttner & Moore, 1997; Soutar & Still, 2000). These findings are confirmed by this study of 63 women small business owners.

Business Growth

One of the distinguishing features of women small business owners is that they are not primarily 'growth-oriented' (Flinders University of South Australia, 1995; Still & Chia, 1995; Still & Timms, 1997; Cliff, 1998; Chaganti & Parasuraman, 1999). Many women pursue small business as a lifestyle choice, with the question of growth of the business being linked to lifestyle issues such as balance and flexibility. As already mentioned, the question of values, and the way a person conducts business, is also significant.

Contrary to a lot of other studies, the 63 women in this study were almost evenly divided between growth and non-growth. Those who were pursuing growth as a goal expressed some doubts about the employment of staff (people had to be compatible and to follow the values set down for the business), while others had some fears or lack of confidence on how to manage growth. While not overtly expressed, their fears may have stemmed from the fact that women are not socialised to be wealth-creation conscious or profit-oriented. Nevertheless, they were determined to continue the growth mode and realised that their businesses would achieve much more through becoming larger.

Those who were not growth-oriented were more concerned with keeping 'control' of the business, not from a status point of view (such as being Managing Director), but from a flexibility and life-style perspective. They did not want their business to 'take over' what they had created for themselves by entering the small business arena. Examples of this position are expressed as follows:

> *What I control now is a very lean but creative environment that has a nice friendly environment with it. Once you start to get bigger the ability to talk to people on a one-to-one basis and really hold them to your vision and in your arms on one-to-one is more difficult. That's why I have specified quite clearly that I'll keep it small.*

> *The very reason I went into it is gone. I went into it for the freedom. There are three levels of freedom. Freedom to work for the clients that I chose to work for, or work with. Freedom of income, to grow it to whatever I needed it to be. And freedom to work wherever I wanted to work….But as the business has got bigger, all of that freedom has gone because it has taken on its own life now…*

One woman expressed a slightly different view which helps shed light on why many women prefer to keep their businesses small.

> *I think one of our problems is that we won't let go. It's very hard to delegate the jobs, and I think too that when you've created the company yourself all those ideas are in your mind. And you think that by the time I teach someone to do it I could have done it. Which is not necessarily the right answer. We get trapped that way.*

Growth in women-owned businesses is thus a complex issue and appears to be closely linked to stage in the lifecycle and lifestyle choices rather than to a great desire to increase wealth for family-line purposes. Personal goals thus appear to have a more dominant influence than business goals when it comes to the expansion or non-expansion of women-owned businesses (Still & Timms, 1997,1999; Cliff, 1998). As Cliff (1998) explains in his study of 229 small business owners in Canada:

> *Although male and female entrepreneurs seem equally likely to desire business growth….the qualitative findings suggest that female entrepreneurs are more likely to establish maximum business thresholds beyond which they would prefer not to expand and that these thresholds are smaller than those set by their male counterparts. These thresholds represent the size that the entrepreneur is comfortable managing – the size that enables him/her to maintain control of the organisation, devote a reasonable amount of time and energy to the firm, and /or balance work and personal life. The attainment of such size thresholds appears to be a key trigger in the no-growth decision.*

Contributions to the Economy

Little is known about the contribution of women-owned businesses to the economy (Still & Timms, 1997). In fact, there is no single data source from which such contribution can be measured. Some information is available in a recent study of employment generated by the small business sector (Year Book Australia, 1999) but it is not gender specific. In view of this

limitation, a part of the focus group discussions focused on what contributions the women believed their businesses made to the economy.

Interestingly, no woman spoke in terms of economic measures such as contribution to GDP. However, about a third considered their contribution to be the employment of others, while a number identified 'invisible' contributions such as assisting some group in the community, how the particular service they provided made it 'better' for people by saving on insurance claims, the contribution made by their creative vision, the servicing of customers, 'getting people enthusiastic again', and the fact that by being self-employed, the person was providing opportunities for others to gain work in other organisations.

The general result from this part of the discussions was that the women did not measure contribution solely in economic terms. Rather, they preferred to be more holistic and incorporate wider social and community issues into their goals and outcomes. This is where they felt they could 'make a difference'. Unfortunately, these issues are not measured in economic terms, and planners and policy makers are not necessarily sympathetic to the ideas. However, if the value of women-owned businesses are to be assessed at all, then perhaps new measures may need to be devised to incorporate some of this thinking. After all, economic units do not exist in isolation. They are also an integral part of the wider society. The manner in which women pursue their business goals suggests, then, that wider measures should be encouraged to ensure that all value-adding is incorporated into contribution to the economy.

Balance and Life Course Integration

As previous research has indicated (Still & Timms, 1997,1998,1999; Flinders University of South Australia, 1995; Cliff, 1998) women small business operators place a high priority on obtaining 'balance' in their lives. Usually this means integrating work and family (especially if the woman has a young family), but it also means incorporating 'rest'-type periods such as extended holidays, part-time involvement in the business, or time off to undertake other activities such as volunteer work. All of these interpretations were verified in the focus group discussions.

However, what also emerged was confirmation of the new model proposed by Still and Timms (1997,1998) in their investigation of the barriers confronting women in operating their business. The new model proposed that women's involvement in their business was linked to their stage in their life cycle. Hence, at a certain time, balance between work and family is important to women owners; at other life stages they are able to put more time into the business. Still and Timms (1997, 1998) concluded then that the operation of women-owned businesses could not be viewed from the standpoint of traditional trajectories of growth and economic contribution (such as assumed in analysis of men-owned businesses). Rather, because women play multiple roles in society, a more appropriate framework for understanding the operation of women-owned businesses was to incorporate this diversity and multiplicity into a cellular-type model which allowed for the variations encountered in both women's businesses and their lives. The focus group discussions gave ample verification of this course, suggesting a new paradigm for policy makers interested in the *modus operandi* of women-owned businesses.

Being a Woman in Business

Despite the fact that women now constitute 35% of all small business operators in Australia, old stereotypes were still found to prevail in certain sections of the community making it difficult for some women's businesses to function effectively.. Because some women-owned businesses were in conservative industries, some male clients still refused to deal with the woman owner in a business relationship although it was recognised that most men did not fall into this category.

In addition, a number of women reported that their husband's viewed their businesses as 'hobbies', while their children also found it difficult to understand that 'Mum' was involved in running a business. The women felt that both they and their efforts were not taken seriously. Other women reported government restrictions on home-based businesses which were making it difficult for them to develop their businesses, while still others described the physical and emotional restrictions involved in having a family, running a household, holding down a job and being involved in all sorts of unpaid work.

Again, others complained about being subject to sexual harassment. One woman summed up the situation as follows:

> *I find that right now the most important thing to do in consulting is networking. However, there are certain things I don't go to any more. There are certain companies I don't deal with because of the overtones that go on there. I don't want to deal with that and I resent it. I resent it very much because I am a professional. I enjoy being a female, and it certainly works very well in a lot of situations. You can get a guy to talk to you for a lot longer than another bloke can. [Being female] does work in your favour. But then you get to the point where you realise that if you are going to keep in contact with people a totally different interpretation will be placed on it. And it only happens because you are female. You suggest to a client that you should get out of the office and away from interruptions and have lunch and concentrate on your issue, and the next thing you know you run into gossip. I know this is being incredibly general. More than 88% of the people, guys you deal with, are strictly professional. You just run into the odd one every now and then…*

Still others reported having difficulties negotiating with banks, especially if their husband or a male director attended the meeting. The bank managers addressed all conversation to the other male and ignored the woman. Some women also found it difficult to give instructions to staff when their husbands were involved in the business. Staff generally treated and referred to the husband as 'the boss' even if he was only a secondary partner. Finally, some women reported that their husbands became jealous of their success, leading to problems in the domestic and/or business relationship.

Despite the advances made by women, then, in entering the small business field, a number of gender stereotypes still appear to function making it difficult for some women to be a 'woman in business'. Women still have a way to go before all will report a 'level playing field' in the world of business.

CONCLUSIONS

The focus group discussions involving 63 women small business owners thus performed two functions. First, the results verified previous research; and secondly, they verified a new direction for analysis which emerged in the work of Still and Timms (1997, 1998).

The paper also confirmed other evidence that women tend to pursue small business as a lifestyle choice. Although different women may seek different lifestyles, ultimately the question of growth of the business is pinned to lifestyle issues such as balance and flexibility. The question of values, and the way a person conducts business is also significant.

Most women running their own businesses express the desire 'to make a difference'. However, as already mentioned, the difference is expressed in terms of lifestyle combinations and the values they pursue in their business. The difference is not expressed in terms of 'grand visions', 'building empires' or 'making money'. Rather the difference is expressed as follows:

> *I went to a business networks meeting recently at a hotel. I got there a little late and looked around the room. There were five women present and about 100 men. The whole meeting was dominated by "What are we here for? Making money!" And I was going "There's something else guys!" The whole thing was a sell on networking, networking for profit. I wasn't even prepared to stay in the end for the open discussion panel because I thought I didn't want to be involved in this. If I stood up and argued the case for another set of values, who would listen? It's like why don't women go into politics? Why? Who would want to join that lot? It is a whole way of working with which a lot of women are uncomfortable.*

This study then has provided a better understanding of the reasons why women do not necessarily want to 'grow' their businesses and are content to operate within certain thresholds (Cliff, 1998). It is also one of the few studies to do so, as most research is quantitative rather than qualitative. There is a need for further such research to gain a greater understanding of the operations of women-owned businesses.. However, irrespective of this, it does appear that women are prepared to experiment more in their business *modus operandi,* suggesting that there is more than one way to do business. Not as profitable perhaps as the mere pursuit of economic goals, but one in which greater enrichment and satisfaction can be gained. Thus, evidence has been gathered to support Barrett's (1998) view that women are prepared to use different frameworks, especially more 'integrative' ones. As Brush (1992, p6) explains: 'Women view their business as an interconnected system of relationships instead of a separate economic unit in a social world". It is felt that this study has lent further evidence to support these views, thereby adding greater perspective to the need for women 'to make a difference' by integrating both social and economic approaches in their small business operations.

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MOTIVATIONAL BACKGROUND AS AN EXPLANATION FOR DIFFERENCES BETWEEN MALE AND FEMALE ENTREPRENEURSHIP

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SUMMARY

Recent literature on the subject of entrepreneurship reflects quantitative and qualitative changes in female entrepreneurship. It is argued that female entrepreneurship is in transition, it is changing from the traditional to a more modern type of entrepreneurship, seeking new forms, which are typical for male entrepreneurship: high profile, growth oriented and expert based.

The purpose of this study is to look at the current situation in Finland. The research questions are: 1) What is the frequency of female intentions to set up enterprises compared to male intentions, and 2) Do the intending women differ from men and non-intending women in terms of their motivational background. By motivational background we mean various push and pull factors, personal motivation structure, instrumentality of entrepreneurship and barriers to entrepreneurship.

An analysis of data consisting of 1841 observations produced the following results. Female intentions represented 31% of all intentions. The intending women are influenced by stronger push and pull factors than the intending men. Also the perceived instrumentality of the entrepreneurship was higher among the intending women than men. The differences between intending and non-intending women were significant. Especially the motivation structure between the two groups was highly different. The non-intending women regarded secure income, the possibility to grow and learn as well as social relationships as the three personally most motivating factors at work. The current good working conditions and the women's personal motivation structure were thought to explain the fact that the current trend in modern female entrepreneurship does not clearly manifest itself in Finland today, either in terms of quantity or quality.

INTRODUCTION

According to several recent reports female entrepreneurship is growing. This has been a clear trend since the 1980's when, for instance in the United States, the number of non-farm sole proprietorships owned by women increased by 62% between 1980 and 1986 [4]. The trend has continued strongly in the 1990's, and it has been found that businesses owned by women employ more people in the USA than the Fortune 500 companies worldwide [1]. In Canada there has been an increase of 265% in female self-employment during the last two decades, compared with an increase of 74% among males [20]. It will be interesting to see if the new statistics confirm the forecasts, made earlier in the 1990's, which suggest that women's share of business proprietorship will be 40–50% of all small businesses in the U.S. in 2000 [1].

Besides the quantitative growth of female entrepreneurship, it has been argued that female entrepreneurship as a phenomenon is transforming itself. The stereotypical approach to business by women has evolved into different patterns of modern female entrepreneurship, representing diverse high profile patterns, thus demarcating the field from the traditional female entrepreneurship. From this perspective, the practices of female entrepreneurship deserve renewed interest.

Recent literature considers entrepreneurship more as a process of becoming than a state of being. [6] The process of an individual becoming an entrepreneur consists of several phases, starting from changing values and attitudes and identifying oneself as an entrepreneur, and finishing up finally with the entrepreneurial action, for example, starting up a new venture. Entrepreneurial intention is a state of mind which evolves during the process, referring to the person's awareness of the entrepreneurial career choice. By investigating entrepreneurial intentions in a population it is possible to estimate the future level of entrepreneurial actions. This study seeks to find out the recent trends of female entrepreneurship in Finland. The focus of the study is on entrepreneurial intentions and the motivational background supporting the female entrepreneurial behaviour.

FEMALE ENTREPRENEURSHIP: TRENDS, DIFFERENCES AND TYPES

Work related values, desires, and needs

Male and female entrepreneurs have been suggested to differ according to their values regarding entrepreneurship. For example, Solomon and Fernald [28] have investigated the values of U.S. entrepreneurs. In terms of terminal values, at the top of men's ranking list were pleasure, true friendship, sense of accomplishment, a comfortable life and salvation. The three least preferred values among men were national security, mature love and wisdom. On the other hand, the top four terminal values for women were health, self-respect, family security, freedom and a sense of accomplishment. At the bottom in their list were national security, social recognition and salvation. In terms of instrumental values, the two gender groups did not differ a great deal. For male entrepreneurs the two top values were ambition and broadmindedness. Honesty, lovingness, imagination, cleanliness, capability, helpfulness and politeness were almost equal in importance. Men regarded self-control as the least important value. The most important value for women was honesty. The second important values were responsibility, independence, ambitiousness and capability. Cleanliness, politeness and obedience were the least important values in this ranking.

A person's occupational situation may play an important role in the formation of entrepreneurial values. Harpaz has [12] studied work-related goals among different occupational groups (professionals, administrative and managerial workers, clerical and related workers, service-workers, production-related workers) in seven countries (N= 8192). The respondents were asked to rank 11 items according to their perceived personal importance. In the comparison between genders Harpaz found that *interesting work* emerged as the leading work goal for both genders at all organizational levels. Furthermore, *good pay* was the second most important item for male employees and supervisors, but only third (employees) and seventh (supervisors) for their female colleagues. The difference between genders concerning pay was small among managers. *Good interpersonal relations* was the second most important goal for women, except female managers, who ranked it third. That represented only mediocre importance for men. Also *good match between job requirements and one's abilities* was regarded as significantly more important among women than among men. *A lot of autonomy* was regarded as a significantly more important a goal for men than for women at all organizational levels. In contrast, *convenient work hours* was much more important for women than for men at all organizational levels. In

addition, *opportunity to learn* was more important for women than for men, especially in the blue-collar group. *Good job security* was more important for men at all organizational levels.

It has been suggested that female entrepreneurs are very similar to female executives in large corporations. Richardsen, Mikkelsen and Burke [26] explored the question of job satisfaction among Norwegian female managers (N=191). Their research revealed that those women who perceived opportunities for advancement in the organization felt high job satisfaction. Also career satisfaction and job satisfaction were significantly correlated. On the other hand, the results showed that the larger the organization the woman worked for, the less job satisfaction she felt. Richardsen et al. concluded that conflicts between work demands and family responsibilities represented major pressures for women. Should these results be contrasted with female entrepreneurs, it is reasonable to expect that, for women, the advancement of their own business would increase the associated job satisfaction. However, it should be remembered that the traditional types of female businesses are small services or craftsman-type sole proprietorships, where possibilities for significant development may be poor.

Besides values and work satisfaction, goal-seeking behaviour has been associated with female entrepreneurship. The entrepreneurship research has revealed that many women launch their businesses, above all, to achieve independence, job freedom, higher incomes and personal development [17, 21]. Carter and Cannon [8] found that the most important reason for women to start their own businesses is the *need for independence*. This urge for independence is emphasized in different ways. Moore and Buttner [21] found several factors that can be associated with independence. They found that *to be able to advance oneself* was the most important reason for 23% of the respondents. The second category was *to create a work environment matched with one's own values*, which was the most important goal for 21% of the respondents. *To be in charge of a new and exciting venture* was the most important reason for 18% of the studied entrepreneurs. Finally, the *desires to regain excitement about work, the balance between work and family and to become an entrepreneur were* all most important for 11% of the respondents. While characterizing female entrepreneurs, these goals are typical also for male entrepreneurs [21] and for managers in general [23].

To conclude, the studies have shown that there are no major differences between entrepreneurial men and women in personality dimensions [4]. However, when starting up the male entrepreneurs more often cite

economic reasons, whereas women more often cite family needs and career dissatisfaction [4]. It seems that for men it is a business decision and for women it is more like a life choice – a means for combining family and career needs [4]. Building on this, the evidence suggests a sociological, rather than a psychological explanation for entrepreneurship. Socialization patterns during childhood and also in work life are suggested to be able to explain the reasons for decisions to start up own businesses.

Life-cycle factors

Some researchers have suggested that women's decisions to start their own businesses depend strongly **on life-cycle factors** [30, 17]. People's life cycles themselves have an impact on their personal values. That is, the values a person carries seem to change along with age. Harpaz [12], for example, found differences in values between age groups. For young respondents (under 30 years), *a lot of autonomy* was the most important factor associated with work while, at the same time, this item was the least important for the oldest group (over 50 years). In some respects values receive their highest point within the middle-aged group. For example, *good match between job requirements and one's abilities* was more important for respondents between 31–50 years old than for the younger or older groups. *Interesting work* was important for all age groups.

Contingent factors associated with life cycles are people's situations in working life and their family-situations. For example, Cromie and Ayling [9] have argued that at early stages in a woman's career problems are more clearly connected with gender-related factors than at later stages. Research on female entrepreneurship have come to the same conclusion as studies concerning working women overall. The family-related boundaries depend on the social and ideological context. Different countries have different social infrastructures and ideologies concerning family roles and gender equality [2]. Finland, as one of the Scandinavian countries, has a contrasting situation with the US, Britain and many other European countries in this respect. Gradually since the 1960's a social consensus has developed in Finland that women should have jobs [16] and that fathers should involve themselves in the care of their children [2]. This has, in fact, become also an economic necessity in the modern way of living. The state has supported this development by offering good children's day-care provision. Interestingly, there is a connection between women's self-employment and the changes and development of the welfare state. The state has provided public services that have offered plenty of possibilities for women to participate in paid working life [17]. The social effect has been an equalizing of gender roles. These improvements in the social infrastructure may, however, have lowered the push-related needs of women to start

their own businesses, as the opportunities to work outside home are improved without the need for taking personal risks and 'buying' one's own employment.

Another major problem for women is combining **entrepreneurial work and family life** [24, 7]. Household work and parenting chores still appear to be mostly women's province. In Finland women still carry 67% of the workload in households, in comparison with the median of 69% in other OECD-countries [13]. This family-work conflict is very strongly a life-span related matter [25]. It could be suggested that this factor is one of the main barriers for many female young adults to start their own businesses.

In summary it seems that women face more problems with combining family and work than men do [4]. It is claimed that socialization to gender roles is one of the causes for women to traditionally regard work less central to their lives than men do. However, while most research on women's possibilities for entrepreneurship assumes male oppression as the point of departure, it is possible to consider other approaches. An interesting finding is that of Campbell et al. [7], who found that family-life has a positive rather than a negative effect on women's work performance.

Types of female entrepreneurs

The earlier research has proposed several typologies for female entrepreneurs. In Goffee & Scase's [11] typology the basic idea is to see how women react to a situation of subordination. Goffee and Scase interviewed 54 women and classified women's experiences of business proprietorship according to two sets of factors. The first was women's attachment to the entrepreneurial ideals. This refers to a set of attitudes: belief in economic self-advancement, adherence to individualism (self-help, personal responsibility and self-reliance) and work ethic. The other factor was the extent to which women were prepared to accept conventionally defined male-female relationships. They describe female entrepreneurs in terms of four different types:

- *Conventional women* are strongly committed both to entrepreneurial ideals and conventional gender roles. They work in areas where they can combine traditional female-roles and business activities. Their businesses are small, non-growth oriented and traditional – such as restaurant-business, cleaning, nursing and hairdressing. Many of them work in assisting tasks in family businesses.
- *Innovative proprietors* are women with high commitment to entrepreneurial ideals and reject prevailing notions of conventional female role. Those women are strongly motivated to growth and profit

potential in business – often at the cost of social life. For them business ownership offers a possibility to create a rewarding career – easier than as an employee. Their typical fields are business-related services.

- *Domestic proprietors* are strongly attached to the traditional female role and have a low degree of commitment to entrepreneurial ideals. These women seek non-monetary self-fulfillment and personal autonomy within the limits of domestic responsibilities. Profitability is not very important for them in business, which could partly explain the low profit exhibited by their businesses. Typical forms are arts and handicrafts, health foods, dressmaking, to name but a few.
- *Radical proprietors* have a low degree of commitment on both entrepreneurial ideals and to conventional female roles. They are often highly educated and have met barriers in work careers. Owning business offers these women a means to overcome their subordination in the labor market. For them the maximizing of profits is not the primary goal. Typical areas are publishing, education, manufacturing and craft trade.

Sundin and Holmqvist [30] contribute to the understanding of types of female entrepreneurs with their categories of women in business. They use situational factors such as the way of life (independence as a way of life, the waged worker's way of life and the way of life appropriate to a career), marital status and attitude towards gender roles (traditional, modern). Sundin and Holmquist end up with three ways of life: the traditional independent, modern independent and the life of the waged worker. The traditional independent refers to a group of women who do not differentiate between work and leisure. They are often assisting family members in business, as "invisible" entrepreneurs. The modern independent way of life refers to women who see their own business as important and essential. For them the work is not just a means to something but also an end in itself. Entrepreneurship is a way of building one's own career. Finally, the life of the waged worker refers to women who combine work and family through self-employment. They often adapt their working lives to family situations or the changing situations of waged work.

Kovalainen [17] combines elements of the typologies described above. She uses two dimensions in forming her own typologies. The first refers to the extent of different economic necessities, independence and life-style. The other refers to the extent of the dependence or independence of the traditional role models and role ideals of each gender. The separate groups can be set on a continuum between women with high degree of dependence and

necessity and women with high degree of independence and freedom. The first group consists of those women Goffee and Scase call 'home-based entrepreneurs'. In addition, unemployed women are categorized in this group. At the other end of the continuum there are women who are classified as radical business proprietors and innovators. In between these two ends are the so-called take-overs, those who have worked as wage workers in the same businesses.

Procter and Padfield [25] criticize strongly the separation between family-oriented and career-oriented women. In their study they found out that different situations and preferences change during a woman's life. Besides those life-span changes there may be some other differences in women's values, attitudes and choices. They also noted that nowadays many women want both career and family. The 'modern' female entrepreneur is not willing to accept either-or–choices, they want both.

Modern female entrepreneurship

As demonstrated by the above review, a discussion about a 'new' entrepreneurship of women has arisen. Professionalism and careerism are important factors when describing female entrepreneurs in this group [17]. Starting a business is seen an easier way to success than working your way up the corporate ladder. It has been claimed that women's migration to entrepreneurship has been more a result of frustration with organizational barriers or experiences of downsizing than to any unique personality attributes [4]. Many of them have had good occupations and careers as a waged workers [5]. Typical reasons for their leaving organizations are attitudinal and organizational barriers to career advancement [10]. Although the number of women in working life has increased dramatically during the last decades in western countries, the proportion of women employed as top-level managers is still small [26]. The phenomenon has been named 'the glass ceiling', a subtle and almost invisible yet strong barrier that prevents women from moving up to senior management levels [22].

Modern women entrepreneurs typically seek new challenges and opportunities to prove to themselves that they can succeed on their own [5]. For these women entrepreneurship is often a means to obtain deeper job satisfaction. They are typically highly educated and have specific know-how [11, 15]. Additionally, research has described a typical modern female entrepreneur as belonging to the middle- or upper-middle-class, being married with children, 30 to 45 years of age, often first-born, college-educated daughter of a self-employed father [28, 4]. Many of these women use their organizational experiences as incubators for the businesses they

create [5]. Especially business related services are potential enterprises for these women. They often capitalize on their training and experience in the same industry, in manufacturing, engineering, transport, construction and other traditionally male-dominated fields [4].

Differences in female and male entrepreneurship in Finland

The number of self-employed women in Finland is growing steadily but slowly compared with the growth in male entrepreneurship [17]. Statistical figures show, however, that the number of self-employed women has not increased to the same extent as in the US and the UK, when the whole group of self-employed women is considered. In terms of absolute figures, the bias for male entrepreneurs is easy to depict in Finland. Only one third of all entrepreneurs in Finland are women [17]. The situation has been nearly the same since the 70's, remaining independent of the general economic fluctuations. This implies that self-employment is not an option for women in Finland, at least to the same extent as reportedly in many other countries [17].

Approximately 30% of female entrepreneurs work in societal services in Finland. These consist social and healthcare, personal and home services. Nearly as many work in trade, concentrating on retailing: pharmacies, florists, textiles and shoes. The ten most typical occupational titles in Finland for female entrepreneurs are retailer, hairdresser, caterer, daycare provider, dressmaker, dentist, beautician, manager and gardener [18]. Usually women's business ideas are based on women's traditional work roles and most of these branches are female dominated [17]. That is, women become entrepreneurs in those branches where the majority of employees are women.

The situation in Finland reflects the general picture of women business owners. All over the world the literature describes female businesses with factors such as tradition, concentration on service sector, small size and lack of potential growth [28, 17, 21]. This typical group of female entrepreneurs has been titled as "traditionals", thus giving room for identifying the "modern second generation" female entrepreneurs [21]. However, in Finland the nature of women's self-employment has changed relatively little since the 1960's [17].

Although growth rates in Finnish female entrepreneurship have been lower than in other western countries, the general circumstances for increasing female entrepreneurship in Finland should be positive. For example, women's participation in work life is equal to that of men (71% of women aged 15–64 years). Almost half (46%

in 1998) of the employed women work in the public sector, which is reducing personnel. Women's educational background in Finland is one of the highest in the world.

COMPARATIVE STUDY OF FEMALE ENTREPRENEURIAL INTENTIONS

Main theoretical concepts of the study

This research concentrates on entrepreneurial intentions. The concept of intention is grounded on cognitive psychology that attempts to explain or predict human behaviour. It is seen that behavioural intention results from attitudes and becomes an immediate determinant of behaviour. **Entrepreneurial intention** is "a conscious state of mind toward the goal of founding a business" [3]. Entrepreneurial intentions are aimed at either creating a new venture or creating new values in existing ventures. Intentionality includes both rational/analytic thinking (goal directed behaviour) and intuitive/holistic thinking (vision) [3]. Entrepreneurial intention has the role of eyeglasses through which a person seeks out information she or he can use to start a business [14]. It may be a critical factor for the beginning of a business [19].

Motivation structure and **instrumentality** are rooted in Lewin's Field Theory, which considers behaviour as a function of a person and his environment. One of the main explanatory concepts of behaviour is valence. Valence can be seen as a vector of power, which has a strength and a direction [31]. It is determined by a person's internal value for a thing (e.g. money), and the attractiveness of a certain field (e.g. entrepreneurship) to fulfil the need. Vroom [31] defines motivation (the force to perform an act) as a function of valence and expectancy. Furthermore, valence is a function of perceived value and perceived instrumentality. Applying this reasoning to an entrepreneurial decision, the motivation to start-up is stronger the more a person (1) perceives that the rewards from entrepreneurship (instrumentality) can satisfy the needs which are important for him (value), and (2) the more probable he sees that he is going to succeed in the tasks related to entrepreneurship. It is important to notice that all these are subjective perceptions, which means that entrepreneurial motivation can be very different between different individuals due to their different perceptions of entrepreneurship.

Prior research has dealt with several types of **push factors.** Specht's [29] literature review showed that the five most usually used contextual factors used as determinants of entrepreneurship can be grouped as social, economic, political, infrastructure development and market factors. A failure of a previous organisation, getting

fired, or concluding that the organisation or one's career is not progressing can also be treated as factors 'pushing' towards entrepreneurship. [27]

Data and measures

The base population used in this study comes from three counties consisting of 13 municipalities, and having a total population of 403.000 inhabitants. All inhabitants under 16 and over 65 were excluded and a randomly selected sample of 4500 persons was taken. After one reminder with a questionnaire the response rate rose up to 40,9% and thus the data consists of 1841 observations, representing the normal working age population.

The main purpose of the study is to find out whether there are differences between female and male entrepreneurial intentions, and whether signs of modern female entrepreneurship can be found. To allow for our comparative research design, we have four distinct groups which are based on the suggestions in the literature review. Thus we have 1) males, who have an entrepreneurial intention, 2) females, who have an entrepreneurial intention, 3) males, who do not have an intention and 4) females, who do not have an intention. The second group consisting of women carrying entrepreneurial intentions is of special interest to us, because we expect that the members of this group reflect indications of the suggested modern female entrepreneurship.

The groups are compared in terms of the following factors associated to motivational background of entrepreneurship: 1) push –factors, 2) pull –factors, 3) instrumentality of entrepreneurship 4) personal motivation structure, and 5) barriers to entrepreneurship. Intentionality was measured with a Likert-type question ranging from “I am sure that I’m not going to start a new venture during the next year” to “I am sure I’m going to start …”. The push –concept was operationalised by a 5-item Likert –type measure (see table 1) and the pull –factor in a similar fashion (see table 2). The instrumentality was measured by a comparative setting, where the respondents were asked to define, whether entrepreneurship is fulfilling certain factors related to work motivation better or worse than working as a hired employee (see table 3). The personal motivation structure was measured with a 10–item list of certain motivation factors. The respondents were asked to choose the 3 most motivating factors for them (see table 4). The barriers to entrepreneurship were measured with a 26–item list, which included various barriers from 7 areas: 1) personal characteristics, 2) unsuitability of the entrepreneurial role, 3) economic risk, 4) social risk, 5) current life situation, 6) lack of support in social environment, and 7) lack of support in economic environment (see table 5).

The data was analysed by comparing means and frequencies between the selected and formed groups. Through these comparisons it is possible to find out whether the females who have an entrepreneurial intention differ from other women and men.

ANALYSIS AND RESULTS

Entrepreneurial intentions were quite rarely found in the data. Only 1,3% of the respondents were sure that they were going to start a new venture within the next year. 4,4 % of the respondents were quite certain they were going to set up a new company and 11,6% were unsure about the future. As many as 1049 respondents (58,1%) were confident that they will not start up as an entrepreneur during the next year. Comparing between genders, men seem to have entrepreneurial intentions more often than women: 22,7% of men were sure, quite sure or uncertain of their becoming an entrepreneur, whereas only 11,5% of women chose the same alternatives. The most frequently mentioned sector for possible start-up was personal services: 41,6% of intending women and 26,1% of intending men aim to start-up in that sector. Industrial services was the target for 31,3% of women and 25,2% of men. These two sectors as well as retailing were practically the only routes for entrepreneurial action for women. In the case of men the distribution was more evenly split up into various types of enterprises.

To allow further analyses, the data was split into four groups: 1) Men, having an entrepreneurial intention (214 respondents; 12,0% of the data), 2) women, having an entrepreneurial intention (96; 5,4%), 3) men not having an entrepreneurial intention (728; 41,0%) and 4) women not having an entrepreneurial intention (739; 41,6%). The analysis was continued by studying the push and pull–factors, instrumentality, personal motivation structure and perceived barriers to entrepreneurship in these groups.

Table 1. Perceived push in groups of men (m) and women (w) having (+) and not having (-) entrepreneurial intentions

I am unsatisfied with…	all (sd)	m/+	w/+	m/-	w/-	F-value	sign.
… my earnings	3,32 (1,38)	3,51	3,68	3,21	3,31	4,99	,002
… the relation of my “input” and rewards	3,18 (1,33)	3,41	3,66	3,14	3,09	7,40	,000
… my career development	2,87 (1,32)	3,18	3,43	2,83	2,76	11,45	,000
… possibilities to use my ideas and creativity	2,68 (1,31)	3,04	3,35	2,62	2,56	16,24	,000
… possibilities of personal development	2,61 (1,36)	2,82	3,28	2,54	2,53	10.75	,000

The differences of perceived push–factors are shown in table 1. All the push–variables get higher values in both the groups of entrepreneurial intention. The other important result is the large difference between men and women having an intention: women have clearly higher values in most push–variables. The difference between women and men is largest in questions dealing with personal development, career development and the possibility to use one's ideas and creativity. Looking at the non-intention groups, there are practically no differences between women and men. According to the results shown in the table 1 it is possible to argue that push–phenomenon is closely related to entrepreneurial intention, and that the link is especially strong for women.

The presence of a pull–factor was measured by a 5 item set of statements. The results shown in table 2 reflect even stronger differences between the groups. Women and men differ in both categories. The main finding in this analysis is that the intending women seem to have a higher pull than the intending men. This concerns especially two variables. Women have a clearly stronger push in their intention to test a product or service they have developed and they also feel that their competencies are worth of selling more than men. On the other hand, in terms of pull the non-intending women stand out in the comparison. It seems that the non-intending women see practically no pull–factors in their current life situation. The only variable that could be seen as a pull-factor to entrepreneurship in this group concerns the selling of competencies. It seems that the pull–phenomenon is closely related to entrepreneurial intention. The differences are very big between the intending and non-intending groups. For women the difference is even stronger, which indicates that the women having an entrepreneurial intention may be quite different from the rest of the female group.

Table 2. Perceived pull in groups of men (m) and women (w) having (+) and not having (-) entrepreneurial intentions

	all (sd)	m/+	w/+	m/-	w/-	F-value	sign.
My competencies are worth of selling	2,90 (1,40)	3,88	3,94	2,89	2,49	82,12	,000
I have a good business idea	2,22 (1,13)	3,33	3,36	2,21	1,78	131,58	,000
I want to test a product or service	2,07 (1,27)	3,08	3,37	2,03	1,67	138,80	,000
My life situation is suitable	2,20 (1,25)	3,39	3,34	2,11	1,79	142,96	,000
I see an opportunity	1,87 (1,13)	2,89	2,62	1,86	1,50	112,00	,000

The instrumental value of entrepreneurship was measured with a 10–item set of statements comparing the outcomes of entrepreneurship with those of individuals working as a hired employee. The results shown in table 3 demonstrate clear differences between the intending and non-intending groups. The difference within items

dealing with independence is especially strong. While comparing the intending groups it is evident that women value entrepreneurship higher than men in some aspects. Moreover, women see the instrumental value of entrepreneurship much higher in terms of achieving a higher position in society. Also the difference in perceived opportunity to grow and learn get a higher mean value in the women's than the men's group. For women the difference is especially noticeable: the group of non-intending women systematically receive the lowest mean values, whereas the group of intending women receive the highest mean values. The difference is strongest regarding the perceived opportunities to use one's creativity and innovativeness. This result indicates again that the women having an entrepreneurial intention have to be quite different from the rest of the women and the differences are larger than in the male groups.

Table 3. The instrumental value of entrepreneurship compared with working as a hired employee.

Compared with working as a hired employee as an entrepreneur I could…

	all (sd)	m/+	w/+	m/-	w/-	F-value	sign.
…be more independent	3,64 (1,12)	4,03	4,32	3,55	3,53	25,02	,000
…have higher earnings	3,56 (1,12)	3,64	3,64	3,35	3,24	9,01	,000
…have a possibility to better decide on my working hours	3,47 (1,23)	3,77	4,04	3,37	3,40	13,54	,000
…have better a possibility to develop myself and learn	3,36 (1,12)	3,68	4,16	3,26	3,25	27,09	,000
…have higher organisational status and more power	2,98 (1,15)	3,11	3,32	2,85	3,03	7,18	,000
…better use my creativity and innovativeness	2,90 (1,40)	3,88	3,94	2,89	2,49	82,12	,000
…have higher social status	2,89 (1,07)	3,06	3,44	2,82	2,84	11,98	,000
…better relationships with peers	2,47 (1,03)	2,85	2,90	2,42	2,34	19,48	,000
…have more secure earnings	2,42 (1,11)	2,73	2,96	2,31	2,37	15,98	,000
…have enough free-time	2,33 (1,20)	2,58	2,65	2,27	2,27	6,22	,000

In addition to the instrumentality of entrepreneurship, we measured the motivation structure of the respondents. The most important motivators seem to be secure earnings, high payment and independence. Also the possibility to grow and learn appears to be an important motivation factor in general (see the table 4). On the other hand, status and power as well as the social value of an occupation do not motivate people on average.

Several differences can be found between the analysed groups. It seems that the personal motivation structure differs according to gender and intention. In the table 4 above the three most motivating factors in each group are expressed in bold type. It seems, that secure earnings is clearly a motivation factor for persons not having an entrepreneurial intention. High payment seems to be clearly a male motivation factor, whereas the possibility to grow and learn is more a female than a male motivator. Independence is clearly stressed as a motivator for those

intending entrepreneurship. The female group intending entrepreneurship differs in many ways in relation to both intending men and non-intending women. Independence, the possibility to grow and learn as well as the possibility to use one's creativity are typical motivation factors for intending women. In comparison with the non-intending female group the biggest difference is in the membership of a group item.

Table 4. Motivation structure in groups of men (m) and women (w) having (+) and not having (-) entrepreneurial intentions; % of respondents who chose the motivation factor among the three personally most motivating reward

	All %	m/+	w/+	m/-	w/-
Secure earnings	51,1	34,1	37,5	**52,2**	**56,7**
High payment	46,7	**50,0**	30,2	**54,7**	40,1
Independence	45,8	**61,2**	**63,5**	**43,7**	41,1
Possibility to grow and learn	44,9	**44,9**	**53,1**	42,0	**46,7**
Membership of a group	34,4	22,0	19,8	32,8	**41,5**
A possibility to use one's innovativeness and creativity	29,0	33,2	**45,8**	25,0	29,5
A possibility to plan and decide on one's own working hours	23,0	29,9	36,5	22,7	19,5
Enough free time	21,8	16,8	12,5	24,0	22,2
Occupation's social value	10,0	9,8	12,5	10,6	9,3
Status and power	6,1	8,4	11,5	6,5	4,3

Barriers to entrepreneurship were measured with a 26–item set of statements each ranging from 1 (no barrier at all) to 4 (decisive barrier). All the 26 barrier variables are listed in table 5 with a comparison between the research groups. In overall, the most decisive barriers to entrepreneurship were various fears of economic risk. Running into debts, insecurity of income, fear of losing property and uncertainty of the continuity of demand were all among the five top barriers. Also the current life and work situations were generally regarded as significant barriers to entrepreneurship.

In comparing the intending and non-intending groups the difference is systematic and clear: the non-intending groups seem to receive constantly higher means of entrepreneurial barriers than the intending groups. The non-intending men and women also differ quite clearly from each other, whereas the differences between intending groups are not so strong. However, in most cases the intending women have higher barriers than the intending men. The biggest differences between men and women can be found in items dealing with fears of running into debts, losing one's property and uncertainty about the continuity of demand. The intending women have lower barriers of entrepreneurship in such aspects as marketing one's know-how and the difficulty in commercialising one's competencies through entrepreneurship. These differences are, however, very small.

Table 5. Barriers to entrepreneurship in groups of men (m) and women (w) having (+) and not having (-) entrepreneurial intentions

	m/+	w/+	m/-	w/-	F-value	sign.
I fear of running into debts	2,52	2,71	2,80	3,14	34,76	,000
I fear of insecurity of income	2,51	2,58	2,78	3,09	37,60	,000
Entrepreneurship does not fit the current life situation	1,98	2,17	2,83	3,10	72,31	,000
I fear of losing property	2,34	2,56	2,64	2,91	24,92	,000
I don't trust in the continuity of demand	2,32	2,51	2,64	2,84	24,78	,000
It's not feasible to change my current job to entrepreneurship	1,97	1,96	2,70	2,80	40,96	,000
I don't want to market my competencies continuously	2,21	2,14	2,51	2,78	32,61	,000
I don't want to take the responsibility of others'. employment and incomes	2,15	2,30	2,39	2,84	44,58	,000
Entrepreneurship does not offer enough leisure time for me	2,10	2,31	2,52	2,71	24,30	,000
Entrepreneurship requires too much commitment from me	2,06	2,16	2,47	2,74	33,46	,000
I fear of hard competition	2,09	2,25	2,34	2,69	34,90	,000
It's difficult to commercialise my competencies through entrepreneurship	2,01	1,90	2,40	2,60	31,16	,000
I don't trust in getting financing	2,15	2,16	2,25	2,52	16,51	,000
My competencies are not general enough	1,83	1,96	2,22	2,58	45,41	,000
My tolerance of ambiguity is weak	2,01	2,07	2,20	2,47	19,88	,000
I don't have a good enough business idea	1,98	1,83	2,29	2,39	14,87	,000
I don't want to be known as a failure	2,06	2,14	2,20	2,27	3,32	,019
I avert the loneliness associated with entrepreneurship	1,73	1,78	2,01	2,29	28,72	,000
Entrepreneurship does not offer me enough mental freedom	1,77	1,70	2,04	2,15	15,56	,000
I don't want to ridicule myself with a bad idea	1,86	1,75	1,99	2,07	5,67	,001
I don't trust in the availability of suitable facilities	1,70	1,75	1,12	2,05	14,53	,000
I feel a lack of support from the social environment	1,81	1,63	1,87	1.88	3,73	,042
I don't trust in the availability of skilled work force	1,84	1,75	1,85	1,85	,46	,708
I feel a lack of support from the family	1,70	1,62	1,82	1,83	2,46	,061
I don't have enough commitment or hard-working attitude	1,67	1,65	1,73	1,76	,99	,390
I don't have an aptitude for service	1,65	1,51	1,86	1,59	14,08	,000

Once again the difference between the female groups is stronger than between men's groups. The most striking differences between intending and non-intending women can be found in items dealing with the current life and work situations. Also various fears linked to economic risk are much higher in the non-intending group. Personal competencies and adopted role models seem also to act as stronger barriers to entrepreneurship in the non-intending group than in the intending group of women. This becomes evident in comparing the differences in items: "I don't want to market my competencies continuously", "My competencies are not general enough", "It's difficult to commercialise my competencies through entrepreneurship", "I don't want to take responsibility of other's employment and incomes" and " my tolerance of ambiguity is weak".

According to these results it is evident that various barriers to entrepreneurship inhibit most people to proceed in their own processes of becoming entrepreneurs. This is especially evident for women. However, the analysis

suggests that there is a certain group of women, who do not perceive the barriers as being as strong as other women. Once again, who are they? In order to find out the eventual differences between these two groups of women a series of comparative analysis was conducted between the groups. Age, education, family background, and career status were taken in to the analysis. It was found that the intending group of women differ significantly from the other group only in two aspects. First, the women reflecting entrepreneurial intentions come more often from an entrepreneurial family than those women with no intentions of starting their own business. The other important difference was the career background of these women. The analysis shows that in the intending women's group there were more women with marketing experience than in the non-intending group. Interestingly, the women's educational level did not differ significantly between the groups.

DISCUSSION

The results of the study demonstrated clearly motivational differences between those women who have an entrepreneurial intention in comparison with both intending men and non-intending women. The intending women have stronger push and pull than their male counterparts. Also perceived instrumentality of entrepreneurship was more positively favoured among the intending women than men. Even though there were differences between women and men, the most striking difference was, however, the huge difference between intending and non-intending women. In almost all comparisons between various groups, the female groups represented the opposite extremes. This result may indicate a higher barrier to entrepreneurial intention among women than men. In other words, a woman has to be more unsatisfied, she has to have more promising opportunities in sight, more trust in her own capabilities and more faith in the entrepreneurship offering her a better future, before she starts to think about entrepreneurship. This might be one explanation behind the remarkable difference between male and female intentionality in a normal population.

The results of the study supported the reviewed literature in that intending women have a stronger push than men. In addition it was found that also the pull is stronger for intending women than men. What can be considered as a new result is the more positive attitude of intending women towards entrepreneurship as a way to fulfil their various work related needs than men. All these results seem to support the glass-ceiling hypothesis. However, the group of intending women is not a homogeneous one. Only two variables showed group level differences between intending and non-intending women: the marketing experience and entrepreneurial family

background. Distributions of age and education did not differ between groups, which suggests that the modern female entrepreneurship is still insignificant in the large population. Also the fact that almost a half of female intentions were aimed at personal service businesses does not indicate increase in modern female entrepreneurship. However, one-third of the intending women targeted their businesses to industrial services, which, again, could be regarded as a sign of modern female entrepreneurship. In summary, it is possible to conclude that signs of modern female entrepreneurship in Finland are quite weak. Also the distribution of male and female entrepreneurs seems to stay as it has been: one-third of entrepreneurs in Finland are women and 31% of all intentions are female intentions.

One explanation for the reluctance of women to start as entrepreneurs can be found in their motivation structure and the prevailing conditions of working life in Finland. According to the results of the study the three most motivating factors for non-intending women were secure earnings, the possibility to grow and learn and membership of a group. It is self-evident that entrepreneurship is not an option for a person ranking secure earnings at the top of her/his priorities. There also exists a living myth about loneliness of entrepreneurship, which contrasts strongly with the highly ranking social needs of the non-intending women. Work conditions have changed in a positive direction in Finland. The work related experiences of women have changed dramatically in the 1990's. When 28% of employed women considered their work very important in 1990, the rate was 46% in 1997. Training at work has risen at the same time (27% of the respondents had been in training in 1990 and 47% in 1997). In addition, 91% of women think that they are able to develop themselves at work.

It is fully understandable that a person, who is relatively satisfied with the prevailing conditions, does not seek other alternatives. Using the concepts of the expectancy theory of human motivation it can be concluded that the vector of power leading to entrepreneurship is not strong enough, because the value structure, perceived instrumentality or expectancy of success is weak. According to the results of this study the "weak link" is the value structure, which points to waged working rather than entrepreneurship. This phenomenon is similar between genders, but it seems to play a more important role for women than men.

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A new model for analyzing female entrepreneurship

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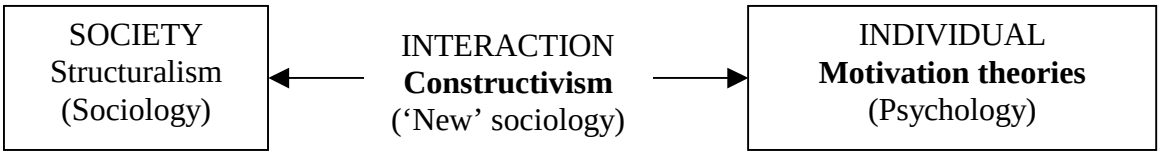
This article analyses the relationships between the following research areas :
1/ general theories in sociology and psychology,
2/ gender (social relationship between men and women),
3/ entrepreneurship (starting up of new businesses).

The idea of this combined analysis between these distinctive fields resulted from an on-going research project concerning female entrepreneurship. The connection that emerged in the study was based on the sociological theory of constructivism and the psychological theory of motivation.
After a brief review of the constructivist and the motivations theories, we present one of the main conclusion generated by gender studies as well as the main categories of motivations behind entrepreneurship. A synthesis model of these three fields is analyzed as a conclusion.

I – Presentation of constructivism and motivation theories

Constructivism is a research area grounded in sociology, whereas motivation theories belong to the psychology field. In a very simplified way, it is possible to represent these two fields by the following model[1] :



Boudon (1992) states that the epistemological debate in sociology is : "Should we study social facts as determinisms of systems to be explained in a causal way, or should we study social facts as the results of the individuals' autonomous decisions ?". In both cases, "the theories about human behavior are never neutral. They lead us to consider human beings either as unique and creative individuals, or as victims controlled by others (McNall & McNall, 1992, p. 18)". Today, sociologists tend to have moved away from radical views such as those described by structuralism, which was very active though in the 1960s and which considered individuals as entirely conditioned by existing social structures (Morin, 1999, p. 216).

It is interesting to briefly discuss the concept of *habitus* because it "aims at taking into account this double-way process : (...) 'conditioning' and 'freedom' (Dortier, 1998, p. 275)". The concept of *habitus* more precisely "indicates the psychic characteristics that can be influenced by education for example (or the professional environment) but which are neither unconscious, nor independent from the willingness, nor determined in a exclusively class system ; furthermore, these characteristics do not mechanically determine the subject's representations or acts. We would rather consider them as frames or guidance, from which the subject can get away with more or less ability (Boudon *et al*, 1989, p. 100)". Actually, the

[1] It would be necessary to add a fourth dimension to these model, the interpretation or representation one, which would lead us to the anthropology area. This might be the topic of a future research.

opposition between determinism and freedom is a caricature : an individual does not act in a completely mechanistic way, nor does he/she acts in a completely rational, free and conscious way according to one's objectives.

Constructivism enables to reconcile these opposite views. Corcuff (1995[2]) describes the 'social constructivism' theories, referring to authors who "attempt to get out of the traditional and now sterile oppositions (such as objective/subjective, collective/individual) considering social reality as the product of constructions and not as a fact (back cover)".
Constructivism is not a homogeneous area in sociology but, in spite of differences between scholars, there is to be found some converging trends. The synthesised definition suggested by Corcuff is : **"In a constructivist perspective, social realities are considered as historical and day-to-day constructions of individual and collective players.** (…) The word 'constructions' refers all together to the products of previous elaborations and to the process being under reconstruction. The concept of 'historicity' constitutes a major approach for the constructivists because :
1/ the social world is built on the basis of former pre-buildings (...) ;
2/ the former social forms are reproduced, integrated, moved and transformed whereas others are invented, in the acts and interacts of people's everyday lives ;
3/ this inheritance from the past and this everyday work open on a field of possibilities for the future (p. 17-18).
The main mechanism under the constructivist approach of social universes is the consideration of "**the way that structures constitute constraints and grounds for our acts** (p. 19)".

Within the global area of constructivism, the works of Elias, Bourdieu and Giddens have "aroused an increased interest over the last ten years in the French sociologists community looking for ways between the objective (or positivism) and the subjective, or between the collective and the individual (Corcuff, 1995, p.21)". These three authors "still attribute some predominance to the social structures and to the macro-aspects of reality, together with integrating more or less the subjective and interactional dimensions (ibid, p.21)".

One of the central outcomes by Norbert Elias[3] is the "attempt to go past the opposition individuals / society in the field of social sciences. Indeed, the individual is not considered as an external entity to the society, nor the society as an entity exterior to the individuals, and so the society is neither viewed as the simple aggregate of individuals unities (methodological individualism), nor as a whole independent from individuals acts (holism) (ibid, p. 24) ".
For Elias, the sociological field of study is composed by **'interdependent individuals '**. These interdependences are not always balanced relationships ; indeed, Elias shows more often the **desequilibriums through examples of inequality, domination and power**. "When we depend more on others than they depend on us, they have some power over us (Elias, 1970[4])".
The idea of interdependence is closely related to the one of 'margin of action'. This concept leads to the other classical opposition between freedom and determinism. Indeed, the degree of autonomy of each actor depends on the "web of interdependences in which the individual finds a **margin of individual choice** and which at the same time imposes **some limits to his/her freedom of choice** (Elias, 1969, p. LXXI)".

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[2] Corcuff P. (1995), *Les nouvelles sociologies*, Nathan, Collection Sociologie 128, Paris, 126 p.
[3] Norbert Elias : 1897-1990
[4] Quoted by Corcuff : Elias N. (1ère éd 1970), *Qu'est-ce que la sociologie ?*, French traduction, Paris, Pandora, 1981.

Pierre Bourdieu[5] developed the concept of "**structuralist constructivism**". By the concept of structuralism, he means taking into account the "objective structures independent from individuals' consciousness and willingness, which are able to direct or restrain their acts or their representations (Bourdieu, 1987, p. 147)". He grants some priority to the 'objective' aspect of structures in the sociological analysis. He considers the concept of constructivism as the second moment in the sociologist work, the 'subjectivist time'. After having identified the actual social structures getting away from the subjective representations, the sociologist must take into account the way in which individuals represent these structures for themselves, in order to understand what is driving them (individuals) when they want to maintain the structures or, on the contrary, make them evolve. Bourdieu distinguishes a primary *habitus*, which is incorporated through our first experiences, especially during infancy and teenage, and a secondary *habitus*, which corresponds to the adult life. He considers the habitus as an 'interiorisation of externality'. Bourdieu thinks that an individual is not conscious of this phenomena and that, what he can tell about it a posteriori ("the biographical illusion") must be reconstructed by the sociologist, taking into account a number of environmental parameters.
Besides, Bourdieu presents the concept of 'fields' as the part of 'externalisation of interiority'. "The 'field' is a sphere of social life that progressively became autonomous through an history of own social relationships, stakes and resources (Corcuff, p. 34)". As examples, we can refer to the political sphere, or the economics, the sports, the arts, etc. Within each 'field', and between 'fields' themselves, some consensus exist about the basic rules, the power and competition relationships according to the resources and the individuals. Bourdieu develops in particular the **concept of domination**, force relationships between social groups which have been historically fighting against each others, and interpretation relationships in their symbolical aspects. These relationships of domination originate because of different levels of resources (physical, cultural, economical).

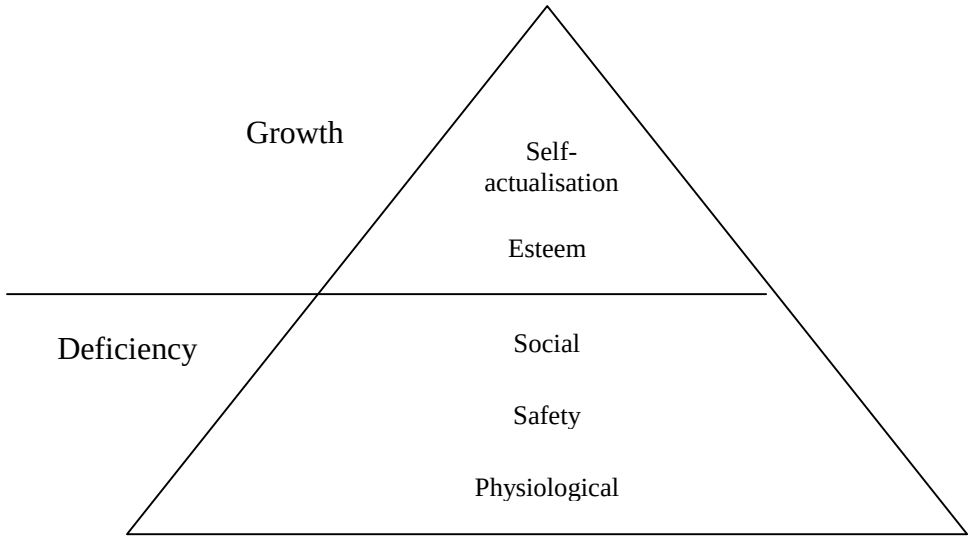
Anthony Giddens, with his **theory of structuration** (1987), presents a complex and particularly rich version of the constructivist approach. His perspective combines, as do Elias and Bourdieu, the positivist research traditions – objectivity prevails through the quantitative research for systematical links between cause and effect, 'averages' and 'typologies' ; society is an actor that *determines* the social relationships – and the more subjectivist traditions – which give priority to individuals, their perception of the world, and their ways to use their margin of action, with more or less distance to a pre-determined model (Gioia et Pitre, 1990).
In summary, Giddens informs us about the 'duality of the structure' ; existing social structures are indeed both the results of individuals' actions, and as a return (or rather it is a permanent dialectic), structures impose themselves on individuals and limit their margin of tactic (*constraint*) or on the contrary help individuals in their activities (*competency*). It is a circular dynamic. The theory of structuration establishes the 'competency' of social actors, understood as "everything that actors know (or believe), in an explicit or implicit manner, on the circumstances of their action and those of other people, and that they use in the production and reproduction of action (Giddens, 1987, p. 440)". Human beings are "capable of understanding what they do when they do it (*ibid*, p. 33)". However, this understanding of one's competencies is only partial. Giddens distinguishes the competencies that the individual can express (discourse), and those that the individual is not conscious of but which are very real (practical consciousness).
However the 'competency' of individuals faces many limitations : first the one of their subconscious, which are the forms of cognition or impulsion that are rejected ; then

[5] Pierre Bourdieu : 1930-

individuals act under the framework of "the structured characteristics of social systems that extend well behind the control of each individual, both in time and space (*ibid*, p. 75) " ; These characteristics, unknown to the individuals, lead to "unintentional consequences of their action". Individuals, even with the best capability and motivation, provoke by their acts some desired results, and others uncontrolled or even reverse effects.

As a concluding comment on constructivism, we can emphasize that "**Although individual behavior displays inherently conservative characteristics, individuals are important vehicles for and initiators of change over the long run** (Stevenson et Harmeling, 1990, p. 6)".

The theories of motivation are more simple to present. Actually, Maslow and Aldefer are considered as the principal authorities with complementary approaches.
Maslow's famous theory of motivation (1954) suggests a hierarchy of five major needs expressed by human beings through their acts[6] ; Maslow's theory develops the principle that, if these needs are not fulfilled, individuals do not behave in the most coherent or efficient possible way. A pyramid usually represents the five needs identified by Maslow :



Maslow's needs are activated in an ascending way, from the most 'basic' to the most elaborated, one after the other. The first three needs are grouped under the term 'deficient', which means that if they are not satisfied, there is a high probability that the individual will not behave in a normal way. The two other need, associated under the 'growth' label, are the ones which enables an individual to completely fullful one's potential.
The physiological needs correspond to the satisfaction of biological needs, such as drink, eat, and rest. The security needs refer to the necessity of living in an environment free of physical or psychological fears. The social needs refer to the desire of being part of a geoup, such as having friends, being accepted and loved by others. The need for esteem is the willingness to be respected for one's ideas and to attract others' approval ; for example, the desire to succeed, to reach a prestigious status, to obtain a higher position in a firm's hierarchy. At last, the self-actualisation need, on top of the Maslow's hierarchy, refers to the willingness of fullfilling one's personal potential, realise one's deepest desires.

[6] *'The need hierarchy theory' : physiological, safety, social, esteem, self-actualization needs.*

Some further research hasbrought some nuances into Maslow's theory, especially on the fact that needs were activated one after the other, as well as on his restricted view of five only fundamental needs.

To answer these criticisms of Maslow's theory, an alternative approach was suggested by Adelfer, under the name of 'ERG' theory (1972). His approach is far more simple as he identifies only three main categories of needs : existence – refers to the physiological and safety needs of Maslow ; relation – social needs ; et growth – esteem and self-actualisation. One major difference with Maslow is that Aldefer considers that any need can be activated without a specific hierarchical order.

II – Perceptions of gender relationships

A contradictory approach appears between two conceptions of the male and female relationships, through the works of sociologists, historians, political scientists, managers or even advertisers : the permanence of the male domination or the progressive evolution of women. Another way to present these two sides is to talk about 'pro-immobility' or 'pro-evolution'. New research orientations might enable to overcome this basic opposition.

The scholars who are convinced that the **domination** of women is continuing, in spite of an evolution of the domination forms, are the 'pro-immobilists'. "The radical perspectives consider indeed that the destiny of women has always been (and will always be ?) marked by an oppression which forms can vary but that remains profoundly identical (Frisque, 1997, p. 131)." This first described orientation, of the permanent domination by males, can be found mainly within the theoricians of oppression, who provide rather few landmarks, geographical or historical, that could support their arguments. One of them is Pierre Bourdieu, who insists on the "constances and invariances, at leats at the level of representations" of the masculine domination (Bourdieu, 1993, p. 64, quoted in Frisque, ibid., p. 131). Together with recognizing the visible evolutions – growth in the access to university education, to the salaried workforce, distanciation from the reproduction function, etc. – and the difficulty of firmly establishing the masculine domination, Bourdieu insists on the "permanences, so much in the objective structures as in the representations (1995, p. 84)". To comfort his argument related to the 'objective structures', he bases himself on the statistical reports regarding wages inequalities, the high proportion of girls in 'non-professional' education orientation, their difficulties to reach the highest levels of management, and suggests that : "To understand these permanences (…) it is required to look at different factors than external constraint or male bad will. But it would be as much naïve (and outrageous) to put the responsibility on women themselves, as it sometimes happens (Bourdieu, 1995, p. 84)". He refers particularly on the weight and the strength of "collective expectations" that influence teenage girls ; the positive or negative inticements, generated by parents, teachers and orientation advisors, would constitute a constant reminder of their "assigned destiny, based on the traditional vision principle.(…) Furthermore, they all tell about the difficulty to find themselves alone – or just a few – within mainly male classrooms (ibid., p. 85)".
According to Bourdieu, the causes behind the domination stillness are to be found in the symbolic representation of women, "whom being is a perceived-being, which places women in a permanent unsecure state or, worse, in a symbolic alienation. Provided with a being that is a look-alike, women are implicitely asked to demonstrate, in the way they hold and present their bodies (…), a kind of availability towards men (ibid., p. 86)".

Bourdieu's theory is developed in other words by Marie-Claude Hurtig and Marie-France Pichevin who denounce the "gender prisons", which refer to the many sex-stereotypes. For example, a similar behaviour will be qualified as 'wise' for a man and 'fearfull' for a woman ; these representations being shared by men AND by women (Hurtig & Pichevin, 1986, quoted in Fournier, p. 22).

On the contrary, many researches emphasizes the evolutionist view of a progress toward sex equality. Albert Brimo worte in the 1960s that "the arrival of women into industry and services has been accompanied by the progressive conquest of equality (1975, p. 8, quoted in Frisque, 1997, p. 131)". Those research works about the 'drives' and 'brakes' in the change of female activity enter as well in the evolutionary perspective.
Other authors talk about the evolution of the sex-stereotypes, positioning themselves within a domination perspective, but which would tend to decrease because, amongst others things, of the devaluation of the male stereotype of the 'macho, dominating and violent' (Welzer-Lang, 1997, quoted in Fournier, 1998, p. 22). The former stereotypes evolve with education and the happening of counter-models.

When only reading about these two theories, it seems difficult to conclude about the prevalence of one or the other within the occidental countries. Indeed, they are both arbitrary from the beginning, originating from a pessimist point of view (domination) or an optimist one (evolution). "It would be necessary to balance the ratio of the evolution and of the inequality perpetuation (Frisque, ibid., p. 132)".

Recently, some authors have suggested new ways to understand the gender relationships, which would enable to **go over the Domination-Evolution dialectic**. Two directions of research seem particularly interesting, the 'indetermination' on the one side and the 'identity' on the other side.

The heart of the feminist orientation is the recognition of "the women's right to position themselves, that is not being defined, judged or labeled in the name of any definition of the feminine, whatever positive or negative (Zaidman, 1995, p. 219)". This relates to what Lipovetsky (1997) identifies as well under the label "**undetermined woman**", whom characteristics is her "autonomy from the traditional power exerted by men on the imaginary-social definitions and significances of women (p. 236). He identifies the forthcoming of the undetermined woman since the middle of the 1960s. The undetermined woman refers to the contemporary woman. In principle, all possibilities are open ; each woman now can defines her own choices : which studies ? which career ? getting married ? having children ? etc. In reality, this new 'model' does not coincide with the disappearing of inequalities, and constraints together with cultural norms imposed on women are still heavy. However, pioneers open roads in many fields.

Another way, very complementary, to go beyond the Domination-Evolution dialectic arises from the assertion of the women's **identity**. The desire not to behave like men is increasingly vivid in the French culture – one historical feature being the courtesy relationships between the genders – and much stronger than in the American society for instance. Whereas in the United States, women claim first 'let us get into the field like men, next we will see if, being enough women, we can put forward a new style'. In France, it is mainly "for the new generations that the theme of identity overcame the one of equality (Fournier, 1998, p. 20)". "The self-actualisation and the personal development became a priority for individuals of the end of this century (Singly, 1996, quoted in Fournier, p. 21)".

The concept of identity is reinforced by two others approaches, namely the plurality and the mixity.
The concept of **plurality** is well defined in the quote of Françoise Collin, making some comments about Hannah Arendt's work : "A person's identity is complex and singular. The belonging to a community does not define it all, even if this person chooses one community temporarily or definitely by choice or under the circumstances pressure. (...) A woman is a woman but is not only a woman and is not a woman in the same manner as the others women (Collin, quoted in Frisque, 1997, pp. 219-220)."
The philosopher Sylviane Agacinski claims for the **mixity** in the defining of the society. Conscious of the inequalities, particularly in the political field where female presence is next to zero, she considers that the principle of 'parity' and the quota establishment would allow to promote mixity. "Thinking in terms of mixity is considering that there are two versions of the human being, et represent humanity as a couple (Agacinski, 1998)" because men and women cannot live without each other. In this view, the difference does not impede gender equality, but on the contrary, contributes to its enrichment (Fournier, 1998, p. 23).

III – The motivations behind entrepreneurship

The topic of motivations leading to the starting up of one's own business is certainly one of the most frequent in the entrepreneurship literature. Actually two steps must be distinguished : the idea of creating a business and the actual motivation for a venture creation (Duchéneaut & Orhan, 1999). In short, the first step is linked to the general environment around the entrepreneur, whereas the second step, the actual creation, is more related to the individual him oe herself. We will precise our position in the next sections.

The **society environment** plays a major role in the generation of the idea to create a business. This idea corresponds within an individual to the development of an entrepreneurial-oriented mind, which can leads one day to become an entrepreneur. Three factors seem to particularly influence the birth of an entrepreneurial spirit : the national socioculture, the family context and the educational system (ibid, p.1). These three components are deeply rooted in the environment of the society at large and can be analysed through the use of a macroscope, at the scale of a country or a region for instance.

This is what can be found in McClelland's works (1961) which suggest the concept of "self-actualization need" as a major drive to entrepreneurship. In spite of the limitations of his works about individual motivations (Gasse, 1978 ; Brockhaus, 1982), the interest of his research is to have demonstrated that **human beings are social products who tend to reproduce a certain model** : "The higher the number of entrepreneurs in a society, the more will be young people who tend to imitate these models, that is to choose entrepreneurship as a career orientation (McClelland, cité par Filion, 1997, p. 137)". Louis Jacques Filion adds that : "In order to the self-actualization need be fully orientated towards entrepreneurship and business start-ups, it is necessary that the current social values recognize and value enough the success in business to attract those people with a high self-actualization need (ibid.)".
What appears as well is that the entrepreneur is also a 'product of his/her environment' **Entrepreneurs "reflect the characteristics of the time and location where they live** (…) Entrepreneurship seems first of all as a regional phenomena ; cultures, needs, habits of a region shape behaviours. Entrepreneurs integrate, assimilate and interpret them, and this reflects in the way of doing things, of building up their business. (...) The highest relationship

frequency that a population has with entrepreneurs is with the local entrepreneurs. And local entrepreneurs are good mirrors of their initial culture. Thus they often constitute good transmission relais of regional culture that they make evolve as well (Filion, 1997, p. 140)."
In a more general way, Guy Minguet (to be published), in his introduction to a *Sociologie de l'entrepreneuriat*, asserts that : "Entrepreneurship is far from being a natural behaviour : it is socially constructed and invested by cognition and affects, interactions and rules, a memory and a future, former routines and learning in-process (p. 10)".

A somewhat paradoxal dimension of the influence of environment on the entrepreneurial drive can be found in the '**entrepreneurship of mal-adjustment'**. Kets de Vries (1985) claim that entrepreneurs are mal-adjusted people who need to create their own environment. Others scholars came out with similar findings: "Entrepreneurs create business, not so much because they are attracted by self-employment but because they react to a working environment that does not suit them (Filion, 1997, p. 139)". However, this trait, which could be defined as a 'negative' reaction, is diminished by others academics : "The American Shapero attributed business creation to the gap felt by the entrepreneur with the society. This thesis can appear to be somewhat excessive (Julien & Marchesnay, 1996, p. 62)".

The influence of the immediate environment, family and social in particular, is a major component of the culture or 'mental programmation' (Hofstede, 1991) of individuals. A study about French entrepreneurs showed that 66 per cent had at one close relative who was self-employed or entrepreneur (Rasse & Parisot, 1989). This acculturation by an entrepreneurial environment was confirmed by another French survey in 1994 which showed that most of the entrepreneurs knew someone who was maleading a business : family member (41 %), friend (21 %) or both (10 %) (Bonneau & Francoz, 1996). Such similar facts were reported from the United States, where Shapero indicated that starting up a new venture was becoming a 'pictureable act' when the hypothetic entrepreneur could refer to a model who tried it before (Shapero, 1975).

The decision to become an entrepreneur and the effective starting phase relate more to **individual characteristics**.
The most often cited entrepreneurs' motivations, are search for independence, desire for self-accomplishment, tolerance to uncertainty, initiative, innovation / creativity, risk-taking propensity (in a moderate way), flexibility, self-confidence, the internal locus of control, the result-orientation. This non-exhaustive list presents the 'positive' motivations to entrepreneurship, which can be grouped under the **'Pull' factors** label (Brush, 1990).

Some of this list's characteristics need a brief description as they are the most frequent motivation criteria found in quantitative studies about entrepreneurs. The **search for independence** is always ranked first in the surveys about the decision to start up a business. Entrepreneurs "prefer to earn less, but being their 'own chiel' (Julien & Marchesnay, 1996, p. 51)". Next is often ranked second the **self-accomplishment** need, or 'self-actualization' need as described by McClelland (1961). An American survey showed that entrepreneurs were scoring much higher than the managers on this particular trait (Carland & Carland, 1991), not even talking of the differences found with the average population. The '**internal locus of control**' relates to the will of influencing on the flow of events. It is one the form of self-confidence ; entrepreneurs feel less constrained by day-to-day situations or the environment pressure than most of the individuals. They think of events in terms of opportunities or, in the opposite case, that they do not constitute definitive brakes to their action. Such a behaviour may have been described as well under the concept of 'proactivity'.

On the opposite side of the driving motivations behind entrepreneurship, desrcibed as ‘Pull’ factors, Candida Brush identified **motivations of necessity, or factors ‘Push’**, in the context of the female entrepreneurship (1990), but most of these criteria described as Push factors can also applied to men entrepreneurs, with more or less intensity . She identified four ‘Push’ factors : income, dissatisfaction at work, difficulty to find a salaried job and the flexibility in the balance of own time.
The **income** motivation, in the necessity perspective, refers to a lack or insufficiency of financial resources. The objective of the firm is then often limited to the provision of an income for the entrepreneur. It is a subsistence activity. The entrepreneurship choice is related generally to strong external constraints, which result actually from choices made over a lifetime as well as environmental pressure.

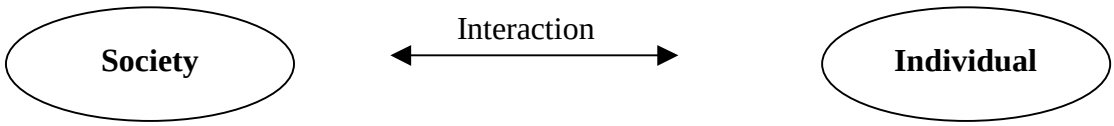
The criteria of **dissatisfaction at work** originates from two sources, both for executives or employees : being overqualified compared to the actual position, and the related blockage in terms of hierarchical progression, and eventually a frustration over wage and esteem levels, or another cause that can be the personal disapproval of the strategic orientations of the business, or the work climate, etc. Again, sources of dissatisfaction at work may arise from structural factors such as the internal promotion mechanisms, or individual factors mainly related to the ability to bear a dissatisfying work situation.

The difficulty to find a job constitutes the thord ‘Push’ factor. Obviously, this one can combine with the first two criteria described : income and dissatisfaction at work. In order to put an end to a period of dole or non-economic activity (family care), one way is to create his/her own job. Causes can relate to the overall environment : a non-dynamic employment area, the cultural distinction of roles between men and women which forces women to periods out of the professional field, economic downsizing, precarious jobs, etc. Or else, the difficulty to find a job can relate to a personal origin such as a low (or inadapted) level of qualification, the lack of experience, expectations higher than the job market, etc.

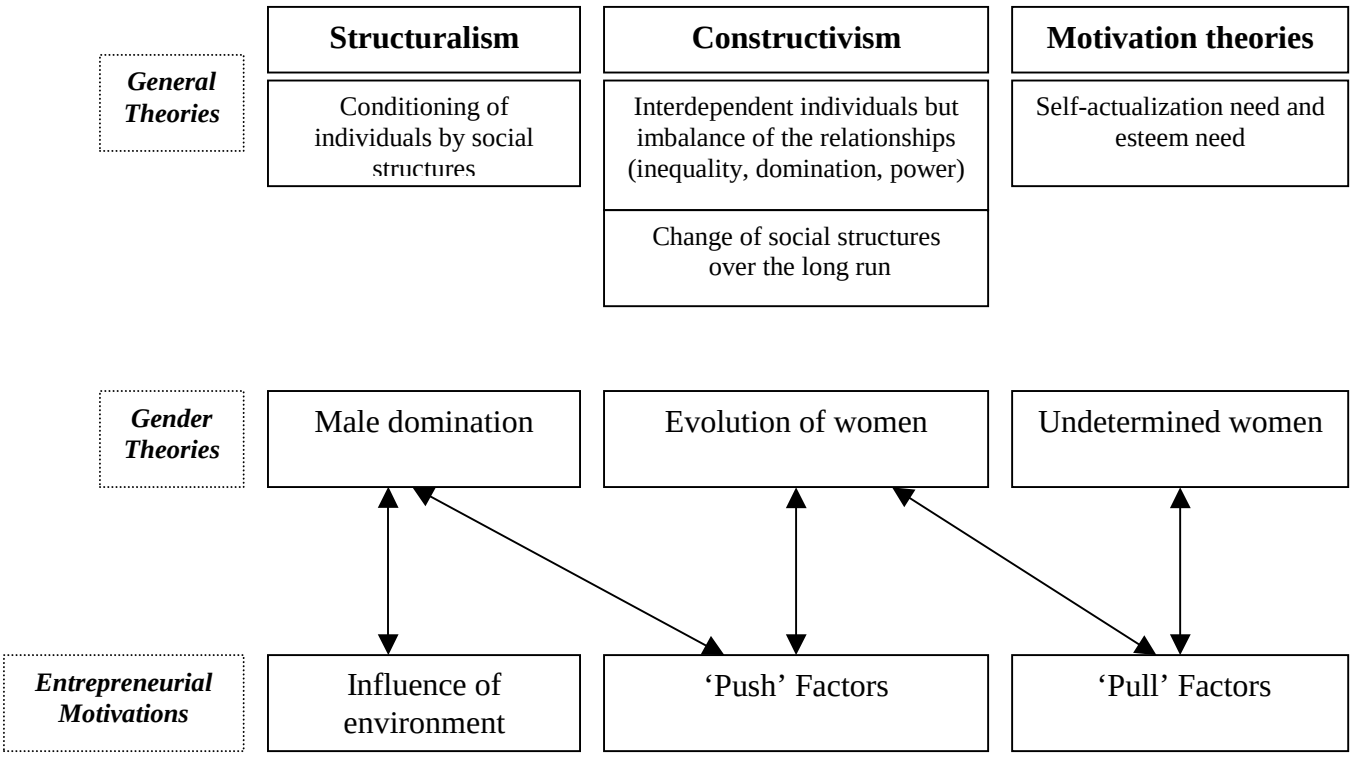
At last, the criteria of **flexibility in the way of managing one’s time** would be specifically feminine, in all types of societies. However, besides the question of the family care, men and women can wish to organize their time in order to devote more time to extra-professional activities.

IV – Synthesis : general theories, research about gender, research on entrepreneurship

Let us first remind of the initial model of interaction that we described at the beginning :



Following our separate analysis of the three fields of research, some major convergences emerged, that the following model attempts to represent :



The model presents analogies between the three areas of research, which are the general theories in human sciences, the gender theories and the research on entrepreneurial motivations (each is presented in the horizontal way), with the vertical dimension giving three main views of analysis, which are the structuralism, the constructivism and the individual approach – through the theories of motivation. We do not develop once again the horizontal parts as this was the purpose of the previous sections of the article.

The vertical reading suggests connections across the general theories, the gender theories and the entrepreneurial motivations. We perceived that, for instance, the male domination approach, and the influence of the social and family environment on entrepreneurial motivations, could be related to the structuralist view of society. We now develop further each vertical part of the model.

Structuralism is a way to view society without considering the individual actions at all, as individuals are perceived as entirely conditioned by social structures. In a similar way of viewing the world, some research about gender consider the masculine domination as a permanent and atemporal data, independent of men and women within a particular society, even if it is recognised that the forms of domination are evolving. On the side of entrepreneurship, one of the recurrent findings is the existence of a close environment positive to entrepreneurship, and often with relatives or friends already working as self-employed. Entrepreneurship then would not be a matter of innovation but mainly the reproduction of an existing model. Indeed, many are those who think that entrepreneurs are 'born'. This would

establish a kind of genetic and sociological cause to the entrepreneursship process in which individuals show no particular willingness to become an entrepreneur ; they are 'meant to act' as such.
We then consider the female entrepreneurship as a form of masculine domination, which would manifest itself in two ways : the first one refers to the cases when a wife or a daughter – or a female relative in general, is strongly encouraged to takeover an existing business, whereas she would have liked to pursue with another type of activity ; the second ways refers to the difficulties encountered by women in the professional field and which push them into the creation of their own job, in the context of necessity or complete dissatisfaction with their current position.

Constructivism sets out the interdependence between individuals but claims also some disequilibrium within these relationships (inequality, domination, power). The theory of structuration (Giddens) conceived the concept of circular dynamic between structures and individuals ; individuals are perceived as agents of change over the long run. Research on gender that describes the female situation in terms of evolution can be situated within this constructivist view ; scholars or feminists claiming the evolution of women consider the historical dimension over the broad picture, like centuries of female history, but as well the most recent progress such as statistics about women in politics and management positions. About entrepreneurship, we see as well the motivations driven by necessity (Push factors) as related to the constructivist approach. Indeed this type of entrepreneurship seems to be the best compromise between structural 'constraints' (job market, dissatisfaction with the firm's working conditions or desire to balance professional with family requirements) and the 'competencies' or individual resources.
About female entrepreneurship, executive women enter within this constructivist scheme. Executive women, or women who have developed a particular skill that can be turned into a business, have a specific 'competency' but they also face 'constraints'. These constraints can be a blockage in the hierarchical promotion (glass ceiling) or a 'traditional' family structure that put them in the role of main caretaker, which calls for a readjustment of the time balance. Women then see entrepreneurship as a way of going around those environmental constraints.

Psychologists distinguish various levels of an individual's motivations. When 'deficiency' needs are satisfied, it is argued (Maslow) that individuals turn themselves to 'growth' needs' fulfilment : the esteem and the self-actualization needs. The women's desire to define themselves, to have their own identity recognised, apart from the men's view and the sociostructural norms, as falling into these individual's needs for esteem and self-actualization. Entrepreneurial drive (Pull factors) relate as well to this category of 'growth' needs : self-actualization can be satisfied through entrepreneurship – even if entrepreneurship is certainly not the only way, depending on each one's objectives.
Some interviews with women entrepreneurs, as well as the current level of creation by women in the area of services to business, are representative that more and more women choose entrepreneurship in a deliberate way. Because they had a vision of a service or a product, or just because they wanted to achieve a business project in their own name, women become entrepreneurs, driven by 'Pull' factors. This takes women one step further into the overall evolution of the women's possibilities of choice. Female entrepreneurship can become a life-style choice, or one moment in a career, or the way to put one's creative views into action, etc.

In summary, this synthesis model presents relationships between entrepreneurial motivations and gender theories, within the context of industrialized societies. The use of general

sociological and psychological theories enables to generate a renewed vision of the female entrepreneurship and their motivations to create a business. Besides, the relationships established between very different theories seem to bring in a new vision of entrepreneurship at large.

However, the conceptual model has presented its own limits, in the sense that we could not cover all the general theories developed in the social sciences. Furthermore, the attempt to synthesise a rich context into a model obviously simplifies reality.

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Title: How does investing in information technology enhance the franchisor-franchisee relationship?

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SUMMARY

Information technology is being adopted in many franchise systems to improve relationships between franchisors and franchisees. However, little research addresses the extent to which investments in information technology enhance these sorts of relational exchanges, and none explores the franchise sector in particular. This study aimed to address this issue within franchise systems by surveying the views of Australian franchisors about the effects of their investments in information technology upon their franchisor-franchisee relationship. We focused on franchisors because they usually make the decisions about the introduction of information technology into a franchise system.

First, a framework of the structure of a relationship between business alliance partners was synthesised from the business-to-business literature because no literature had directly addressed the issue in franchising. We hypothesised that this framework could be used to measure the effect of information technology on seven elements that involve both the technical and social aspects of a relationship: equity, competence, trust, conflict, benevolence, commitment and investment. A sampling frame of all Australian franchisors was mailed a questionnaire with several items measuring each of these elements, asking them how much their investments in information technology had affected each element.

Structural equation modelling techniques were used to analyse the data. The results provided support for the conceptual framework, with the franchisor's increased technical competence from information technology improving the social elements in a relationship but that relationship being secondary to further technical investment. An implication for franchisors is that although the drivers and benefits of investments in information technology are primarily technical, the investments also operate through the social elements within

their franchise system and these social elements therefore influence the success of their ongoing information technology investment.

INTRODUCTION

Information technology is introduced in many franchise systems to enhance business processes and to facilitate communication. For example, many franchise outlets have used point-of-sale systems to facilitate daily operations and to customise and speed the preparation of reports. In the last few years attention has also turned to computerising the processes linking franchisor and franchisees. IT between franchisor and franchisees presumably enhances efficiency within the franchise system. At the same time, increasing use of IT can potentially harm the quality of the relationship between franchisor and franchisees. This study was designed to investigate the extent to which investments in IT affect the technical and social elements within the franchise system.

The main parties in a franchise system are the 'franchisor' and the 'franchisees'. The 'franchisor' is the company, person or firm granting a contractual license to another party; the 'franchisee' is the company, person or firm obtaining a license from a franchisor [1]. The franchisor, company-owned outlets, and franchised outlets together comprise the 'franchise system' [2].

There is a need for regular and frequent information exchange within the franchise system. The franchisor communicates to franchisees in order to inform franchisees about new and updated procedures, to provide up-to-date pricing and product information, to supply marketing information to the franchisees, and to provide on-going training [1]. The franchisees communicate to franchisors in order to provide performance data on a regular basis. Apart from the two-way information flow within the franchise system, there is communication with external parties including suppliers, banks, advertising agencies, and consultants. Close and regular information links between organisations suggest that there is an opportunity for the use of IT to improve efficiency and effectiveness of the links and transactions between organizations within this network [3].

Nevertheless, little has been published about the use of IT for communication within franchise systems. Simeonson and Anstadt [3], Sen and Lee [4] and Nault [5] contribute theoretical papers on the potential impact of IT on the development and efficient operation of franchise systems, however, none of these papers provide analysis of empirical data. Cavaye et al. [6] report on an Australian empirical study investigating factors which enhance adoption of IT links between franchisor and franchisees. However, there has been no previous, structured investigation into the effect of IT on relationships between franchisors and franchisees. That is, the trend for IT to replace mail, fax, telephone and face-to-face contact enhances business processes, but can it affect relationships between business partners in undesirable ways by undermining social links?

Thus this study surveyed Australian franchisors about their use of IT with franchisees and about their perceptions of consequent changes in relationships with franchisees. Essentially, we found support for a framework about relationships that is somewhat different from the extant literature about business-to-business relationships. An implication for franchising research is that this new framework for understanding the franchisor-franchisee relationship has to be tested further in other countries and in non-franchise contexts. Our contribution is this first step towards that framework and an improved understanding of social and technical elements in any business-to-business networks.

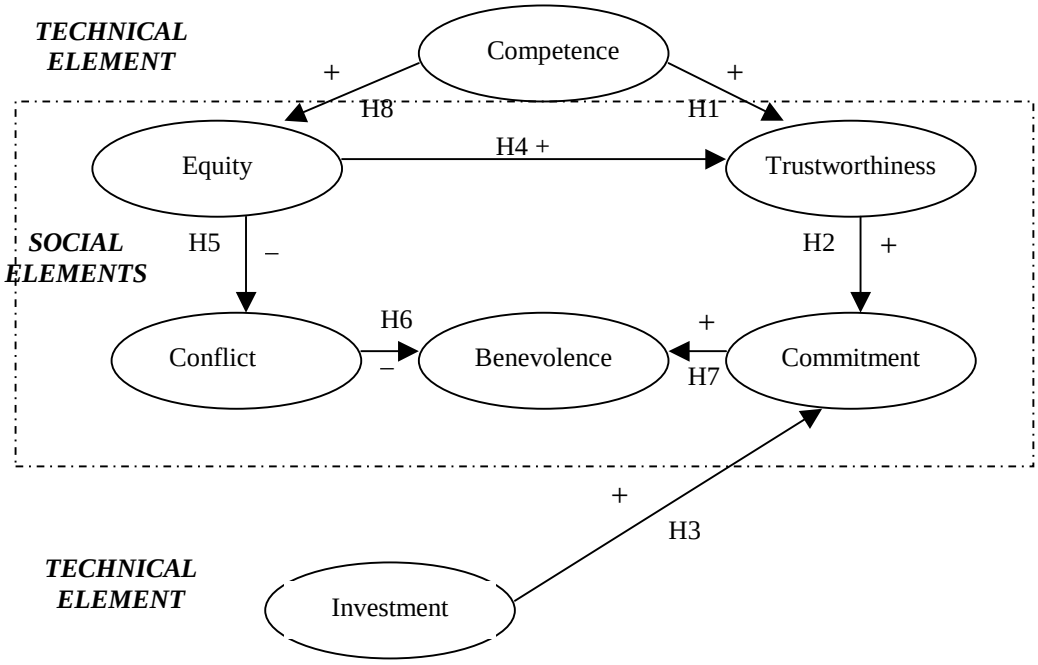
The paper has three main sections. First, business-to-business marketing literature is reviewed in order to develop a framework of the structure of relationships between business partners in a franchise system. Then details of the survey are outlined. Next, survey findings are discussed. Finally, conclusions are drawn and their implications for franchisors and further research are noted.

CONCEPTUAL FRAMEWORK

The foundation for this research was the extant literature on relationships in non-franchise forms of industrial networks, especially business-to-business networks. We identified seven core elements in this literature and developed a model of their interrelationships, as shown in figure 1. The model will be explained next, starting with the five elements about *social* aspects of a relationship like trust and commitment, before moving on to the

two *technical* elements of competence and investment. Then, we suggest a modified model that we hypothesise is particularly appropriate for the franchisor-franchisee relationship within an IT context.

Figure 1 Model of social and technical elements in a relationship



Our distinction between social and technical elements has not been emphasised in previous *empirical* research, although the distinction is explicit in the non-empirical literature [7]. By *social* elements, we refer to investments of time and energy to produce positive interpersonal relationships between the partners. In contrast, *technical* elements are forged when two companies adapt to each other in some economic or structural way such as product or process adjustments [8], for example, investments in assets that are dedicated to a particular relationship such as 'just in time' deliveries on demand. We refer to these elements in this paper as 'technical' elements rather than 'economic' or 'structural' elements because 'technical' seems more appropriate for the process adjustments brought about by IT. We consider figure 1's five social elements next.

Trust. The first element is trust. Trust is considered one of the core features of a relationship: 'trust underlines the whole thing, without it, it is just a waste of time' ([9], p. 33). Most research has concentrated on two components of trust. The first component is cognitive and is based on confidence in the role reliability of the partner. This component could include competence or contractual trust identified by Sako [10]. The second

component of trust is behavioural and is based on confidence in the *intentions* of the partner [11] [12] [13]. This component could include goodwill trust identified by Sako [10]. In this behavioural trust, a partner is not expected to display opportunistic behaviour that grasps a short-term win-lose outcome at the expense of a future stream of long-term win-win outcomes that will benefit both partners.

In brief, trust appears to be critical in a relationship – it has 'a central role in the development of marketing theory' ([14], p. 35). It has one aspect that is related to 'technical' roles and their reliability, which is called 'competence' below, and another aspect that is related to more 'social' factors like intentions in the future, which is called 'commitment' below. We explore the links between trust, and technical competence and social commitment in this research.

Commitment. The second major element of a relationship is commitment, that is, intention to continue the relationship into the future [15]. Like trust, commitment has two aspects that can be explicitly linked to social and technical elements in this research. The first, social aspect is affective commitment, that is, wanting to continue the relationship because the partners *like* their relationship [16]. This affective commitment is sometimes considered to be the end point of the development of a relationship because it ensures a relationship will continue into the future. The second, technical aspect is calculative commitment caused by the presence of switching costs that 'lock' at least one partner into the relationship. These switching costs are created by investments in the technical elements of the relationship. For example, switching to another supplier could involve costly re-engineering of processes.

In brief, from the above discussion about trust and commitment, and about their links with each other and with technical elements, we hypothesise the following linkages:

H1: Competence is a positive determinant of trust

H2: Trust is a positive determinant of commitment

H3: Investment is a positive determinant of commitment

Equity. Trust and commitment are the most common elements used to understand relationships. But they are both related to equity or a sense of fairness and so equity is a core element of the social aspects of a relationship. That is, equity is a fundamental element of ethical exchange [17] because partners *share both benefits and costs*

in their long-term win-win relationship. Equity is an antecedent to trust and commitment, as implied in the discussion of reliable intentions and affective commitment above. In brief, we predict the following relationship:

H4: Equity is a positive determinant of trust

Conflict. All the discussion above of win-win relationships does not mean that conflict between partners does not occur, for costs go along with benefits, as noted above. Conflict *must* occur and so it needs to be incorporated into our model. However, in a successful relationship, this conflict is resolved through negotiations and other conflict resolution processes [18], that is, communication and bargaining [19] is used within relational social norms [20] such as a sense of fairness or equity. We therefore hypothesise that equity will have a negative effect on conflict:

H5: Equity is a negative determinant of conflict

Benevolence. The final social element we consider is benevolence. This has been included in this research as a form of 'overall' or 'capstone' social element that encapsulates and is the end point of all the social elements. The inclusion of such an overall social element would seem to be necessary in this research where the differences and linkages between social and technical elements are investigated. Indeed, benevolence has been defined explicitly as a social element that is not the same as a technical element: 'the sentiments of friendship and the sense of diffuse personal obligation which accrue between individuals engaged in recurring contractual economic exchange' ([21], p. 460). This social element is the end-point of a series of exchanges where commitment has been increased in the relationship over time, as conflicts are resolved through a sense of fairness. Thus, commitment will be considered to be an antecedent of benevolence. In brief, we hypothesise two more linkages between elements in a relationship:

H6: Conflict is a negative determinant of benevolence

H7: Commitment is a positive determinant of benevolence

Two technical elements. Most relationship marketing research appears to have concentrated on social elements like those above. However, the discussion above has identified links between social elements and the 'technical' element of role competence in the cognitive aspect of *trust*, and the 'technical' element of investment with calculative *commitment*. We need to consider how these two elements fit into figure 1.

To begin, consider that *competence* is an antecedent of trust. Demonstrated competence leads to performance satisfaction and may be defined as the degree to which business transactions meet performance expectations [22]. Thus role competence will build calculative trust in a relationship, as noted in the discussion of trust above. However, the technical roles that each partner plays depend on their competencies and so these roles will also influence equity. Although both partner's inputs and outputs may differ considerably, exchange participants are likely to consider the extent to which an exchange partner fulfils their role expectations when making judgements about equity or fairness. Conceptually, competent parties would be viewed more favourably by their exchange partners if their skills and abilities lead in turn to higher levels of perceived fairness. Thus, we hypothesise that competence is an antecedent of equity:

H8: Competence is a positive determinant of equity

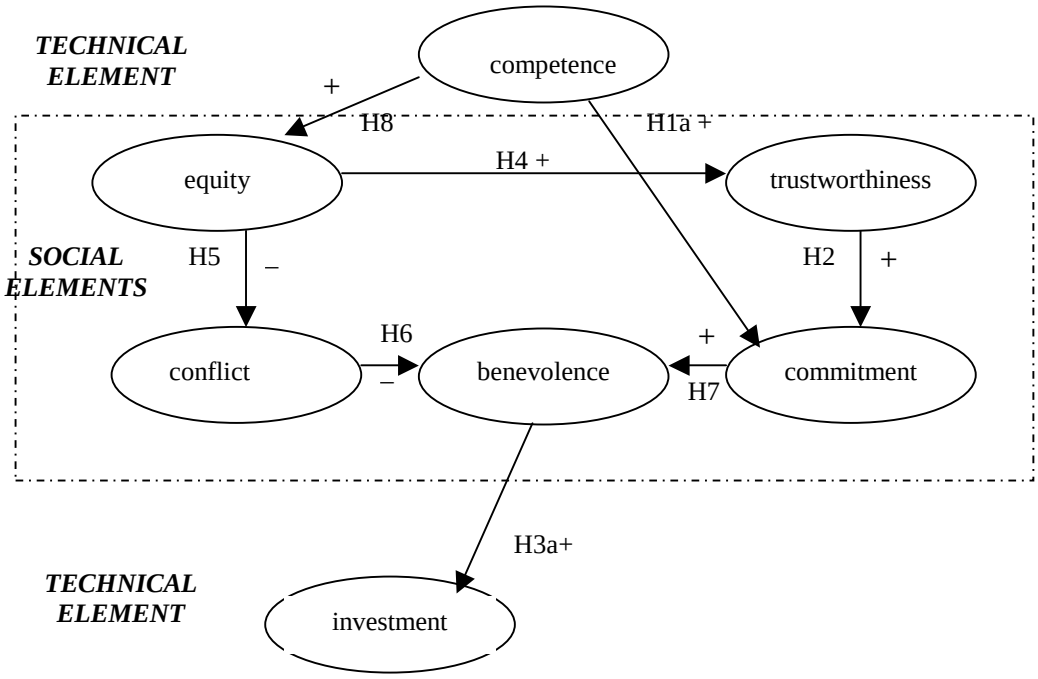
After competence, the second technical element is investment. We have already noted that it links with calculative commitment in the discussion of commitment above, and included it as H3 above.

Rival model for IT in franchise systems

Figure 1 showed a conceptual framework developed from the *literature*. However, two changes to that framework appear to be necessary for it to be suitable for the IT/franchise context, producing the second model shown in figure 2. First, a franchisor would adopt information technology to primarily improve his or her own competence as franchise system leader rather than the *partner's* competence. Thus the element of partner competence that previous research has focussed on in this research is not the same for this research, that is, competence is not an antecedent of trust in a franchise system. Instead, we hypothesise that competence has a direct influence on commitment, rather than an indirect influence through trust. That is, increases in franchisor competence from his or her IT adoption will be an antecedent of his or her commitment because the IT adoption will allow the franchise system to operate more effectively through improved reliability of operations and so increase his or her commitment to the franchise system. Thus H1 can be modified for IT investment in a franchise system, to become:

H1a: Competence is a positive determinant of commitment

Figure 2 Modified model of social and technical elements in a relationship, for IT adoption in a franchise system



In turn, we hypothesise that investment will not influence commitment through a 'locking effect' because the partners in the franchise system are locked in anyway through their franchise agreements and fees. Instead, we hypothesise that benevolence has a direct effect on investment. From previous research's emphasis on social elements within a relationship, it might be thought that the social element of benevolence could be more important than the technical element of investment. However, we hypothesise that a franchisor is *more* interested in 'technical' profit and investment than in feelings of 'social' benevolence. Thus H3 can be modified for IT investment in an franchise system, to become:

H3a: Benevolence is a positive determinant of investment

METHOD

Research setting

Our research setting consisted of franchisor-franchisee relationships in Australia. *Franchisors* make decisions about the introduction of information technology into a franchise system and are the focal actor. Further, their perceptions drive managerial actions. Restricting the setting to franchisors minimised extraneous sources of variation like types of distribution channel and power inequalities within franchise systems. Moreover, each nation has its own legal, cultural and historical context of franchising and so delimiting the setting to Australia was appropriate for this exploratory research. The unit of analysis was the franchisor-franchisee relationship.

Measures

The purpose of this research was not to explore the nature of relationships, for it was 'testing out' research that examined the application of an established theoretical framework to the new area of information technology in franchise systems [23]. Thus, the operational definitions of elements were taken from the literature rather than being developed from scratch. The items were modified slightly so they would be appropriate for our research context. For example, Morgan and Hunt [15] used this item to measure trust: 'In our relationship, my major supplier can be trusted to do what is right'. Our equivalent item was: 'Investments in information technology have improved my trust that the franchisee will do what is right'. Indeed, the common root of *all* the items was, 'Investments in information technology have…' Moreover, we used only three or four items to measure each element although US researchers have sometimes used more, because our experience in Australia has shown that these were the most appropriate [24] and that many Australian business people think more than three or four items becomes repetitive and silly. Three or four items for each latent element are required in structural equation models [25]. A copy of the questionnaire is available from the first author.

Trust was measured with Morgan and Hunt's [15] established items about confidence in a partner's integrity (four items). *Commitment* was also measured with Morgan and Hunt's established items about a partner's attitudinal orientation (four items). Items to measure *equity* were based on Kumar, Scheer and Steenkamp [26] and Oliver and Swan [27]. Their dichotomous items were made into a 7-point scale to be like the others in this research (three items). *Conflict* was measured with items from Kumar, Stern and Achrol [28] and Anderson and Narus [29] that had been successfully used in industrial relationships research (three items). Measures for the two technical element elements of competence and investment were also based on previous research. *Competence* refers to skills and abilities, and the items were again taken from Kumar, Stern and Achrol [28] (four items). Three items for investment were adapted from Frazer and Perry [30].

All these items to measure each element were appropriate because they were evaluated using confirmatory factor analysis. All items fitted their element or latent variable with a t-value for the regression coefficient above 2.0, indeed the smallest t-value was 5.3 and most were above 8.0. That is, all measures demonstrated acceptable levels of fit, convergent validity, discriminate validity and reliability.

Data collection and the respondents

Data was collected by mail survey because measures of the theoretical elements had been developed in previous studies (as discussed above) and so they did not require an explanation in an interview or over the phone. A mail survey also gave us access to many more franchisor-franchisee relationship all across Australia than would have been possible through personal interviews. The questionnaire was carefully designed according to the proven total design method of Salant and Dillman [31].

The sampling frame was a list of all Australian franchisors maintained over ten years by the fourth author that has been used in many surveys of franchisors. There is no alternative because there is no required registration of all franchisors in Australia. The mail out was sent to the complete list of 693 franchisors in 1998. Fully 175 franchisors replied, giving a satisfactory response rate of 25 percent for this type of survey of business people where 15 percent becomes questionable [32]. Only 113 of the 174 were able to answer the questions about investment in information technology, because the others had not invested. This figure of 113 is within the

normal bounds of 100 to 200 for structural equation modelling [33]. In brief, the data is the best and only data that can be obtained to explore the phenomena studied in this research for the first time.

The respondents provided a reasonably representative profile of all Australian franchisors. Replies were obtained from all states, with some franchises starting in 1967 through to 1996, and with turnovers ranging from $9 000 000 to $17 000. Moreover, the respondents provided a picture of *IT emerging as an important issue* in franchise systems. Of the 174 respondents, 28.9 percent saw no need for IT linking franchisor and franchisees, but others had started to do this and fully 19.1 percent had a complete IT links between franchisor and franchisees. Indeed, as many as 53.7 percent had implementation and use of franchise wide IT systems written into contracts for new franchisees and in renewals of existing franchises. The franchisors were split 60.6 percent between services and 39.4 percent retail, with 50.4 percent of the services using or contemplating IT for their franchise system, and 43.1 percent of retail.

Results for the structural equation modelling

The data was analysed with the structural equation modelling program LISREL. Table 1 shows the covariances of the seven latent variables. The magnitude of these relationships provides initial support for our conceptual framework. However, structural equation modelling techniques can be used for a stronger test of the hypotheses, because these techniques hold constant all the nonspecified structural relationships and account for measurement error.

Table 1 Covariances among the seven latent variables

	1	2	3	4	5	6	7
1. Trust	1.000						
2. Commitment	0.448	1.000					
3. Investment	0.254	0.314	1.000				
4. Competence	0.370	0.747	0.317	1.000			
5. Equity	0.572	0.550	0.415	0.648	1.000		
6. Conflict	0.470	0.452	0.478	0.533	0.823	1.000	
7. Benevolence	0.425	0.525	0.597	0.531	0.695	0.801	1.000

After establishing the measurement model was appropriate, the next step was to test the structural model. This step establishes if the latent variables in the two figures above fit the data. The first model in figure 1 provided

poor fit to the sample data, as expected because it was not modified from the extant literature for a franchise system. In contrast, the modified model in figure 2 which was developed for IT investments in franchise systems provided good fit to the sample data (chi-square = 493.5, d.f. = 244, p = 0.0, RMSEA = .956, GFI = 0.748 , CFI = 0.874 , PNFI = 0.691). All of the paths in the model of figure 2 were significant at the $p < 0.05$ level, which provides additional evidence that the modified model fits the sample data well. Findings about each hypothesis are described subsequently.

CONCLUSIONS AND IMPLICATIONS

This research investigated the effects of the introduction of information technology on franchisor-franchisee relationships as perceived by the decision-making or focal actor, that is, the franchisor. This innovative research showed that technical as well as social elements are important parts of this relationship.

Consider each of the hypotheses in turn, by looking at the *right hand side of figure 2* first. Competence is one of the driving forces in the IT investment decision. Franchisors perceive that their competence to execute their role is enhanced by IT, and in turn, that competence makes the members of the franchise system more committed (H1a). Trust also enhances commitment (H2). But the initial investment is not exogenous as initially hypothesised (H3), for IT investment is a *result* of the social element of benevolence (H3a) and *not* a *cause* of social elements. That is, social elements are not more important than technical elements and so do not deserve to be researched apart from technical elements. This is the first research that investigates this linkage between social and technical elements and establishes the primacy of technical elements despite their neglect by empirical researchers.

Now consider the *left hand side of figure 2*. Equity does influence trust (H4), although this too has rarely been investigated. Moreover, as expected, equity has a negative influence on conflict (H5), which in turn has a negative effect on benevolence (H6). These three linkages concern 'subjective' social elements. However, the 'objective' technical element of competence has a direct influence on equity (H8) and so is a key driver of the entire relationship process illustrated on the left hand side of the figure. Of course, it is a key driver of the important element of commitment on the right hand side of figure 2, too.

In summary, both technical and social elements contribute to relationship success within the context of IT within a franchise system. We find that the technical element of competence is the starting point for understanding relationships, and the technical element of investment is the ending point of this understanding. An implication of this finding for *franchisors* is that the technical elements provided by investments in information technology can indeed be used to enhance the efficiency and effectiveness of their franchise system, but those technical elements operate through social elements. That is, during and after investments in information technology, franchisors should recognise that more social aspects of exchange need to be developed for franchise systems to be successful. An implication for *further research* flows from our innovative attention to both social and technical elements. Our finding of how they are linked together could be tested in franchise systems in other countries; as well, the research could be done in non-franchise systems where the peculiar characteristics of franchise agreements and fees do not exist. In particular, whether H# or H3a operates in non-franchise systems would be a useful test of the importance of the technical element of investment within a business-to-business relationship.

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LIMITATIONS OF FRANCHISING FOR SMALL FIRM DEVELOPMENT: PUBLIC ATTITUDES AND AWARENESS IN BRITAIN.

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Summary

One of the difficulties small businesses encounter when trying to grow through franchising is the recruitment of suitable franchisees. This paper argues that the level of awareness and understanding of the concept by the general public will affect the ability of small firms to grow through franchising: people will only apply to become franchisees, and will only attempt to grow their existing businesses through franchising, if they are informed about it and the opportunities it afford. This paper examines, therefore, the public awareness of franchising in Britain; how well the concept is understood, how it is perceived and the implications for the future of the franchise industry.

A sample of 1250 members of the public were surveyed in five city centres. The results from the survey suggest that approximately a fifth of those questioned had no understanding of the concept, and only a tenth demonstrated a clear grasp of the term. The results revealed that understanding varied by age, occupation and location.

The paper concludes that if franchising is to continue to grow and to achieve its potential for the creation of self-employment and the growth of small firms, public awareness needs to be raised and the image of the sector needs to be improved.

Introduction

Franchising has long been seen as a method of small business development, enabling small firms to overcome the scarcity of resources so frequently associated with growth (Ayling [1]; Golisano and Worth [2]), and/or reducing

the agency/transaction costs associated with branch expansion (Carney and Gedajlovic [3]). It is argued that because franchisees provide at least part of the capital required, it should be a cheaper growth strategy than company owned expansion. In addition, franchising may reduce the agency costs of adverse selection and the moral hazard normally associated with company owned expansion: by making franchisees residual claimants through the payment of the franchise and royalty fees, it aligns more closely the incentives of the principal with those of the agent (Norton, [4]).

Given these benefits over organic expansion, franchising may appear a panacea for the problems of small business growth. It should be noted, though, that these benefits are contested. For example Rubin [5] contends that franchising is an inefficient method by which to raise capital to fund expansion, while Stanworth [6] suggests that despite the capital franchisees bring, the cost of establishing a franchised operation may be more expensive than company owned expansion, in fact. These contentions aside, one of the difficulties franchise businesses face when trying to grow is the recruitment of suitable franchisees. For example, McGuire [7] states that the "..number of franchisees with the requisite capital and managerial skills has not kept pace with the number of franchise offerings, and many franchisors report that this may act as an impediment to their future growth"(p. 33). Indeed, Knight [8] found 44% of franchisors in his survey of Canadian and American franchises were facing a shortage of suitable applicants, and Kirby and Watson [9] in a survey of franchises operating in the construction industry in the UK discovered that the recruitment of franchisees was becoming increasingly problematic. If franchisors are unable to recruit franchisees into their system, then any potential benefits from franchising become an irrelevance. It seems probable that the ability to recruit franchisees will be affected by the level of awareness and understanding by the general public. People will only apply to become franchisees if they are informed about franchising, and believe it offers a useful opportunity. It seems then, that the lack of suitable franchisees may stem from a lack of understanding, or a negative perception of franchising (or indeed both). Similarly, existing owner-managers are only likely to consider franchising as a potential growth strategy for their business if they understand the concept and are aware of the opportunities it affords.

Aims and methodology

Against this background, this paper examines the awareness of, and attitudes to, franchising by the general public in Britain. It is based on a survey of 1257 members of the public drawn from five city centres around Britain:

Cardiff (Wales), Birmingham, London and Newcastle (England) and Glasgow (Scotland). These centres were selected to ensure representation from across the country. Shoppers in the selected centres were interviewed using a short, structured questionnaire. A strict quota sample was not imposed but the interviewers were required to ensure that the majority of the respondents were employed and that there was a diverse sample in terms of age and occupation. The interviews were conducted at weekends in the period between January and April, 1999. Approximately 250 people were surveyed in each centre and the results indicate no significant bias in terms of gender, with 51.6 per cent of the sample being male and 48.4 per cent being female. The age profile of the sample showed some skewing towards the younger age groups with just over 50 per cent of the sample being under 35 years of age. However, all age groups are represented, with the smallest (5 per cent) being those respondents aged 65 years or over. All classes of employment were recorded, including the unemployed (7 per cent) and self-employed (8 per cent).

As franchising is a relatively recent phenomenon in the U.K, which is concentrated largely in the service sector where female employment is characteristic, it was expected that understanding of franchising might be greatest among those in the younger age cohorts and among females. Accordingly, two hypotheses were formulated and tested.

Hi – understanding of franchising is dependent on the age of the respondent.
Hii – understanding of franchising is dependent on the gender of the respondent.

Evidence suggests that those with some history of self employment are more likely to consider becoming a franchisee than those with no such history (Kaufmann and Stanworth [10] and Stanworth and Kaufmann [11]). In addition, it seems probable that franchisors will prefer to recruit those with at least some managerial experience. Indeed, Fenwick and Strombom [12] in a study of New Zealand franchise systems, found all of the franchisees questioned had some prior managerial experience. Further support for this notion comes from Stanworth's [13] 1991 study, which found that for a car tuning franchise, less than a fifth of franchisees had previously been employed in a manual occupation immediately prior to purchasing the franchise. It seems pertinent, therefore, to determine whether awareness of franchising varies by current occupation. Also, it was believed that those who

had been involved in franchising (some 9 per cent of the sample – 15 respondents) would have a better understanding of franchising than those who had not. Hence:

Hiii – understanding of franchising is dependent on the occupation of the respondent

Hiv – understanding of franchising is dependent on franchise experience.

Finally, it was felt that respondents' perceptions of, or attitudes towards, franchising would be dependent on their understanding of the concept. If they had a sound understanding they would be more likely to view the concept favourably. Thus

Hv – attitudes towards franchising are dependent on understanding.

Findings

Understanding of Franchising

The respondents were asked the open-ended question: "What do you understand by the term franchising?". A sample of responses was analysed to facilitate coding and 16 categories were identified (Watson and Kirby, [14]). The responses were then coded into one of these categories and subsequently re-coded into 3 broader categories reflecting the accuracy of the response, i.e. "Understand", "Part Understand" and "No Understanding". This revealed that the concept was fully understood by only 11 per cent of the respondents (126), while some 53 per cent (585) showed no understanding whatsoever and approximately 36 per cent (394) demonstrated part understanding. This would suggest the need for greater awareness raising if the franchise sector is to continue to grow.

When analysed by age, the results showed statistically significant variations, with those in the middle age ranges (25-64) most likely to have at least some understanding of the term and those in the upper and lower age cohorts showing least understanding (Table 1). This would lend support for hypothesis 1 and suggest that there is a need for awareness raising amongst, in particular, the younger age cohorts. Although understanding of the concept appears to develop with age, franchising may be a particularly beneficial mode of entry for those younger, less

experienced members of society who wish to enter self-employment, providing they appreciate, fully, what is involved and how to identify a quality, ethical franchise system.

Table 1: Understanding of Franchising by Age of Respondent.

Age	**Level of Understanding**			**Total**
	None	Some	Full	
	%	%	%	%
Under 25	59	29	12	27
25-44	50	39	11	46
45-64	46	40	14	22
65 and over	77	21	2	5
Total	53	36	11	100
Pearson Chi-square value p=0.000.				

Analysis by gender showed similar statistically significant variations. As table 2 reveals, however, the variations were in the opposite direction to that hypothesised (Hii). Males were more likely to understand the concept than females. Only 8 per cent of the women (47) in the sample understood what franchising is compared to 14 per cent of the men (79), suggesting that it might be appropriate to target awareness-raising at women, given the dominance of service businesses in the franchise industry.

Table2: Understanding of Franchising by Gender.

Gender	**Level of Understanding**			**Total**
	None	Some	Clear	
	%	%	%	%
Male	48	38	14	51
Female	58	34	8	49
Total	53	36	11	100
Pearson Chi-square value p=0.002				

Those respondents who were self-employed, managers and professionals were more likely to have an understanding of the term franchising. Even so, approximately 50% of those who were self employed had no

understanding, and approximately 40% of managers. This has serious implications if franchising is to continue to grow and fulfil its potential as a small firm growth strategy, especially if the self-employed are more likely to consider becoming franchisees than are those with no such history.

Table 3: Understanding of Franchising by Occupation

Occupation	**Level of Understanding**			**Total**
	None	Some	Clear	
	%	%	%	%
Professional	29	54	17	13
Managerial	42	42	16	10
Clerical/admin	52	40	8	15
Supervisory	53	37	10	8
Student	57	29	14	20
Manual	64	31	5	7
Self-emp'd	52	33	15	8
Unemployed	72	22	6	7
Other	67	27	6	12
Total	53	36	11	100
Pearson Chi-square value p = 0.000				

The data was further analysed to consider whether understanding varied by location, as this would have implications for awareness raising. Significant differences were found, with respondents from London more likely to understand the term. However, the sample for London respondents contained fewer unemployed and manual workers than for the other cities, and so the analysis was repeated, controlling for occupation. No significant differences were then found, suggesting awareness raising should be on a national basis.

Some 9 per cent of the respondents (99) had been or were involved in franchising in some capacity, usually as an employee and mainly in the fast food industry. These people appeared to have a better understanding of the franchise concept than those who had not. Thus the findings (Table 4) appear to support Hiv that understanding of franchising is dependent on franchise experience. Clearly this finding has considerable implications for the franchise sector and it would seem that franchisors could play a significant role in its growth. Apart from

providing possible recruits for their own system, franchise employees could provide the seedbed for both the development of new franchise businesses and the recruitment of franchisees for other systems, especially if generic franchise training were provided alongside system specific training.

Table 4: Understanding of Franchising and Prior Involvement

Prior Involvement	**Level of Understanding**			**Total**
	None	Some	Clear	
	%	%	%	%
Involved	39	41	20	9
Not involved	54	35	11	91
Total	53	36	11	100
Pearson Chi-square value p=0.002				

This finding has added significance as the results indicate that, though of only marginal significance statistically (p=0.075), those who have been involved in franchising are more likely to explore it as a means of starting a business than those who have not.

Attitudes towards franchising.

To gain further insight into the public awareness of franchising in the UK, respondents were asked to indicate on a five-point scale whether they agreed or disagreed with a series of positive (table 5) or negative (table 6) statements about franchising. A number of interesting findings were revealed. Over half of the sample "agreed" or "strongly agreed" with the statements that franchising "is a good way to own your own business", "is safer than starting out on your own", or "guarantees a similar standard of quality or service wherever you are". Only a small proportion of the sample (13 or 14 per cent) either "disagreed" or "strongly disagreed" with these statements. By comparison, fewer respondents believed "franchising helps businesses grow more quickly". Less than half of the sample held this view and some 26 per cent "disagreed" or "strongly disagreed" with the statement. Thus it would seem that while the general public do not necessarily have a clear understanding of the concept of franchising, the opportunities it offers for self-employment are appreciated by many, though its

potential as a strategy for the growth of existing small businesses appears to be appreciated somewhat less. Such findings have implications not just for franchising but for the development of small businesses. Indeed, it would seem to be this aspect of franchising, its contribution to business development, which needs to be better promulgated and appreciated.

Table 5: Responses to Positive Statements about Franchising

Statement	**Response**				
	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
	(%)	(%)	(%)	(%)	(%)
A good way to own your own business	25	31	31	9	4
Safer than starting out on your own	23	36	28	10	3
Helps businesses grow more quickly	12	31	31	19	7
Guarantees a similar standard of service & quality	28	33	25	10	4

For the negative statements, few respondents (16 per cent) believed franchising to be “unreliable”, and no more than a third (32 per cent) regarded it as harmful to existing competition. The main criticism, held by some 51 per cent of the sample, was that it was “ a way for big companies to get money out of people”. Even then, many respondents elaborated on their views with statements such as “why else would they do it?”, suggesting, perhaps, that this is not something entirely detrimental to franchising but rather a means of growing an existing business. Given that failures in franchising are believed to be as high, if not higher, than in the SME sector generally (Price [15]; Stanworth, et. al. [16]), it is somewhat surprising, perhaps, that public attitudes towards franchising on the whole did not appear to be negative.

Table 6: Responses to Negative Statements about Franchising.

Statement	**Response**				
	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
	(%)	(%)	(%)	(%)	(%)
A way for big companies to get money out of people	22	29	28	15	6
A threat to existing competition	11	21	32	24	12
Unreliable	4	12	38	32	14

Further analysis of the data revealed a statistically significant relationship between the level of understanding of the franchise concept and attitude towards franchising as expressed by the above statements. Those who have at least some understanding of the concept are more likely to agree with the positive statements and disagree with the negative than those with no understanding. Clearly this reaffirms the need for the franchise industry to ensure that, if it is to develop, the concept is properly understood and that understanding is disseminated as widely as possible.

Conclusions

Franchising has become one of the world's fastest growing methods of conducting business (Justis, Castrogiovanni and Chan [17]). In the UK the number of franchise systems has increased from 170 in 1984 to 596 in 1999, with turnover increasing from £0.9 billion ($1.44 billion) to £7.4 billion ($11.84 billion). Currently, it accounts for just under a third of all retail sales (NatWest/BFA Annual Survey [18]). If such growth is to continue long-term, there has to be sufficient numbers of potential franchisees. However, there is evidence to suggest (McGuire [7]; Knight [8]; Kirby and Watson [9]) that franchisors find it difficult, and seemingly increasingly so, to recruit suitable franchisees. Unless the general public is aware of, and understands franchising, it seems unlikely that this situation will improve, as the pool of franchisees will be restricted. Also, earlier research by the authors (Kirby, et. al. [19]) indicates that the concept is not fully understood by those responsible for supporting and advising small firms, suggesting that possibly the concept is not presented as frequently as it might be as a possible small firm growth strategy.

From the research presented here, it would seem that the vast majority (89 per cent) of the general public in Britain have no clear understanding of what franchising is and that "understanding" appears to be critical in determining whether attitudes towards franchising are positive or negative. This suggests, therefore, that those with an interest in promoting the development of franchising as a strategy for small business development need to ensure that there is greater awareness of it. As Dant, [20, p. 10] has recognised, and this study confirms, franchising *"…is still a poorly understood phenomenon"*.

Various strategies can be adopted to raise awareness and understanding, ranging from promotional and publicity campaigns on behalf of the sector to ensuring that teaching about franchising occurs on business studies curricular and small business courses in schools, colleges and universities. However, there is much that the industry can do for itself. As the research has demonstrated, those who have been involved in franchising have a better appreciation of it than those who have not. This would suggest that franchisors might consider ways, within their geographical territories, of involving the general public and promoting the franchise concept. As this survey has demonstrated (Watson and Kirby [14]), there is very considerable confusion amongst the general public over which firms are franchised and which are not. Only 17 per cent of the respondents recognised that the 10 successful franchise firms listed in the questionnaire were, in fact, franchise operations. Perhaps there is no reason why they should. If there is to be greater awareness, though, of the opportunities afforded by franchising and if a more positive image is to be projected, the public needs to be more aware of the role that franchising plays in the economy. However, raising awareness is not just about increasing the number of recruits to franchising, whether as franchisors or franchisees. Rather it is about increasing understanding. Not only do those with a better understanding of franchising perceive it more favourably, as this research has indicated, but by raising awareness of the problems as well as the opportunities which franchising affords, it seems probable that the risks associated with franchising will be reduced and the theoretical benefits will be experienced more widely.

Awareness and understanding also needs to be raised within the small firm support infrastructure and the private and public sector organisations responsible for advising those wishing to enter self-employment or to grow their business (Kirby et.al. [19]). These are the "gatekeepers" who can either encourage or discourage their clients. If they are either unaware of franchising as an option or view it negatively, the sector is not likely to develop and the potential that franchising affords for self-employment and small business development will not be realised.

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Dynamic Financial Management for the Entrepreneur:

a breakthrough in Financial Management techniques for Growing SMEs.

By

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And

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Abstract

This paper discusses some new, exciting and innovative financial management tools and techniques for entrepreneurs in growing businesses. Lack of Financial Management is often cited as the main reason for business failure. Formal accountancy techniques and reports fail the entrepreneur by being too rigid, too slow in response to events, and not reflecting the current activities of the business.

In a growing entrepreneurial business, the *shape of the business* changes too quickly to be captured by the visiting professional accountant. Furthermore, these professionally produced management reports represent the past - *'what has already happened'* - and not *'what we are doing now'* or indeed *'what we should be doing'*. Entrepreneurs need to have control of their own destiny and should therefore not have to delegate financial management of their business to outsiders. Nor should they need to *be* accountants. This paper addresses the need to bridge the gap between accountancy praxis and entrepreneurship.

At Durham University, we have developed a full Financial Management training programme to deliver a solution to SMEs and Business Support Agencies. Through this programme the authors have supported the successful implementation of improved financial management in over 40 businesses.

The programme concepts are built upon ***Dynamic Financial Management*** tools and techniques that are new and innovative and can rapidly and easily portray the moving shape of a growing business. The techniques allow the entrepreneur to keep their *finger on the pulse* of a fast moving business. By using simple and easily produced key indicators of the business, the entrepreneur has access to just the information necessary to manage growth, without needing professional reports or help. *Dynamic Financial Management* uses a combination of Key indicators. Visual representations, Targeting, and measurement and monitoring of *Gaps*, facilitating rapid investigation and so correction of business performance where necessary – *entrepreneurial action* not over-reaction.

The Financial Management Programme provides a *guidance system* for the entrepreneur to navigate through rapid growth. This paper will establish the need for this *entrepreneurial* approach to financial management, and provide case study examples on their successful application and benefits.

Introduction

There is no such thing as Finance! A bold statement perhaps, and certainly one that needs an explanation. It simply means that financial information is the output from business activities. The word *Finance* typically refers to the function that manipulates this information, and therefore is abstraction rather than actuality.

Context

'Progressive diversification' (Weber) within growing entrepreneurial firms brings about Differentiation, professional divisions of labour, utilising individual skills and knowledge to achieve specific targets within their own specialisms. It is, therefore, usually a specialist within the firm who manages the financial information, yet Finance is the output of **all** activities within a business. Financial Management becomes the realm of the accountant(s) whether inside or outside of the company, rather than becoming embraced within the management of the business.

As a specialism, *Financial Management* has come to represent collecting the required information, collating it in a structured manner, and then historically reporting on the 'results' of the business operations for that specific period – *the past*. This simply engenders a belief in the *'Magic of Finance'*, the mystique of the numbers, and generates a disbelief that they relate in any way to the real activities of the business. Yet, all of the financial figures used by the professionals are generated by the decisions of the managers in the company. It is their day-to-day actions that create the very results they no longer understand when presented to them by the professional accountant. The *'non-financial managers'* simply opt out and concentrate on *managing* their area of the company, making decisions without reference to their financial implications. It is no surprise therefore that a 'lack of Financial Management' is often cited as the main reason for business failure. (NatWest Bank, Coopers & Lybrand Mid-Market Barometer). And yet,

> "Financial Management enables the success of management by providing the funds that are necessary to plan, build, operate and maintain facilities, and the information and "handles" necessary to control the facilities and the management organization"

It seems therefore that a de-mystification of Financial Management is necessary and more importantly the creation of a direct relationship between the actions of managers and the financial information they receive. This is paramount to their understanding of business performance and their ability to act accordingly when results indicate opportunity or danger. If standard financial information is presented badly or at best inappropriately it may not be used. It builds up the barrier between the entrepreneur and the accountant perpetuating the myth of the irrelevance of finance to the entrepreneur. There must be a better way to present this vital information to portray the events of the past, the activities of the present and the possibilities of the future.

The Problems of Finance

For a growing entrepreneurial company, the entrepreneur is often the driving force, the strategist, the manager, and the sole person responsible for the finances of the business. If this is a sole trader, then the finances may be simple, but the addition of say one employee can suddenly multiply the difficulties many-fold. There is a strong need to gain an understanding of the drivers of the business and so of the financial information required to understand the business.

Yet the level of required understanding may be difficult to gauge. The entrepreneur does not want to be an accountant. They see no need to understand 'standard' accounting reports. They certainly do not need to be able to produce standard accounting reports. Indeed, there is little evidence that it is the format or content of these reports that enable the entrepreneur to successfully manage the business. But the question the authors would ask is, is there a methodology of Financial Management that will suit entrepreneurial behaviour and is it possible to educate/train the entrepreneur in that methodology?

Entrepreneurial behaviour provides the behaviours and practices needed to better manage risk and uncertainty, variety and uniqueness – so can we invent or improve Financial Management as a praxis to better enable entrepreneurial behaviour?

But why are entrepreneurs averse to standard financial information? Why can't accountants present information relating to the business from the entrepreneur's point of view? What information can we use that will communicate the performance of the business to not only the entrepreneur but also to all the stakeholders of the business? How can this information be presented in a way that will convince the key stakeholders of good business performance and sound financial management? What will enable the entrepreneur to be able to design the future – manage tomorrow - by responding to trends visible in the business today?

A *Weltanschauung* (Checkland, 1981) is a world view made up of values, beliefs and attitudes that influence language, thought and action. There are many differences between the typical *Weltanschauung* of the entrepreneur and that of the accountant. This is driven by their *Lebenswelt* – their world of experience. The authors have summarised these differences into two categories as follows:

The Entrepreneurial Landscape

- Entrepreneurial Characteristics versus accountancy practices
- The Personalities involved
- Decision making style of the entrepreneur
- Problem solving style of the entrepreneur
- Learning Styles of the entrepreneur

The Entrepreneurial Financial Management Requirements

- Timeliness of Information - Act in the present
- Format of Information - The Financial Triangle
- Variety and Uniqueness - Complexity of activities
- Risk management - Uncertainty of environment

Aims and Objectives

This paper will now describe the *Entrepreneurial Landscape* and the *Entrepreneurial Financial Management Requirement.* This paper will then introduce the ***Financial Management Programme*** (Annex One) as a solution that addresses the issues raised within these two categories.

The Entrepreneurial Landscape

Before moving on to examine aspect of the entrepreneurial landscape we need to summarise what we mean by entrepreneurship. Robert C. Ronstadt ("Entrepreneurship", p.9-12) after reviewing the evolution of entrepreneurship and examining its varying definitions put together a helpful summary definition (in D. F. Kuratko and R. M. Hodgetts, 1998, p.32);

> "entrepreneurship is the dynamic process of creating incremental wealth. This wealth is created by individuals who assume the major risks in terms of equity, time, and/or career commitment of providing value for some product or service. The product or service itself may or may not be new or unique but value must somehow be infused by the entrepreneur by securing and allocating the necessary skills and resources."

And, perhaps a more succinct summary for the purpose of this paper is provided by Kuratko and Hodgetts (1998, p.35) defining Entrepreneurship as *inter-disciplinary*;

> "In the study of contemporary entrepreneurship, one concept recurs:
> Entrepreneurship is interdisciplinary."

If entrepreneurship is inter-disciplinary, then finance, as a subject is simply part of entrepreneurship. Entrepreneurial action will de facto produce and incorporate financial information.

1. Entrepreneurial Characteristics, Accountancy practices and Personalities involved

Gibb (1987) in a section of his paper entitled 'sorting out definitions' provides a list of 12 entrepreneurial attributes (Gibb, 1987, p.7); These can be contrasted with accountancy practices to identify mismatches between the two *Lebenswelt* in the table below*:*

Entrepreneurial Attribute	Accountancy Practice
Initiative	Accountancy practice does not engender initiative. Finance is a by-product of other people actions or plans and is reactive rather than proactive.
Strong persuasive powers	Charismatic leadership is often the order of the day for the entrepreneur and this can contrast with the accountants need for objective rational

Entrepreneurial Attribute	Accountancy Practice
	data on which to be persuaded.
Moderate rather than high risk-taking ability	Accountants talk about risk analysis in relation to tools like ratio analysis and capital investment appraisal. These are used as a means of reducing risk, often to a lower threshold than the moderate risk taking of the entrepreneur.
Flexibility	The traditional training for accountants is driven by standards, especially for those who have come from an auditing background.
Creativity	Accountants are often analytical which may be seen as boring or lacking enthusiasm. There is a lack of understanding of the right personality for the right job.
Independence/autonomy	The external accountant who also performs *audit* duties is meant to be independent of the company with which the work. This can lead to two independent and autonomous individuals working with differing goals.
Problem-solving ability	Accountants are often seen to criticise – they focus on "negative variances" and are seen as pessimistic. Yet entrepreneurs problem solving abilities should be the ideal attribute to resolve under-performance. Maybe accountants also need to look for positive variances as a way to inspire the entrepreneur. Instead of steering them away from the bad they could be directing them towards the good.
Need for achievement	Finance may be more related to Herzberg's hygiene factors whereas the need for achievement of the entrepreneur is related to the motivators.
Imagination	In the preparation of accounts it is the process that is more important than the result. The beans have to be counted and have to be counted in a specific way. System predominates and the ability to analyse the route to the result – the audit trail - is important.
High belief in control of one's own destiny	Accountants for small businesses are often external to the business and therefore may not be felt to be within the internal locus of control of the entrepreneur. It is not within their control so they ignore it or deem it not necessary to their success.
Leadership	Accountants are held in a position of professional regard and often obtain leadership through the use of expert or legitimate power (French and Raven 1960). But whom are accountants committed to. Even internal accountants working for entrepreneurs may sometimes be more committed to their profession. External accountants are committed to their accountancy practice; they often do not have the time or the opportunity to develop a committed relationship with their entrepreneurial customer. Conflict arises between who is the leader and who is the follower in this relationship.
Hard work	Perhaps, at last, a common attribute.

Table 1

This table shows the contrast and indeed tension between the Lebenswelt of the entrepreneur and the praxis of the accountant. This has further identified the gap that needs to be bridged.

Having firstly looked at the attributes of the entrepreneur, it would now be useful to explore the personality of the accountant and contrast the two:

Aranya and Wheeler [1986] suggested that accountants tend to be

- precise in detail
- uncreative
- unwilling to encounter new ideas without being thoroughly prepared.

Segal and Szabo [1964] used psychoanalytic examinations to indicate that accountants were concerned with

- social norms
- were emotionally controlled
- had difficulty in handling emotional and ambiguous situations
- had rigid fearful identifications.

These findings contrast strongly with those mentioned previously for the entrepreneurial attributes.

2. Decision making style of the entrepreneur

There is often conflict over the method that should be used to aid decision making. Accountancy praxis often suggests that a strong structure underpinning the decision making process will give a project the best chance of success. Entrepreneurs are tempted to think that all they need is their intuition and they will be able to solve any problem and take the appropriate decisions – troubleshoot. It may be better to differentiate the process from the decision itself. Some decisions by their very nature have to be unstructured and these can be seen as a pendulum (Simon 1957, 1960):

Structured Decisions	**Semi-structured Decisions**	**Unstructured Decisions**
Established situation		Emergent situation
Ordinary		Novel, unique
Repetitive		One-shot
Issues Understood		Issues elusive
Knowledge already available		Knowledge difficult to get

Programmable Specialised manufacturing strategy		Creative General manufacturing strategies

Table 2

The *unstructured decisions* represent the situations facing the entrepreneur. Importantly, later in the paper we will show that traditional approaches to improving financial management in entrepreneurial enterprises is to move the entrepreneur into the world of *structured decisions* that are embedded in the Weltanschauung of the accountant. This is further evidenced by the adaption of Gibb's (1991) comparison of Entrepreneurial Management with "*Corporist*" management below :

Values Beliefs and Goals		
Entrepreneurial management		**Corporist Management**
Informal Strategic project planning (policy and practice interlinked and changing and emerging)	↔	Formal planning systems (policy laid before practice)
Failure means missed opportunity	↔	Failure means resource centred misdemeanour (variance from standard)
Seeks incremental development as a means to risk reduction	↔	Seeks large scale development with personal risk reduction by analysis information
Management evaluation on task completion	↔	Management evaluation as routine aspect of organisation
Avoids overheads and risk of obsolescence by extensive sub-contracting	↔	Seeks ownership of all resources with objective of power and control
Pursues effectiveness in the marketplace	↔	Pursues efficiency information to justify control

Table 3

Standard Accountancy methods of risk analysis, such as Ratio Analysis and Discounted Cash Flow techniques, are clearly more suited to the Corporist environment of 'formal planning' and of 'risk reduction by analysis information'. These are very *structured* decision making techniques that are foreign to the entrepreneur's *unstructured* world. This paper maintains the need to bring together these two actors into the arena of *semi-structured* decisions.

3. Problem solving and Learning Styles of the entrepreneur

Other areas of research adapting the Myers Briggs (adapted from Hellriegel, Slocum and Woodman) personality types have shown contrasting approaches to problem solving and differing learning styles. Information gathering and evaluation methods fall into four categories:

1. Sensation thinkers establish order, control and certainty, enjoy detail and are prone to over-simplifications. They are not risk takers.
2. Intuitive thinkers see across disciplines and focus on possibilities and respond to new ideas.
3. Sensation thinkers prefer interpersonal relationships and are the natural trouble-shooters who are able to get co-operation from the people around them.
4. Intuitive feelers use their charisma and commitment and examine abstract possibilities and enjoy creative problem solving.

The research goes on to show that 37% of US managers, including accountants, fall into this category of **Sensation Thinkers**. They enjoy dealing with people who can present data in an organised way. Indeed they may be frustrated if they are unable to get enough facts.

Compare this with the **Intuitive Thinkers** who make up 26% of US managers and include the entrepreneurs. Although they admire reason, logic and intelligence in others they tend to discount arguments based on data

Research has shown that preferred learning styles often reflect the styles found in the Myers Briggs results above (e.g. Harvey J. Brightman, Georgia State University).

Sensing types, like accountants, were found to prefer “organised, linear, and structured lectures”. And these should be application based. Sensing types often ask, "why am I learning this?" Sensing types also prefer familiar problems as they feel equipped to cope with these, the over vague leads to frustration.

Intuitive types, like entrepreneurs, prefer to see big picture, the inter-relatedness of the subject. They are able to develop and elaborate their own concepts and use their skills to compare situations.

And who generally teaches finance – people from the accountancy profession. In this context we could take "teaching" to mean formal training but, perhaps more significantly, the transfer of financial management know-how between the accountant and the entrepreneur. The "teacher" and the "student" are mismatched. The traditional approach has been twofold :

1. To develop the role of the business advisor
2. To introduce the entrepreneur to the financial world by training them in the traditional financial techniques.

This has helped in some way. The business advisors, often the accountants themselves have developed their awareness of the wide range of issues facing the entrepreneur. The financial training is often of a very high standard and helps the entrepreneur understand the jargon of finance and the world of the accountant. But they are both limited. They are all aimed at pulling the entrepreneur from their world of the *Intuitive Thinker* and *Unstructured Decisions* into the orderly world of the *Sensation Thinker* and *Structured Decisions*. To the entrepreneur with the *internal locus of control* (John Kao 1991) this is still externalising the problem.

Even lecturers in Accounting find it difficult to consider finance as inter-disciplinary, as an integrated whole:

> "Certainly, some lecturers referred to the difficulty they experienced in attempting to provide an integrated framework for what they felt were discrete and unconnected aspects of the syllabus. Indicative of this point were the concerns expressed about the difficulty of fitting in both management and financial accounting coherently into one introductory course." (Ursula Lucas)

For the entrepreneur there needs to be a new approach both to the subject of financial management and to financial training and these are the areas that provide the conceptual framework for the Financial Management Programme developed at the Foundation for SME Development at the University of Durham.

The Entrepreneurial Financial Management Requirements

After considering the tensions and contrasts between the Entrepreneurial Landscape and Accountancy Praxis this paper will now turn the attention to bringing the two together. The logical place to start is to look at what the entrepreneur requires in terms of financial information in order to manage the business.

1. Timeliness of Information - Act in the present

The usual reporting service from accountants is to produce periodical financial statements in a standard format. These reports are by nature historical and often delivered too late to make any difference to the decisions of the business. Entrepreneurial management means taking opportunities when they arise and minimising the risk, this requires meaningful and, as accurate as needed, information at the right time. These standard reports cannot be relied upon to achieve this immediacy. Accountancy practices are also bound by "financial periods" and "month end routines". Again entrepreneurial needs are for information produced at the time of the decision with information up to that point in time.

2. Format of Information - The Financial Triangle

Accountants place a great deal of emphasis on three separate pieces of the financial triangle – the Profit and Loss Account, the Balance Sheet and the Cash Flow Statement. Each has its own rules of preparation – matching, accruals and prudence principles for Profit and Loss, the rules of valuation on the "static" Balance Sheet and "reconciliation" between the two products of the book-keeping system – the Cash Flow Statement. The accountant's black art has not changed much since the days of Pacioli, still following the same key principles as described by Bryan Howieson:

1. The Monetary Principle - For accounting purposes, a record is made only of information that can be expressed in terms of units of currency.
2. The Cost Principle - All transactions and accounting elements are measured on the basis of acquisition prices.
3. The Period Convention -The life of an accounting entity is broken up into discreet reporting periods, usually one year.
4. The Matching Principle - All resources used up in the generation of revenue are recognised as expenses in the same period as that in which revenue is recognised.
5. Conservatism - A protective bias tending towards the understatement of assets and revenues and the early recognition of liabilities and expenses.
6. The Proprietorship or Entity Concept - The transactions and affairs of a business entity are accounted for separately from those of the owners of that entity.

But , although these have many valid uses, they may not fulfil all the needs of the entrepreneurial business.

The Profit and Loss Account provides useful information about where costs have been incurred but is badly structured for understanding the *nature* of costs and therefore understanding the impact of management decisions. The Balance Sheet is a snap shot of the *book worth* of the whole business, but there is also a lot of noise leaving the entrepreneur confused about what they should manage on a regular basis, and what the results of their management action will be. Entrepreneurs, being personally involved with the financial risk of their venture, recognise that Cash Flow is important. How cash rich, or not, have the operational decisions been? The traditional cash flow forecast, containing a mixture of long term and short term issues, serves a valuable purpose, but it does not directly answer this fundamental questions.

3. Variety and Uniqueness - Complexity of activities

Perhaps the most glaring issue in the financial triangle - the Profit and Loss account, Balance Sheet and Cash Flow statement - is the fact that the statements are separate. At the beginning of this paper we defined entrepreneurship as interdisciplinary. The entrepreneur sees the business as a whole. They have not yet split into functional specialisms. When accountants start to talk about these separate statements and how they represent separate aspects of the business they move away from the world of the entrepreneur.

Lecturers in Accounting have difficulty in focusing on all three statements in an holistic way:

> “"Views" of accounting also varied in emphasis. Within the interviews lecturers were asked mainly about the balance sheet, profit and loss account and the relationship between cash flow and profit. A key divergence in "view" arose according to whether the lecturer saw the balance sheet or the profit and loss account as the point of focus. Not only did the distinction arise, but also some lecturers were strongly attached to their particular point of focus. Some lecturers saw the balance sheet as essentially a secondary financial statement.” (Ursula Lucas)

Many entrepreneurial businesses have been forced to settle on one statement as the eye into the world of their business. When times are bad this is the Cash Flow. But under normal operations, entrepreneurs, like many of their counterparts in larger businesses, give undue emphasis to the Profit and Loss Account. After all this is the statement that at least reflects the level of *activity* over the accounting period.

But activity is more complex than that. Management decisions affect all aspects of the business – concentrating on the profit and loss account does not reveal that. A more holistic approach is needed by the entrepreneur to reflect their view of their business as a complex whole. Entrepreneurs can cope with complexity as suggested by Gibb (1987) in contrasting metaphors of the entrepreneurial culture. Comparing small enterprises to large businesses, Gibb lists untidiness against order; informality against formality and holistic against functional. Accountancy is reductionist in breaking the business down into discrete fragments - functions, more suited to the characteristics of the producer (the accountants) rather than the users (the entrepreneur).

4. Risk management - Uncertainty of environment

Accountancy practice is about managing risk and attempting to reduce uncertainty – a valuable process. Different views on a situation are always useful giving a richer picture for final decisions. Ironically, the I*nformation Uncertainty* in financial statements is well documented (Boritz 1990). No matter how much effort is put into finance it may never be 100% correct. Accountants may be on a quest for the Holy Grail whilst entrepreneurs are quite content to work with these uncertainties.

We maintain that finance is *the business* not a separate part of the decision making process, and business management *is* financial management. The entrepreneur may view the financial result in a different way and may have a different approach to risk. But, nevertheless, they are both interested in some sort of financial consequence. Although not the only measure of success, profitability, growth and survival are often measures used in the academic arena to identify the successful entrepreneur (e.g. Graham Hall 1999).

A Solution – A New Approach to Financial Management

Having identified the major issue as reconciling the Entrepreneurial Landscape, Entrepreneurial Financial Management Requirements, and traditional accounting practices, yet recognising that financial performance is a key requirement for entrepreneurial success, a more detailed explanation of how these are brought together by the Financial Management Programme.

Financial Management Programme

The Financial Management Programme (FMP) approaches the subject from two angles:

1. understanding business activity and how it relates to financial performance
2. developing the ability to make high quality management decisions the financial consequences of which are well understood.

These are not considered as independent bits of learning they are seen as interdependent. The understanding grows throughout the course. However the emphasis does change in favour of management choices and management decisions as the course progresses.

These are all looked at from the perspective of business rather than accountancy practices. At the core of the programme is a new approach to finance – *Dynamic Financial Management*.

Dynamic Financial Management provides key indicators relevant to any business and can easily be maintained using very little information from the business activities. If there is a simple accounting package used in the business then the required information will typically be available already. The simple manipulation of a few key indicators will portray the performance and the movement of the business – *what shape it is in*. The movement of the business may create opportunities for the future or warn of trends today that need addressing now.

The programme has a cumulative approach to learning and development. It uses a multitude of pedagogical techniques:

- Seminars
- Computer based training
- Work based projects
- Business simulations
- Counsellor support

Spread over a 12-month period it allows time to apply and assimilate the knowledge through the use of work based assignments. The length of the course allows a personal paradigm shift for the entrepreneur as they learn and adopt a new language and a new model of finance and, therefore, business. By the end of the programme the entrepreneur is using some sophisticated financial techniques usually done by accountants. This praxis may still be recognised as unstructured by the profession, but is *sufficient* to traverse the Entrepreneurial Landscape.

The programme focuses both on practical results and on new knowledge – Financial Management - but also allows participants to recognise when an expert is really needed. Furthermore the programme provides the entrepreneur with communicative competence, the ability to converse meaningfully with the profession. Work-based projects allow the application of new learning in the entrepreneurial enterprise – learning by doing.

The nine modules of the programme address the Entrepreneurial Landscape and the Entrepreneurial Financial Management Requirements in the following way:

Module	Entrepreneurial Landscape	Entrepreneurial Financial Management Requirements.
Foundation	Appreciation of learning styles and the pedagogical approach of the programme.	Introduction to dynamic financial management and how finance can be *quick and dirty* yet still add value. Breaking down preconceptions about finance.
Building Blocks	Internal locus of control increases Understanding the role and personality of the accountant and why conflicts may arise.	Communicative competence with external stakeholders. Separates statutory and management accountants.

Module	Entrepreneurial Landscape	Entrepreneurial Financial Management Requirements.
Information Multiplier	Importance of information – whether structured or unstructured. Recognising information gathering as distinct from information evaluation.	Importance of the systems in improving the *timeliness* of information.
Planning Projects	Recognising game playing here in the traditional approach to budgeting for external stakeholders.	Looking to the future – accepting uncertainty through scenario planning.
Planning Growth	Belief in the dynamic indicators and therefore the enthusiasm to record them in some way, shape or form, that is accurate enough to aid the decision making process. Concentrates on the *how to* – empathetic to the requirements of an entrepreneur who gathers information in an *intuitive* manner. Uses visual representations to help in a wider range of learning styles. Develops a language of its own.	Unique yet common dynamic indicators for the entrepreneur. Focus on the operational – the nature of costs (dynamic and static), the Dynamic Net Assets of the Business and Dynamic Cash Movements all obviously generated from the decisions made by the entrepreneur. An holistic view of the business as reflected in the dynamic indicators drawn from all three traditional financial statements – they can see the *shape of their business*. Sees sales as the *anchor* that may again have some affinity with the entrepreneur's attachment to the *activity* of the business.
Winning the Price War	Looks to areas for growth using a strategic framework but made to fit the entrepreneurial landscape Dynamic Financial Management techniques onto this framework. Gets the entrepreneur onto the next level in their business creating yet more independence and autonomy over the financial management of their business.	To have a different set of techniques to make the longer term decisions. Looks at very sophisticated finance in terms of Costing Methods and DCF techniques but in a way that reflects the activities of the entrepreneurial business. Focuses on live issues in the business such as the contribution of the product mix.
Managing External Factors	Recognising when it may be in the interest of the entrepreneur to produce more structured decisions– dealing with people for whom this is their lifeblood – tax, bankers, lawyers, and venture capitalists.	Communicative competence is now high and the entrepreneur is able ask for help from professionals without losing control. Being prepared to wait for these longer tem decision whilst still having the Dynamic Information to continue to meet their day to day management needs.
Troubleshooting	True problem solving – matching the intuitive knowledge of what makes their business tick with the changing shape of the Dynamic Indicators of their business.	
Financial Management Exercise	Businesses are complex and the financial techniques we use must stand the test of this complexity. A business simulation combines decision-making, team dynamics, and functional knowledge with Dynamic Financial Management. The visual representations of the financial results of the management decisions made during the course of this exercise prove the validity of the techniques. The communicative competencies are also challenged in dealing with "bankers", "suppliers" and "employee representatives" to create and share financial information and develop the business.	

Table 4

Entrepreneurs are more likely to take financial considerations into account if they can get the information quickly and visually. And that is where the programme delivers – answering some very fundamental questions concerning price, costs, volume, investment and cash flow as a consequence of every day management decisions. It is then up to the entrepreneur to assess and accept the consequences.

The entrepreneur new to the area of finance needs to understand both their Entrepreneurial Landscape and the *Weltanschauung* of the Accountant and other stakeholders in the business. The Financial Management Programme is the ideal vehicle for this as evidenced by the feedback from participants.

Sylvie Walker-Barras – Administration Manager at Automation Conveyors, Morpeth, Northumberland - De-mystification is a word Sylvie Walker-Barras uses often when describing the programme. She also values the work-based assignments, like the costing assignment she is currently working on. It helps her analyse & improve costing within her own company, which manufactures conveyors for industrial use. "The course is geared up for small companies like us which is great."
Henry Franklin, Business Link Oxford – Henry Franklin draws on his experiences in banking, the city and running his own business when he's working as a business advisor. But there's always more to learn. "The programme is helping us help others understand the problem areas more quickly. It's easy to get bogged down with figures and people talking. What the programme looks at is ways of getting key indicators and relevant figures quickly without having to wade through masses of figures."
John Boyd – principle consultant at John Boyd Associates, Teesside – As a busy staff recruitment consultant for petro-chemical companies, John Boyd finds that the programme gives him time to disconnect from day to day work and think strategically rather than one day at a time. "Since I've started the programme, we've started managing the orders better and improved our forward planning."
Graham Kidson, self-employed advisor (Devon) – Graham Kidson has worked in the City and run his own hotel, wanted to widen his skills portfolio by specialising in finance for business rather than finance for accountancy. "Finance is all important because making money is what companies are about. But a key weakness in many small businesses is financial management. Many businesses turn to accountants who take a prescriptive statutory approach. What they really need are better ways of identifying key financial indicators and dealing with problem areas – and this course equips you with additional tools and a deeper understanding of how to do that."

Table 5

But to truly appreciate the role of Dynamic Financial Management in their business they need to delve further. The programme was written in response to participants on other programmes and research carried out at the Foundation for SME Development into small and medium sized firms who requested another source of information to take their knowledge a stage further.

Conclusions

The Financial Management Programme seems to be closing the gap between the entrepreneur and the accountant. Communicative competence has allowed the entrepreneur to ask more of the profession and indeed understand more of the answers. Table 4 shows the mapping of the programme syllabus to the issues raised in the Entrepreneurial Landscape and the Entrepreneurial Financial Management Requirements, and how the issues of decision making, problem solving and learning styles are addressed. Furthermore, it defines the important parts of financial management that are critical to entrepreneurial behaviour. Finally, the programme provides an holistic and visual representation of the financial performance of the business and which responds in real-time to entrepreneurial action.

Participants have not however done away with the need for accountants. Indeed they now appreciate the *Weltanshauung* of the accountant more strongly. The accountant can take away the detail required for statutory and taxation purposes, help the entrepreneur ensure they have good systems to get the *bean counting* right in the first place. Working together, the entrepreneur and the accountant can produce the more complex financial analysis needed at strategic points in the growth of the business.

Many of the participants have *changed* their accountant. Participating entrepreneurs have made effort to understand the world of finance, if they find their accountant is not prepared to meet them half way then they now have the confidence to look for one who will. They now have *value added accountants*.

Policy, Process and Practice

The accountancy professions are aware of the need to move closer to the needs of the entrepreneur and have identified gaps in their own training and development programmes. To support this policy, the Financial Management Programme is also run for Business Advisors who may want to change their way of thinking about the structure and format of the help and advice they give to entrepreneurs. The UK government funded networks supporting small businesses may consider this type of programme as policy for development processes of business support staff.

Future Research

The encouragement gained from participating entrepreneurs in the northeast region of the UK, suggests the need for a longitudinal study to capture the changes in both understanding and praxis of the entrepreneurs and the accountants. This study would provide further evidence to increase the understanding of the Weltanshauung of the Entrepreneur.

Research into finance and entrepreneurship has until now focussed upon the financial consequences of entrepreneurial success or failure. However, Teleological (output based) studies are restricted in their appreciation of the processes involved in entrepreneurial action. Deterministic (input or process based) research would provide the insight into the needs of the entrepreneur as seen from their Weltanshauung. The problems and issues that inspired this paper came from the accepted belief that the Weltanshauung of the accounting profession was the correct interpretation. This is a classic example of professional paradigmatic closure. It is the belief of the authors that the voice of the entrepreneur should be listened to in order to understand the financial information needs of entrepreneurial action.

The conceptual framework of the Financial Management Programme addresses the core information and techniques required to manage a business entrepreneurially. It is therefore the belief of the authors that following national dissemination within the UK, it is entirely appropriate to extend the application of this programme internationally. The authors would welcome partners from interested nations wishing to improve business performance through entrepreneurial financial management.

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Annex One

An Outline of the Financial Management Programme

Reasons to Attend

Every manager needs to understand the financial aspects of the business to make better decisions. This programme develops financial understanding and introduces dynamic techniques to better manage the business. Participants can attain a Certificate/Diploma in Financial Management from Durham University.

Who Should Attend?

Owners, Directors and Key Managers of businesses who need a greater understanding of the financial aspects of business and how to monitor, manage and react to these.

What Are the Benefits of the programme?

For the Participant

- Greater strategic awareness of the future of your business, and how to contribute to and influence the development of the strategic plans
- Understanding of *dynamic* financial management
- The ability to monitor the business effectively through financial information
- The ability to make the best use of professional services when appropriate
- Support of a Mentor to help understand and implement changes to your business
- A Certificate/Diploma in Financial Management from Durham University

For The Company

- Improved Financial Management and Performance of the business
- Dynamic techniques to constantly monitor business performance
- Better strategic planning capabilities at senior management and director levels
- Direct application of course learning to company objectives
- Improved ability to manage daily operations through financial information
- Opportunities to benefit from other projects of the Business School

Programme Content

Foundations of Financial Management

- Introduction to the Programme
- Aspects of Dynamic Financial Management
- Understanding differing stakeholder needs
- Identifying Key Indicators for business performance
- Enhancement of analysis and study skills

The Building Blocks

- Introduction to the basics of Financial Management
- Standard practices of Recording, Reporting and Analysis of financial information
- Designing the right financial system to support the organisational structure and the appropriate use of account codes and responsibility centres
- Understanding the inter-relationship between the key financial statements
- Interpretation of key financial ratios

The Information Multiplier

- Managing and analysing business information
- Assessing the use of computer based financial tools within the business

Planning Projects

- Setting budgets and monitoring performance against them
- Looking at the components of a business plan and translating these into the key financial statements
- Looking at alternative scenarios and producing alternative plans

Planning for Growth

- Dynamic analysis of the business now and into the future
- Focusing on well managed growth
- Managing the financial requirements to meet growth targets
- Developing benchmarks for profitable growth
- Growing within cash restraints

Managing the External Factors

- Understanding the legal requirements of a business
- Appreciating the impact of various forms of taxation

Winning the Price War

- Appreciation of the impact of pricing strategy on financial performance
- Explanation of differing approaches to costing
- Analysing the business by product or service
- Assessing the viability of capital investment

Refinancing the Business

- Evaluating the alternative ways of financing a business
- Optimisation of internal funding
- Sources of External Finance and the ownership and control issues

Troubleshooting

- Identifying problems in business and choosing appropriate solutions
- Separation of cause and effect
- Managing the *whole* business

Financial Management Exercise

- Putting it all into practice using a competitive business stimulation
- Understanding different internal views of the business
- Managing within prescribed resource limitations

How Much Time Does it Take?

The programme consists of 16 days of workshops attended at Durham University Business School. These workshops are spread over a 12 month period, requiring attendance approximately every 4 weeks. Some workshops are 2 consecutive days and are therefore residential at the business school to maximise the time spent.

In between course attendance participants will be offered advice and support from a Mentor in applying the learning in the workplace and to support the submission of the work based projects.

Programme Style

The workshops are interactive and very practical, involving participants in business analysis, case studies, presentation, group activities and business simulations. The residential elements allow participants to work closely throughout the activities to maximise learning opportunities. There is always the opportunity to 'try out' the techniques using your own financial information during workshops if you wish.

There is a strong emphasis on the "can do" with a *dynamic* focus on the immediate business context. Some specialist guest speakers are used where appropriate.

DETERMINANTS OF HOME-BASED BUSINESS SALES PERFORMANCE

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This paper considers home-based business (HBB) sales performance and investigates factors influencing HBB sales. Both the HBB and small and medium enterprise literature were reviewed to identify 18 salient factors likely to influence HBB performance. Hypotheses were developed predicting the relationship between the factors identified and HBB performance. The hypotheses formulated were tested using the responses from a mail survey of 756 Victorian HBBs in 1997.

The bivariate and multivariate test results indicate a core group of explanatory variables that had the strongest statistically significant influence on HBB sales. HBB sales were mainly explained by a positive relation with *total business expenses*, the *number of hours worked by the owner-respondent* and the *use of information and communication technology*. *Age of the business* and *owner prior work experience* also had a statistically significant but weaker positive relation with sales. The *use of a business plan at startup and subsequently* had an unpredicted negative relation with sales.

Research in HBB has focused predominantly on descriptive statistics of demographic characteristics and levels sales. The results of this causative investigation provide a better understanding of the factors that influence HBB performance. Given the growth in the HBB sector and the economic and social contribution of HBB, the results of this study have implications for policy-makers in relation to the external financing, the impact of Local and State Government regulations and the role of information and communication technology in HBB. In addition, further research into these factors is recommended.

INTRODUCTION

Research on the economic marginality of HBB has included focus on the following issues: the contribution to the local economy in terms of sales and employment generation [49] and [55]; whether HBB owners choose to work at home or are forced to due to an inability to participate in mainstream corporate employment [45]; the type of work done in terms of value added [3]; and whether HBB generates income for the owner and wages for employees comparable to those working in larger organisations or commercially based small businesses [18] [26] and [38].

The issue of economic marginality is becoming increasingly important given the growth in numbers of HBB. For example, in a national random telephone and mail survey, [15] reports that approximately 12 % of households in Australia host a HBB. Additionally, growth in the number of persons employed at home between April 1989 and September 1995 is almost three and one half times greater than growth in the total number of person employed for the same period [7]. The experience is similar in the US [50] and Canada [45]. This study augments investigation of the marginality of HBB by reporting on the size of HBB in terms of annual sales; and addressing the research question "what factors influence the size of home-based business measured in terms of annual sales?"

The definition of HBB adopted is similar to that of the Australian Bureau of Statistics i.e. where the business is operated from the home of one of the owners even though very little work might be conducted at home e.g. trades people such as plumbers, carpenters, electricians etc, but with the exception that it is not limited to a maximum of 20 employees [8].

This paper next considers findings on the sales performance of HBB, reviews the SME and HBB literature in relation to the factors that are likely to influence the sales performance of HBB and formulates hypotheses for empirical testing. Then, the research design is outlined, followed by the findings of the study. Finally, the implications of the findings for policy-makers recommendations on further research are discussed.

HOME-BASED BUSINESS SALES PERFORMANCE AND INFLUENCING FACTORS

Sales Performance of Home-Based Business

In this study, the dependent variable HBB sales is defined as the annual level of sales over the 12 months preceding the time of survey. Sales level is the most commonly reported performance measure identified in the HBB literature. Part of its appeal is that it is well defined and understood by respondents. From Table 1 it is evident that most of the research on HBB sales has been conducted in the US and Canada. There is relatively little systematic research on these measures with descriptive statistics on sales reported either as part of a general description of the sector and/ or as part of an assessment of the economic importance of HBB to the local economy. The direct comparison of findings is difficult as studies variously report mean annual sales and ranges of sales. Comparison of the findings on sales is also constrained by other limitations as outlined in [58].

Notwithstanding this, Table 1 below provides findings on sales reported in the international and Australian literature reviewed. It can be seen that annual sales range considerably from nil to over $500,000 (disregarding differences in currency). In regard to international findings, with the exception of [29], approximately half or more of all respondents reported annual sales of below $US20,000 or $US30,000. The limited Australian data makes an overall finding difficult, however, the average annual sales figures in nominal terms may be higher than that for the US and Canadian studies. The findings on sales performance indicate that while some HBBs have very low sales, others generate a significant level of sales, suggesting considerable economic benefit may be generated by this segment of the small and medium enterprise (SME) sector.

Factors Hypothesised to Influence HBB Sales Performance

The sign of the hypothesised relationship between each of the explanatory variables and sales discussed below is consistent with the literature reviewed, or where ambiguous, is explicitly stated or indeterminate. Table 2 below summarises the alternative hypotheses developed from this discussion.

Gender

While most studies on small business performance are not gender-comparative [9], many studies indicate that businesses owned by women underperform those of men [56]. Underperformance has been found in relation to lower remuneration [2]; lower sales [31] and [32]; and lower profit [44]. A number of studies reporting gender-

comparative performance in the context of sales found that male HBB owners had greater sales than females [29], [45], [47] and [55].

Table 1: Findings on Sales Performance of Home-Based Business

Description of Study	Findings
International Studies	
Priesnitz (1988) Annual sales of 530 Canadian women home-based business owners	33% - sales $5,000 to $15,000 37% - $15,000 to $50,000 7% - $50,000 to $100,000 a small number above $100,000
Lozano (1989) In depth interviews with 35 home-based workers (some working for 'employers' on a contractual basis from home) in the San Francisco Bay Area	1982 sales ranged from $0 to $44,000 Mean $14,980
Carter, Van Auken and Harms (1992). Convenience sample, mail survey of rural HBB in Iowa, with 172 respondents. 1988 sales	41.8% - less than $5,000 13.45 - $5,000 to $10,000 15.1% - $10,001 to $20,000 15.7% - $20,001 to $50,000 14% - $750,000
Good and Levy (1992) Survey of HBB with 113 respondents in Manitoba, Canada. 1989 sales	67% - less than $25,000 16% - $25,000 to $50,000 7% - $50,000 to $100,000 7% - $100,000 to $500,000 3% - over $500,000
Orser and Foster (1992) Canadian survey of HBB owners with 404 respondents	Approximate mean sales of $20,450
Payne and Lebsack (1992) Survey with 253 respondents in Nebraska, US	Almost 25% with sales less than $1,000 68% with sales $20,000 or less 32% with sales over $20,000
Roberts (1994) Random telephone survey of HBB in Calgary Canada with 455 respondents	Mean 1993 sales $35,300 51% - sales of under $30,000
Owen, Heck and Rowe (1995) Nine state telephone survey with 899 on home-based work (employees working at home and HBB owners and operators) in 1989 & 1992 in the US	Mean 1988 sales $53,164
Alberta Economic Development and Tourism (1996) Alberta Business Start-up Study (sales for 1990 of HBBs started between 1987 and 1990)	34% - sales less than $25,000 18% - sales $25,000 to less than $50,000 18% - sales $50,000 to less than $100,000 14% - $100,000 to less than $200,000 15% - $200,00 to less than $1,000,000 1% - $1,000,000 to less than $5,000,000
Alberta Economic Development and Tourism (1996). Data provided by Small Business and Special Surveys Division, Statistics Canada 1991	Average sales of HBB with sales $25,000 to less than $36,622 - $30,300 Average sales of HBB with sales $36,622 and over $213,900

Family Responsibilities

SME research suggests one of the difficulties faced by women in operating their own small business is family responsibility [23] and [36]. Women have been found to spend more time caring for children and doing

Table 1 (continued): Findings on Sales Performance of Home-Based Business

Description of Study	Findings
Australian Studies	
Peacock (1992b) Convenience sample of 44 post-startup workshop attendees in Adelaide in 1991	Low financial returns reported for 36% of men and 60% of women
Peacock (1994) Convenience sample mail survey of 200 home-based business owners in Adelaide	Of the 47 responses to question on business size mean annual sales was $101,060 (excluding 7 atypical businesses with turnovers from 0.5 to 2.5 million dollars)
Business Owner Research (1994) Convenience sample of 50 interviews with HBB owner-operators in Sydney and Melbourne-1992-93 sales	16% - upto $20,000 16% - $21,000 to $40,000 6% - $41,000 to $60,000 24% - $61,000 to $100,000 18% - $101,000 to $150,000 10% - $151,000 to $300,000 2% - $301,000 to $500,000 6% - over $500,000 2% - no response Average approximately $120,000*
McInnes and Stanger (1996) Convenience sample, mail survey of targeted women owned small businesses in regional areas of South Australia with 163 respondents	Approximately one-third of businesses were home-based (including primary producers) and of these, 26.6% had business earnings before interest and tax in 1994-5 of over $50,000 (or 15.4% excluding primary producers)

* Mid - point of ranges used except for *over $500,000* range where $600,000 used.

housework than their husbands do [59]; spend fewer hours working in their small businesses than men [2]; and cannot expect support from their spouses in the daily running of the business [16].

International research is consistent with the view that family responsibility is a more important motivation for women starting a HBB [18], [29] and [38]. Australian research also supports the contention that the advantage of HBB in relation to family responsibilities is greatest for women [5], [6], [7], [33] and [49]. Despite the convenience of working at home and the proximity to the family, it is suggested the main disadvantage of operating a business from home is the difficulty in separating work and personal life [15], [24] and [51]. It is suggested that the flexibility offered to mothers by HBB may be gained at the expense of reduced sales [29] and [38].

Financing

It has been long recognised that a significant impediment to the fostering and development of small enterprise is the apparent limited access to debt and equity finance and the undercapitalisation that results [34], [35], [37] and [61]; and that access to external financing is associated with higher business performance [37].

International research indicates that the majority of respondents (between 50% and 82%) financed their HBB from personal savings and a minority (10% to 43%) indicated using bank financing in the form of a loan, overdraft or home mortgage [17], [24], [47] and [52]. Similar findings have been reported in Australia [8], [48] and [49]. The total amount of financing used at startup is relatively low compared to SMEs both internationally [17], [40], [47] and [52] and Australia [8], [48] and [49].

The only study identified that considers the association between financing and HBB performance is [17]. They found HBB relying primarily on outside financing at startup do not perform (in terms of profit) as well in the early years as firms where financing is primarily from the owner's personal savings. The literature does not suggest the amount of financing used at startup influences HBB performance, but rather the source of financing may influence sales. Low financing requirements is consistent with the low overhead, tax deductibility of living costs and the generally lower asset investment nature of HBB. Relevance of the source of financing is consistent with the pressure debt servicing will bring on the firms cash flow and growth.

Both the source and amount of financing used at startup were considered in this study. The three variables used were bank external financing (BANKFI) which included mortgage, loan, credit card and overdraft; other external sources of financing (OTHFIN) such as lease, supplier credit and government agency; and owner financing (OWNFIN) derived from personal savings, sales of assets and private loan.

Local and State Government Regulations

Given the recent growth in HBB, Local and State Government regulations are becoming increasingly important to HBB because the households from which they operate usually fall under residential zoning regulations or by-laws. These restrictions relate to maintaining the amenity of a residential area and are concerned with the impact on immediate neighbours, other residents, and the municipality. There is considerable concern in the literature that Local and State Government regulations are outdated and may restrict HBB operations, growth and performance [24], [25], [46] and [53]. Research on the impact of government regulations on HBB operations suggests it is not considerable [29] and [49]. However, this may be moderated by the apparent lack of owner awareness of Government regulation [45]. It is hypothesised that HBB sales are negatively related to the degree to which owners perceive regulations restrict their HBB operations.

Technology

With the increasing availability and affordability of information and communication technology, more small businesses are able to utilise this technology [63]. SME studies suggest the use of information and communication technology has a beneficial affect on performance in terms of cash flow management [12], strategic management [22] and access to world markets [11]. No empirical research on the effect of the uptake of information and communication technology on HBB performance was found in the literature reviewed. However, anecdotally, [45, p. 101] suggest the use of information technology may enable HBB to operate without hiring outside help and thus may increase output and sales.

Business Expenses

Although a small number of studies reviewed report the expenses incurred in operating HBB, none have related this variable to business performance. However, [1] describe data provided by Small Business and Special Surveys Division, Statistics Canada 1991, which facilitates this analysis. It indicates that higher expenses are associated with higher sales. Additionally, expenses as a proportion of sales increased as sales increased, resulting in a declining profit to sales ratio.

Proportion of Business Expenses Spent on Labour

No data on the proportion of business expenses spent on labour costs were identified in the literature reviewed. However, based on *a priori* reasoning, HBB that spend a greater proportion of their total business expenses on labour costs may employ more persons, all things equal. This employment is likely to result in greater sales as the operating capacity of the business is increased.

Hours Worked

The literature commonly differentiates between full-time and part-time work in the HBB [5], [6], [7], [8] and [45]. It is likely that the more time worked by the owner in the HBB, the less time available for working in another job, and therefore the greater the reliance on the income produced from the HBB. A positive relation between sales performance and the hours worked in the HBB is evident in the literature [29], [45] and [52].

Degree of Formal Planning

The business plan is one of the most important steps in establishing a small enterprise and growing it [13] and [43]. In the US, [24] compared HBB and SME and were surprised to find that the former had the higher failure rate. They suggest the reason for this is the statistically significant finding that HBB undertake a lower degree of formal business planning than SME, both at startup and on an ongoing basis. The use of a business plan for startup and ongoing operations may help reduce the likelihood of failure and the poor performance that precedes it, and thus may be positively associated with sales.

Outsourcing or Sub-Contracting

Outsourcing may be used where the legal maximum number of persons are employed in a HBB [30] or where it is more profitable to outsource than to employ [62]. Sub-contractors as a form of casual labour provide greater benefits to HBB than a full-time salaried employee. The labour cost is only paid when services are rendered and the payment of non-salaried on-costs are often avoided as sub-contractors often have their own personal and liability insurance. This results in HBB incurring less cash expenditure, all other things equal. [55] found that 15% of respondents contracted out part time and full time work as needed. [40] found HBB owners did not employ anyone, but received assistance from either co-owners or paid independent contractors. The use of outsourcing or sub-contracting is expected to have a positive impact on sales performance.

Age of Business

[20] found a positive correlation between the number of years a SME has been in business and annual sales and other performance measures (business income, income per employee, income per owner and sales per employee). The HBB literature also indicates that business age is positively related to sales [29], [45] and [52].

Industry Sector

Few studies have considered the effect of the industry sector of HBB and sales performance. The limited findings indicate an ambiguous effect. [52] found that HBB offering professional and business services (tertiary industry) generally reported significantly higher sales. Conversely, [45] found on average that HBB in primary industry generated marginally more sales than those in tertiary industry, with HBB in secondary industry generating significantly lower sales than both.

Location of Household

[45] found a positive relationship between sales and being located in an urban area, as compared to a farm or non-farm rural location. A positive association between degree of urbanisation and sales is predicted because higher population densities are likely to provide more prospects to increase sales, and also, since markets tend to be concentrated, distribution costs of selling and/ or providing services to the market would be relatively lower.

Usefulness of Networking Organisations

Participation in business networks has been found to be positively associated with business profitability and is one of the main practices contributing to performance in small business generally [56]. [17] found that HBB owners with an interest in networking became profitable sooner after startup, than those with little interest in networking. Anecdotal evidence suggests that networking can help to reduce the isolation of owners and assist with marketing the business and making business contacts [51] and [57]. Despite the potential benefits of networking, [41] suggests that HBB do not tend to belong to business organisations because of their low profile. A positive association between the usefulness of networking organisations and sales is hypothesised.

Owner Self-Funded Superannuation Coverage

A small number of studies provide findings on the extent of HBB-related owner superannuation, however the relationship with sales performance is not addressed. The [5] found that approximately 31% of the self-employed and employers in HBB had superannuation. The [54] suggests this relatively low rate of self-funded superannuation amongst owners could be expected due to the part-time and possibly temporary nature of employment at home. However, somewhat incongruent to this view, is the assessment by Australian studies that the commercial potential of HBB to insurance and superannuation providers is considerable [10] and [14]. Owners that work predominantly or solely in their HBB are likely to be more dependent on the income it generates, both presently and in the future. Thus it would seem likely that sales performance is higher for these HBBs and the owners would be more likely to have self-funded superannuation.

Bartering

A small number of studies have suggested that HBB may barter some of the goods or services produced [39], [45] and [55]. [45] suggest that underreporting of the extent of HBB activity is likely to occur where a business operates, at least partially, on a barter system. It is likely that such transactions, for example where an owner

helps out a neighbour, are not recorded. Additionally, a bartering system (along with cash transactions) may consciously be used as a way of circumventing taxation. Therefore, it is hypothesised that bartering and reported sales are negatively related.

Similarity of Previous Work Experience

The SME literature suggests that business performance and expansion are positively related to the owner having prior experience in the industry [56]. While no empirical evidence has been identified that links prior work experience with HBB performance, it is likely to also be the case for HBB.

Employment

No empirical evidence of the influence of employment level on HBB sales has been identified in the literature. However, assuming the goal of profit maximisation, HBB owners are likely to employ labour when it increases the profit (and therefore sales) generated by the firm.

Explanatory Variables Excluded From the Analysis

Preliminary regression analysis indicated that a number of variables found in the literature to have a possible association with SME and HBB sales performance should not be included in the regression modeling process. These include the education of the owner-respondent [38] and [56]; age of the respondent-owner [38] and [45]; the number of other co-owners (if any) assisting with the business [45]; the legal structure of the business [45]; business income as a proportion of household income [10], [15] and [29]; whether the respondent-owner had a marital or *de facto* partner [49]; and the proportion of expenses spent on professional services (e.g. accountant and lawyer) and advertising [45].

RESEARCH DESIGN

A mail survey of 4,133 Victorian HBB, commissioned by Small Business Victoria (Department of State Development), was conducted based on a convenience sample of all Victorian HBBs listed in the national *Home-Based Business Australia* and the Manningham City Council (Melbourne) HBB databases. The 14 page structured questionnaire contained 48 questions, of which most were close-ended. The questionnaire was pilot tested with peers of the researcher as well as in the field. Feedback and comment was then sought from policy-

makers. Based on the return of 758 valid questionnaires, the response rate as a percentage contact with eligible respondents was 20.1%. A stepwise multiple regression analysis was used because of its model building, as opposed to model testing, nature [60]. Explanatory variables with ordinal scales were used in the multiple regression as the scale points have more or less equal intervals [19, p. 10]. Table 3 below provides a summary of the dependent and explanatory variables.

Table 2: Home-Based Business Sales Performance Hypotheses Tested

Explanatory Variable	Alternative Hypothesis
1. Gender of respondent-owner	**H_A1:** The gender of the HBB owner will influence HBB sales.
2. Existence of a resident child(ren) in household	**H_A2:** Having a resident child(ren) will be negatively correlated with HBB sales.
3a. Total bank external financing used at startup[1]	**H_A3a:** The use of external bank sources of financing will be negatively correlated with HBB sales.
3b. Total other external financing used at startup[1]	**H_A3b:** The use of external other sources of financing will be negatively correlated with HBB sales.
3c. Total private financing used at startup[1]	**H_A3c:** The use of internal owner sources of financing will be positively correlated with HBB sales.
4. Restrictiveness of Local and State Govt. regulations	**H_A4:** The HBB owner's perception of the restrictiveness of Local and State Government regulations will be negatively correlated with HBB sales.
5. Use of information and communication technology	**H_A5:** The use of information and communication technology will be positively correlated with HBB sales.
6. Total business expenses for the last 12 months	**H_A6:** The level of business expenses incurred will be positively correlated with HBB sales.
7. Percent of total expenses spent on non-owner labour	**H_A7:** The proportion of business expenses spent on labour will be positively correlated with HBB sales.
8. Average total hours worked per week in business	**H_A8:** The number of hours worked by the owner-respondent will be positively correlated with HBB sales.
9. Use of a written business plan at startup and currently	**H_A9:** The use of a written business plan will be positively correlated with HBB sales.
10. Percent of sales outsourced or sub-contracted	**H_A10:** Outsourcing or sub-contracting will be positively correlated with HBB sales.
11. Age of business	**H_A11:** Business age will be positively correlated with HBB sales.
12. Industry sector of business	**H_A12:** The industry sector in which a HBB operates will influence HBB sales.
13. Location of home from which business operated	**H_A13:** The degree of urbanisation of a HBB will be positively correlated with HBB sales.
14. Usefulness of networking organisations	**H_A14:** The usefulness networking organisations will be positively correlated with HBB sales.
15. Owner self-funded superannuation coverage.	**H_A15:** Owner self-funded superannuation coverage will be positively correlated with HBB sales.
16. Frequency of bartering in the last 12 months	**H_A16:** The frequency of bartering of goods or services will be negatively correlated with HBB sales.
17. Similarity of prior work experience	**H_A17:** Similarity of the respondent-owner's previous work experience will be positively correlated with HBB sales.
18. Number of equivalent full time employees	**H_A18:** The level of employment will be positively correlated with HBB sales.

Table 3: Description of Variables

Description of Variable	Variable Label	Variable Measurement Scale
Dependent Variables		
1. Gross sales for the last 12 months	SALES (T)	Interval*
Explanatory Variables		
1. Gender of respondent-owner	GENDER	Dummy
2. Existence of resident child(ren) in household	CHILDRES	Dummy
3. Respondent-owner superannuation policy	SUPERANN	Dummy
4. Similarity of prior work experience	WORKEXP	Dummy
5. Frequency of bartering in the last 12 months	BARTER	Ordinal (0 never, 1 rarely, 2 sometimes, 3 frequently)
6. Written business plan at startup and currently	BUSPLAN	Ordinal (0 never, 1 startup/currently, 2 startup and currently
7. Industry-type of business	INDUSTRY	Ordinal (1 primary, 2 secondary, 3 tertiary)
8. Location of home from which business operated	LOCATION	Ordinal (1 farm, 2 rural non farm, 3 metropolitan)
9. Age of business	BUSAGE	Interval*
10. Restrictiveness of local/ state govt. regulations	GOVRSTN	Interval (composite variable with value o to 55 from 11 issues with responses 1 very helpful, 2, 3, 4, 5 very restrictive 1)
11. Average hours worked per week business	HOURSWRK	Interval*
12. % of total expenses spent on non-owner labour	LABEXPC	Ratio
13. Total bank financing used at startup	BANKFIN (T)	Interval*
14. Total other financing used at startup	OTHFIN (T)	Interval*
15. Total private (own) financing used at startup	OWNFIN (T)	Interval*
16. Total business expenses for the last 12 months	EXPENSES (T)	Interval*
17. Usefulness of networking organisations	NETWORK	Interval (composite variable with value 0 to 48 from 16 organisations with responses 0 not at all useful, 1, 2, 3, 4 very useful)
18. % of sales outsourced or sub-contracted	OUTSRCPC	Ratio
19. Use of informtn. and communctn. technology	TECHNLGY	Interval (composite variable with value 0 to 11 for use of 11 appliances)
20. Number of equivalent full time employees	EMPLOY (T)	Interval

(T) Indicates variable underwent natural logarithm transformation subsequent to assessment of non normality through descriptive and univariate statistics.

* Imputed value from midpoint of response ranges/ categories

RESULTS

Two cases with extreme values (outliers) were identified and subsequently deleted. Non-response bias analysis assumed respondents who respond less readily (i.e. later) are more like non-respondents [4]. With the exception of BUSPLAN (p = 0.006), where it was found that early respondents were significantly more likely to have a written business plan at startup and/ or currently than late respondents, no significant difference between early and late responses was evident [58].

Descriptive and Univariate Statistics

Table 4 below provides the descriptive and univariate statistics of the non-dichotomous raw and transformed (indicated by label prefix LN) data. The range of annual sales was from $2,500 to $200,000, with a mean of $87,199. This supports the contention that HBB are not economically marginal forms of small business.

Table 4: Descriptive and Univariate Statistics – Raw and Transformed Data[1]

	SALES	NETWORK	OUTSRCPC (%)	TECHNLGY	EMPLOY	EXPENS
N	615	756	723	648	716	570
Minimum	2500	0	0	0	0	2500
Maximum	200000	48	100	11	32.5	200000
Mean	87199.187	4.148	9.350	6.830	0.633	53394.740
Std Dev'n.	78170.962	5.444	20.640	2.410	2.362	63777.450
Skewness	0.571	2.631	2.979	-0.548	9.468	1.496
Kurtosis	-1.375	10.967	8.583	-0.196	107.231	0.941
K-S Stat	0.226	0.223	0.325	0.132	0.394	0.212
	BARTER	BUSPLAN	INDUSTRY	LOCATION	BANKFI	OTHFIN
N	740	692	742	755	730	730
Minimum	0	0	1	1	0	0
Maximum	3	2	3	3	78750	51250
Mean	0.560	0.550	2.740	2.850	7857.877	2738.014
Std Dev'n.	0.850	0.760	0.460	0.410	14416.459	7490.067
Skewness	1.334	0.974	-1.375	-2.902	2.384	3.664
Kurtosis	0.673	-0.600	0.615	8.072	5.767	15.088
K-S Stat	0.388	0.383	0.463	0.515	0.293	0.404
	BUSAGE	GOVRSTN	HOURSWRK	LABEXPC (%)	OWNFIN	
N	738	756	752	550	731	
Minimum	0.500	0	1	0	0	
Maximum	20	46	7	90	75000	
Mean	7.991	5.257	4.410	10.950	8218.194	
Std Dev'n.	5.997	9.001	1.780	18.490	10525.439	
Skewness	0.673	2.172	-0.332	1.921	2.312	
Kurtosis	-0.844	4.408	-0.900	3.178	6.766	
K-S Stat	0.239	0.280	0.168	0.298	0.259	
	LNSALES	LNEMPLOY	LNEXPENS	LNBANKFI	LNOTHFIN	LNOWNFIP
N	615	716	570	730	730	731
Minimum	7.824	0	7.820	0	0	0
Maximum	12.206	3.510	12.210	11.270	10.840	11.230
Mean	10.737	0.276	10.082	4.366	2.094	7.452
Std Dev'n.	1.347	0.492	1.397	4.609	3.787	3.088
Skewness	-0.687	2.822	-0.176	0.173	1.305	-1.705
Kurtosis	-0.401	10.695	-0.959	-1.853	-0.187	1.671
K-S Stat	0.163	0.317	0.119	0.346	0.471	0.326

1 Variable label prefix LN denotes natural logarithm transformation

From Table 4 above, it can be seen that the variables display varying degrees of skewness and kurtosis and thus are non-normal. Natural logarithmic transformations were applied to the variables with values of relatively large or extreme magnitude and/ or that had a substantially non-normal distribution (LNSALES, LNBANKFI, LNOWNFIN, LNOTHFIN and LNEXPENS). A shift factor of 1.0 was added to cases with zero values [21, p. 111] and [27, p. 341, n. 23]. Variables with relatively large or extreme values were transformed (or 'winsorised') as a precaution against the possible adverse effects of extreme observations on the analysis [21, p. 101]. The departure from normality of the transformed variables, as indicated by the skewness and kurtosis coefficients, is reduced for all variables, except for LNPROFIT and LNEXPENS. The One-Sample Kolmogorov-Smirnov Test (K-S) statistics remained significant ($p < 0.0005$), indicating the hypothesis of normality is rejected. Other variables were not transformed, despite the possibility of substantial departure from normality, as 'there are no distributional assumptions about IVs [explanatory variables], other than their relationship [linearity] with the DV [dependent variable]' [60, p. 136, n. 2].

Bivariate Statistics

The results of the Mann-Whitney U test in Table 5 below indicate that for the dependent variable LNSALES the null hypothesis of equality of the means (i.e. no difference in the distribution) can be rejected for all four dichotomous explanatory variables GENDER, CHILDRES and SUPERANN and WORKEXP ($p <= 0.10$). The mean ranks indicate that being male, having a resident child(ren), having superannuation and having done the same or similar prior work are associated with higher sales.

Table 5: Mann-Whitney U Test Results

Explanatory Variables	Groups	N#	Mean Rank	U-statistic	Z-statistic	Two-tailed Probability
Dependent Variable: LNSALES (N = 615)						
GENDER	Male	409	344.15	27342.5	-7.224***	0.000
	Female	206	236.23			
CHILDRES	No	317	294.96	43098.0	-1.840*	0.066
	Yes	297	320.89			
SUPERANN	No	174	207.29	20843.0	-8.112***	0.000
	Yes	411	329.29			
WORKEXP	No	226	284.12	38559.5	-2.386**	0.017
	Yes	385	318.85			

*, **, *** Denote significance at 0.10, 0.05, 0.01 level respectively.
Sum of N for categories of each explanatory variables may not equal N for LNSALES due to missing data.

The results of the parametric Two-sample t-tests for the dependent variable LNSALES, presented in Table 6 below, are consistent with those of the Mann-Whitney tests, with one exception. The exception being the null hypothesis of no difference between the means can not be rejected for the dichotomous explanatory variable CHILDRES. This suggests that HBB sales are not influenced by a resident child(ren).

Table 6: **Two-Sample T-Test Results**

Explanatory Variables	**Groups**	**N#**	Mean	t-statistic	**Two-tailed Probability**
Dependent Variable: LNSALES (N = 615)					
GENDER	male	409	11.003333	7.200***	0.000 [a]
	female	206	10.206851		
CHILDRES	no	317	10.674681	-1.188	0.235 [a]
	yes	297	10.804012		
SUPERANN	no	174	10.105438	-8.141***	0.000 [b]
	yes	411	11.068937		
WORKEXP	no	226	10.529084	-2.788***	0.006 [b]
	yes	385	10.855187		

*, **, *** Denote significance at 0.10, 0.05, 0.01 level respectively.
Sum of N for categories of each explanatory variable may not equal N for LNSALES due to missing data.
a Levene's Test indicates use of pooled-variance *t* test (p = 0.05).
b Levene's Test indicates use of separate-variance *t* test (p = 0.05).

Table 7 below provides the Spearman rank correlation coefficients for the dependent variable LNSALES and the ordinal scale explanatory variables. It can be seen that LNSALES has a significant negative correlation with INDUSTRY (-0.166, p = 0.01) and positive correlation with LOCATION 90.106, p = 0.01). This supports hypothesis H_A13, that the degree of urbanisation of the HBB is positively correlated with LNSALES.

Table 7: **Spearman Rank Correlation Matrix**

	LNSALES	BARTER	BUSPLAN	INDUSTRY	LOCATION
LNSALES	1.000				
BARTER	-0.009	1.000			
BUSPLAN	-0.060	0.043	1.000		
INDUSTRY	-0.166***	-0.134***	0.133***	1.000	
LOCATION	0.106***	-0.022	-0.028	0.011	1.000
	LNSALES	BARTER	BUSPLAN	INDUSTRY	LOCATION

*, **, *** Indicate correlation is significant at 0.10, 0.05 level, 0.01 level (Two-tailed) respectively.

A number of correlations between the explanatory variables are significant at the 0.01 level. The negative correlation between INDUSTRY and BARTER (-0.134, $p = 0.01$) indicates that HBBs operating in tertiary industry conduct less bartering than HBB in the primary and secondary industry. This is not surprising as HBBs operating in primary and secondary industries are more likely to have a tangible product that is more easily valued and traded. The significant positive correlation between INDUSTRY and BUSPLAN (+0.133, $p = 0.01$) indicates that HBBs in tertiary industry tend to prepare and use a written business plan more, at either startup, presently or both, than HBB in primary and secondary industries.

Table 8 below provides the parametric Pearson product-moment correlation coefficients for the dependent variable LNSALES and the interval and ratio scale explanatory variables. As hypothesised, the dependent variable LNSALES have significant ($p = 0.01$) positive correlations with the explanatory variables BUSAGE (0.405), HOURSWRK (0.617), LABEXPC (0.315), LNBANKFI (0.140), LNOTHFIN (0.298), LNEXPENS (0.864), OUTSRCPC (0.252) and TECHNLGY (0.411). This suggests sales is positively associated with the age of the business, number of hours worked by the respondent-owner in the business per week, the proportion of total business expenses attributable to the cost of labour, the amount of bank external financing, the amount of other external financing, the total business expenses, the percentage of sales out-sourced or subcontracted and the use of information and communication technology. The correlation with LNBANKFI and LNOTHFIN is in the opposite direction hypothesised.

With regard to correlations between explanatory variables, the highest correlation was found between LNEXPENS and HOURSWRK (0.597, $p = 0.01$), which lies within the limits suggested by [27, p. 299] who states correlations of 0.5 are relatively low and correlations above 0.8 are high and present a serious problem for collinearity. The remaining correlations are below 0.4, suggesting that collinearity is not a serious concern.

Multivariate Statistics

It can be seen from Table 9 below, the stepwise variable selection OLS multiple regression produced the following model (unstandardised coefficients):

$$\text{LNSALES} = 2.673 + 0.689\ \text{LNEXPENS} + 0.123\ \text{HOURSWRK} - 0.190\ \text{BUSPLAN} + 0.074\ \text{TECHNLGY} + 0.016\ \text{BUSAGE} - 0.020\ \text{LNBANKFI} + 0.165\ \text{WORKEXP}$$

Table 8: Pearson Correlation Matrix

	LNSALES	BUSAGE	GOVRSTN	HOURSWRK	LABEXPC	LNBANKFI
LNSALES	1.000					
BUSAGE	0.405***	1.000				
GOVRSTN	0.057	-0.001	1.000			
HOURSWRK	0.617***	0.185***	0.071*	1.000		
LABEXPC	0.315***	0.186***	-0.003	0.116***	1.000	
LNBANKFI	0.140***	0.090**	0.151***	0.170***	0.024	1.000
LNOTHFIN	0.298***	0.174***	0.113***	0.225***	0.025	0.317***
LNOWNFIN	0.047	-0.118***	0.095***	0.088**	-0.073*	-0.070*
LNEXPENS	0.864***	0.367***	0.089**	0.597***	0.333***	0.193***
NETWORK	-0.059	-0.115***	0.147***	0.024	-0.022	0.068*
OUTSRCPC	0.252***	0.101***	0.055	0.124***	0.168***	0.086**
TECHNLGY	0.411***	0.041	0.084**	0.267***	0.163***	0.023
	LNSALES	BUSAGE	GOVRSTN	HOURSWRK	LABEXPC	LNBANKFI

	LNOTHFIN	LNOWNFIN	LNEXPENS	NETWORK	OUTSRCPC	TECHNLGY
LNOTHFIN	1.000					
LNOWNFIN	0.008	1.000				
LNEXPENS	0.340***	0.060	1.000			
NETWORK	0.019	0.094**	-0.018	1.000		
OUTSRCPC	0.175***	0.011	0.299***	-0.003	1.000	
TECHNLGY	0.122***	0.135***	0.384***	0.023	0.153***	1.000
	LNOTHFIN	LNOWNFIN	LNEXPENS	NETWORK	OUTSRCPC	TECHNLGY

*, **, *** Indicate correlation is significant at 0.10, 0.05 level, 0.01 level (Two-tailed) respectively

The adjusted R^2 of 0.781 indicates the regression model has very good explanatory power. With the exception of BUSPLAN, which has a negative sign, all explanatory variables have the hypothesised sign, where specified. The standardised coefficients indicate that the explanatory variable with the greatest explanatory power in predicting HBB sales (LNSALES) is LNEXPENS (0.693), followed more distantly by HOURSWRK (0.157), TECHNLGY (0.126) and BUSPLAN (-0.104). The explanatory variables with the least explanatory power are BUSAGE (0.067), LNBANKFI (-0.064) and WORKEXP (0.057).

A scatterplot of the residuals for the regression model of the untransformed and transformed explanatory variables against the transformed dependent variable LNSALES is provided in Figure 1 below. The rectangular random pattern of the residuals evident is due to the discrete nature of the data collected on the dependent variable and a number of explanatory variables. The shape and concentration of residuals in the scatterplot does not indicate a serious departure from assumptions of linearity, normality or homoscedasticity of the residuals[60].

Table 9: OLS Regression Model Results (Dependent Variable: LNSALES)

Explanatory Variable	Expected Sign	Coefficients		*t* – statistic	Two-tailed Probability
		Unstandardised	Standardised		
Constant		2.673	na	9.175***	< 0.0005
LNEXPENS	+	0.689	0.693	18.302***	< 0.0005
HOURSWRK	+	0.123	0.157	4.530***	< 0.0005
BUSPLAN	+	-0.190	-0.104	-3.601***	< 0.0005
TECHNLGY	+	0.074	0.126	4.217***	< 0.0005
BUSAGE	+	0.016	0.067	2.206**	0.028
LNBANKFI	-	-0.020	-0.064	-2.342**	0.020
WORKEXP	+	0.165	0.057	2.091**	0.037

Adjusted R^2 = 0.781
F statistic = 157.608*** (p < 0.0005)
Significance level of F < 0.00005
Durbin-Watson = 2.067
Observations = 309

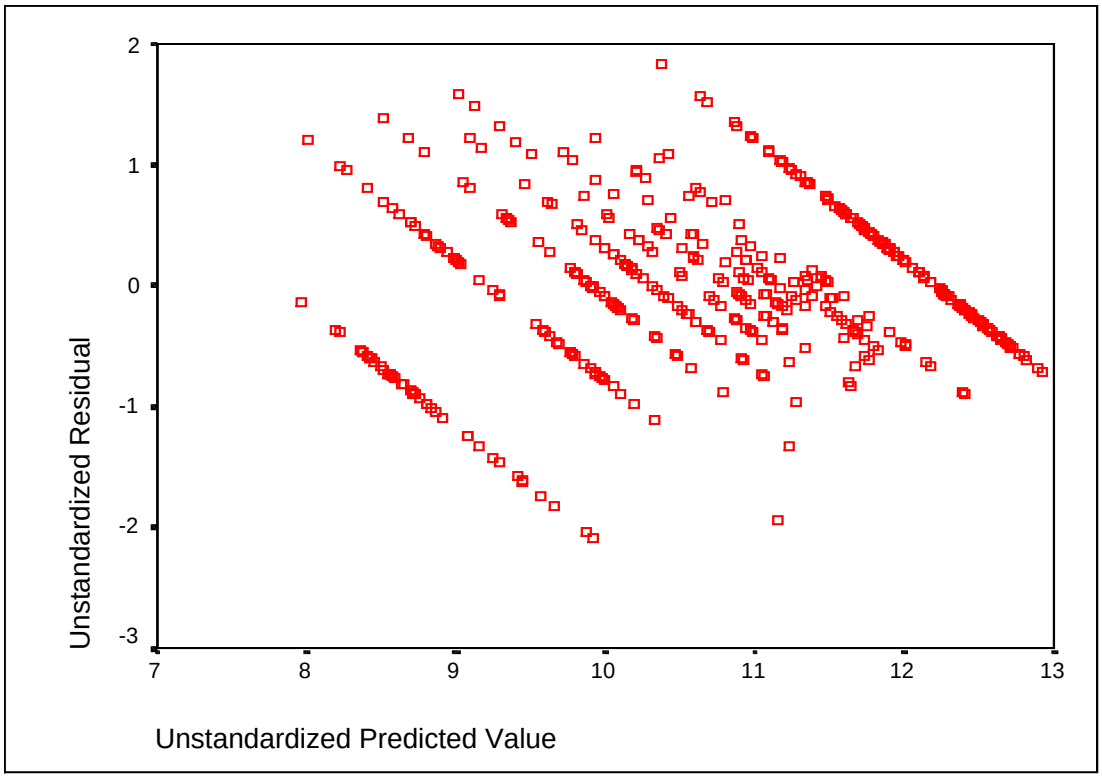
*, **, *** Denote significance at the 0.10, 0.05, 0.01 level respectively.
na Not applicable.

Analysis of the regression correlation matrix (in [58]) indicates that the largest regression correlation coefficients were between the explanatory variables LNEXPENS and HOURSWRK (0.605, p = 0.01) and LNEXPENS and TECHNLGY (0.408, p = 0.01) which, given the limits previously discussed, suggest collinearity is not a significant problem. The remaining correlation coefficients were well below 0.400. The tolerance value measures for assessing multicollinearity (in [58]) indicate LNEXPENS has the smallest tolerance value of 0.496. This value lies within the minimum threshold of 0.10 suggesting multicollinearity is not a significant problem [28, p. 127].

The multiple regression model was validated by regressing the explanatory variables modeled in this study, in standard variable selection method regressions of the original sample, as well as two sub-samples created through a random split of the original sample (in [58]). The signs of the coefficients for each explanatory variable are consistent between the various regression models, except for LNBANKFI (though small and not significant) in the standard variable selection model of sub-sample 1. The coefficients of all explanatory variables for all regression models are significant (p <= 0.10) with the exception of LNBANKFI and WORKEXP in the standard variable selection model of sub-sample 1. This is consistent with their marginal predictive power as indicated by the relatively low standardised coefficients (-0.064 and 0.057 respectively) and *t* statistics (-2.342** and 2.091** respectively) in the stepwise variable selection model of the original sample.

The models have a high level of similarity in their explanatory power. The results of the validation process indicate that the regression model estimated for the dependent variable LNSALES appears to be quite robust.

Figure 1: Scatterplot of Residuals Against Predicted Values (Dependent Variable: LNSALES)



Overview of Results in Relation to Hypotheses

Table 10 below presents an overview of the results of the bivariate and multivariate analyses undertaken to test the hypotheses formulated on HBB sales performance. Shading indicates the level of significance for each of these statistics with increasing significance indicated by darker shading. The summary indicates whether a relationship was found for each explanatory variable, and if so, its sign. A darkened cell border signifies that the relationship found is consistent with that hypothesised. It can be seen 10 of the alternative hypotheses were supported.

Table 10: Summary of Bivariate and Multivariate Test Results (Dependent Variable: LNSALES)

Hypotheses & Explanatory Variables	DEPENDENT VARIABLE: LNSALES						
	Predicted Sign	Mann-Whitney	T-Test	Spear-man[1]	Pearson[1]	OLS[2]	Summary
H_A1: Gender	?	+ m***	+ m***				+ m (- f)
H_A2: CHILDRES	- y(+n)	+ yes*	I				+ y (-n)/I
H_A15: SUPERANN	+ y(- n)	+ yes***	+ yes***				+ y (-n)
H_A17: WORKEXP	+ y(- n)	+ yes**	+ yes***			+y.057**	+ y (-n)
H_A16: BARTER	-			I			I
H_A9: BUSPLAN	+			I		-.104***	I / -
H_A12: INDUSTRY[3]	?			-.166***			-
H_A13: LOCATION[4]	+			+.106***			+
H_A11: BUSAGE	+				+.405***	+.067**	+
H_A4: GOVRSTN	-				I		I
H_A8: HOURSWRK	+				+.617***	+.157***	+
H_A7: LABEXPC	+				+.315***		+
H_A3a: LNBANKFI	-				+.140***	-.064**	+ / -
H_{A3}b: LNOTHFIN	-				+.298***		+
H_{A3}c: LNOWNFIN	+				I		I
H_A6: LNEXPENS	+				+.864***	+.693***	+
H_A14: NETWORK	+				I		I
H_A10: OUTSRCPC	+				+.252***		+
H_A5: TECHNLGY	+				+.411***	+.126***	+
H_A18: LNEMPLOY	+				+.370***		+

*, **, *** denote significance of the correlation coefficient and the regression coefficient *t* statistic at the 0.10, 0.05, 0.01 level (Two-tailed) respectively.

1 Correlation coefficient.
2 Standardised coefficient.
3 1-primary, 2-secondary, 3-tertiary.
4 1-farm, 2-rural non farm, 3-metropolitan.
I Statistically insignificant relation.

IMPLICATIONS OF THE FINDINGS FOR POLICY-MAKERS AND PROVIDERS OF ASSISTANCE AND ADVICE

Three broad implications arise from the findings of this study for policy-makers and providers of assistance and advice. Firstly, it can be seen that findings on the magnitude of HBB sales supports the assertion that HBB is not a marginal economic activity, but has the potential to generate significant income for owners, along with the attendant benefits for the larger community. The second implication of this study is the identification of factors that were found to have a relatively strong positive association with HBB sales performance, and thus which can be used to identify HBB of this type. These factors are total business expenses, the number of hours worked by the owner-respondent, the use of information and communication technology, business age, prior work experience, the proportion of total business expenses spent on labour, number of employees, other external

financing, outsourcing, owner-superannuation. Finally, a number of the findings of this study deserve more detailed consideration and analysis:

- The generally positive association found between the amount of external financing used and HBB sales suggests that it would be beneficial to ensure providers of finance understand the financial needs of HBB and their unique characteristics that differentiate them from small and medium enterprise (SME). These characteristics include the relatively low setup costs, low overheads and consequently relatively lower financial risk.
- A number of factors generally considered important to SMEs that were found to be unrelated to HBB performance should be brought to the attention of providers of assistance and advice. They were the use of a formal business plan and the extent of networking activity undertaken by the owner.
- Perceptions of the restrictiveness of Local and State Government regulations was found to have no impact on HBB sales performance. It is unclear whether this is because owners are generally unaffected by regulations or unaware of them.
- The positive relation found between HBB sales performance and the use of information and communication technology suggests that it is important that the technology equipment needs of HBB be taken into account by suppliers.
- The positive relation between HBB owner self-funded insurance coverage and HBB sales performance suggests the need to ensure that providers of superannuation offer policies that are suitable to the circumstances of HBB.

RECOMMENDATIONS FOR FURTHER RESEARCH

Future research should attempt to confirm the results of this study using a probability-based sampling technique. This would allow the results to be generalised to the broader HBB sector. Issues that warrant further investigation based on the findings of this study:

- The positive association between the use of information and communication technology should be further investigated. Do the reasons for this association relate to the type of applications of this technology?
- A number of findings were inconsistent with the literature and the hypotheses. The presence of a resident child(ren) was found to insignificant or positively related to HBB performance. The role of family in the

provision of unpaid labour should be investigated as well as ways by which to accommodate the competing demands of family responsibilities.

- The reason as to why Local and State Government regulations were generally found to not affect HBB sales performance should be investigated. Is it because owners are genuinely unaffected by regulations, or are they unaware or simply breaching regulations? This issue should be addressed as objectively as possible without relying on the perceptions of HBB owners.
- The apparent lack of association between HBB sales performance and networking activity should also be investigated given the inconsistency of this finding with SME literature.

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Empowering SMEs' growth and R&D through financing intangible investments. Finnish experiences from Business Development Loan.

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Summary

Evolutionary development of the firms is characterised by discontinuities and step changes in their life cycle. During these phases of step changes capital injections are often required in order to meet the needs of a growing company. Management development and organisational development are also often challenged in these situations. In a growing firm capital is tied into growth and they also often lack collateral and thereby have restricted access to finance. Public funding for discontinuities in the firm life cycle is arranged in many countries in the form of guarantees, mutual guarantee schemes and risk loans.

In this paper we discuss the Finnish experience on Business Development Loan that is a risk loan targeted to developing and growing firms. Growth and development often requires intangible investments that do not cumulate collateral. We will also discuss relationship between the financier and the entrepreneur. As a government owned risk financier Finnvera plc is characterised by very close relationship between the entrepreneur and the financier. We argue that the financier may also very important role in promoting business development in the firms and the close relationship can also be a vehicle for controlling risks involved in granting risk loans with weak collateral. This paper is based on experiences of practitioners in Finnvera and a study conducted in 1998 that dealt with experiences of entrepreneurs on Business Development Loan and business development.

1 INTRODUCTION

Great deal of research deals with financial problems of small firms[1]. Both the availability of financing and the cost of financing for those companies that want to grow and develop are discussed widely. Problems accessing external sources of finance have been identified in start-up phase and in so called discontinuities or growth jumps in the firm life cycle[2], [3]. However, pure markets have not solved the problem of access to finance for small businesses in any of the developed countries. Indirect or direct public intervention is widely accepted. In the continental Europe there are two wide spread models of indirect intervention: mutual guarantee systems[4], [5], [6] and public refinancing of investment credits. Direct government guarantees [7] exist in some countries as well. In addition, in the 1950's risk loan system through public credit institutions for SMEs lacking full collateral was developed in Nordic countries.

In this paper we discuss Finnish experiences on Business Development Loan (later BDL). The BDL is a risk loan that is targeted for financing business development and intangible investments in SMEs. Another objective of the instrument is to promote long-term business development based on the strategic objectives of firm. Financing of intangible investments is considered problematic, because these investments do not cumulate collateral. Projects dealing with intangible investments are also often riskier than investments in material objectives. Cash flow and revenues from these projects are realised in the long run. However, in order to successfully adapt to changing conditions and to maintain competitiveness in the long-run business development is vital for the firms. In Finland there is a long tradition in financing intangible investments in SMEs and thereby also experience in fostering small enterprises' willingness to invest in R&D. In this paper we will shed some light on credit granting procedure of Finnvera plc that we think is progressive among financiers.

Our definition of business development originates from the credit granting criteria of the BDL. Business development is distinguished from the day-to-day development work in the firms. Projects that are viable targets for the BDL are characterised by goal-orientation. Also results of these development projects are realised in the long run. The BDL is granted if the development project can be clearly distinguished from the normal activities of the firm. Development is thereby seen as a project that has objectives, implementation plan, schedule for implementation and estimate of costs.

2 FINNVERA AND THE BUSINESS DEVELOPMENT LOAN

2.1 Specialised financing company Finnvera plc

Finnvera plc is a financing company specialised in offering risk financing services to promote the domestic operations, exports and internationalisation of Finnish enterprises, specially SMEs. Finnvera plc was formed by merging the activities of Kera Corporation and the Finnish Guarantee Board on January 1 1999. The company is owned entirely by the Finnish state.

Finnvera plc is working closely with banks and other financial institutions and thereby complements risk financing in the Finnish finance market. Finnvera actively develops its portfolio of products in response to existing or future risk finance shortcomings in the market. With its development and financing solutions geared particularly towards small and medium-sized enterprises, Finnvera also helps to promote the government's regional policy objectives. Finnvera's activities are designed to offer viable Finnish firms opportunities to develop and expand. Finnvera's products are available to firms implementing feasible plans or to establish new firms based on a sound business idea.

Finnvera offers domestic loans, securities and export credit guarantees and insurance system. Portfolio of products covers all stages in the life cycle of a firm, ranging from loans for starting a new business to export guarantees for large company. Finnvera's financing products can used for funding business start-ups, business development, domestic supplies and investments. Companies that are internationalising or seeking to export, Finnvera can provide financing and export credit guarantees. Finnvera also intermediates European Investment Bank's loans and European Investment Fund's guarantees to Finnish SMEs and is the Financial Intermediary in the European Union's Joint Venture programme Phare-Tacis (JOP) and Joint European Venture Initiative (JEV) in Finland.

2.2 Business Development Loan

Finnvera bases its financing decisions on a business analysis, which evaluates current situation of the company, its market position and its future plans and development prospects for the business sector in question. Principally, Finnvera provides a part (mainly 50 % of borrowed capital) of the finance required.

The BDL can be used for the development of basic functions of the firm, product development and commercialisation and eligible targets are, for example, management training, development of product or production methods, development of marketing or preparation of international operations. To mention some

more examples of the use of the BDL, it has been used for implementation of a quality system, building up a data processing system, modifying lay out, training of personnel in a larger scale and patent charges

The BDL´s maturity period is at most seven years, in which the development period is at most three years and during that period no amortisation is needed. The development period is calculated as the time when the development project does not accumulate positive cash flow into the firm. Collateral is negotiated case by case. Usually collateral is secondary that means for example mortgage on company assets. The most common phase for using BDL is presented in figure 1 that is going through the death-valley in the development and growth phase.

Figure 1 Positioning of the BDL in the Finnvera's product range

BDL is also used for "goodbye" financing, when the firm is growing larger than SME size classes allow and it and BDL builds the ground for the firm to gather new equity because loan portfolio is improving when using BDL. BDL has undoubtedly contributed the rapid development of Finnish high-tech companies by softening up financing. BDL has also been a good tool to tackle the problem of lacking collateral in fast growing companies. A typical client of Finnvera's BDL is a subcontractor, which faces demands to develop own processes or new products and understandably their partners are not willing to pay or finance directly these actions.

2.3 Credit granting process and the communication between business analyst and the entrepreneur

Finnvera´s national service network ensures flexible handling of projects and fast decision making because most of the financing decisions related to domestic operations are made by regional offices. One of the Finnvera's values is to appreciate and to support entrepreneurship and most of the Finnvera's loans include state

subsidy in the form of lower interest rate. For this mentioned reason a considerable part of Finnvera's loans are risk loans (no collateral or weak collateral) and Finnvera's business analyst considers the lack of collateral in the interest level while processing a new application. The state also grants credit loss compensation to Finnvera. In practise this ensures the responsible business analyst with freedom to use more time in business development of customer firm without direct fear of loosing his/her job.

Finnvera grants only loans, guarantees and securities without taking deposits from the general public and neither does it take care of payment transactions. It allows more time for business analyst to operate with customers, compared to colleagues in a ordinary commercial bank. One of the basic features of the operating form of Finnvera is that business analysis and further negotiations are generally conducted in customer's own premises and entrepreneur has always "home field advantage". It can be assumed that he/she is also acting and speaking more naturally and the business analyst has better opportunity to built up an open contact to the entrepreneur.

Working field of Finnvera´s business analyst is divided to various business sectors and the business analyst has therefore a sound experience of analytical research on a specific sector with financing knowledge. Furthermore, the entrepreneur gets a good discussion partner. Commonly, Finnish entrepreneurs do not have discussion partners outside his/her family (if even there) concerning developing the firm and focusing the future plans. A Finnish SME-firm very seldom has an actually functioning board of management and even more rarely a board with members outside the firm or entrepreneurs family. This is the reason why a financier knowing the business sector is easily felt as a partner, whose ideas and questions are heard.

The previously described discussion contact leads easily to development discussions, in which the business analyst can together with the entrepreneur tackle the basic strategic questions and search the most suitable development targets and the reasonable terms of BDL and the possibility to take risk in securities promotes the discussion. The possibility for the business analyst to enter on the same side of the table as the entrepreneur creates trust to customers future plans and also willingness to take extra risk, because of open discussion and increased trust (risk transformation[4]). Negative surprises are also avoided better. Business analyst have not the same possibility to follow and control customers' payment transactions as their colleagues in banks, because practically all payments in Finland are taken care by commercial banks in on-line data processing. Instead, good and functioning co-operation with the customers replaces that type of direct source of information. Excessive engagement in the customer and his/her business is prevented by granting only a presentation task to the business analyst and the decision is always made by another person or body.

2.4 Research questions and conducting of the study

Research questions in the study[8] originated from the practical problems in the Finnvera organisation. The BDL was considered as a complex instrument for both customers and business analysts of Finnvera. Marketing of the instrument was difficult due to diverse use of it and many eligible targets of the BDL. Eligible targets for the loan were not clear to customers and thereby the work of business analyst was often characterised by intensive consulting and helping customers to define development projects in their operations and helping customers to use the instrument. Especially for the new customers, the BDL was quite difficult instrument. In the study we were looking for solutions to ease the use of Business Development Loan from both customers' perspective and from the perspective of business analysts in Finnvera. Furthermore we were looking for an answer to a question why do entrepreneurs have difficulties in recognising and recognising development projects in their operations. It seems that business development is often considered as something that is done on the side of day-to-day work in the firms. Thereby, these development tasks that actually do exist do not have a concrete plan, clear objectives or schedule for implementation, which would make implementation easier. It is very common that business analysts find development projects "on the side" of the actual investment projects during the customer visits. Large investments, for example in machinery, also require development in other areas like training of personnel, development of processes, changing the lay out of the plant etc. Quite often these "side" projects are large compared to financial resources of the firm. Research questions were defined as follows:

1. Purpose of this study was to find out how entrepreneurs perceive business development

   What is it? Why is it difficult to form development projects from the operations of the firm?

   How do entrepreneurs define and select sources of finance for business development?

The study was based on three different information sources namely 1) company analysis reports 2) interviews with the business analysts of Finnvera plc and 3) telephone interviews with entrepreneurs that have been granted business development loan. In the first phase of the study company analysis reports were analysed. These reports included general information on the financed firms and development projects in the firms. Analyses originated from the year 1994 to year 1998 and the total number of reports analysed was 190. The reports were randomly selected from the database of business analyses in Finnvera. The type of the development project and general features of each project was identified from these reports and then classified into subtypes in order to form general groups of different types of the use of the BDL for the interviews. In the second phase five business analysts from the Finnvera Plc were interviewed and in the third phase of the study 50 typical cases out of 190 firms that have been granted the BDL were selected. Entrepreneurs of these companies were interviewed

on their experiences of BDL and their view on business development and the role of financing in it. Interviews were conducted by telephone. In general, interviewees took very positive attitude to the interview and only one respondent refused.

2.5 Results based of the company analysis reports: typical targets of BDL

Life-cycle models[9], [10] are applied to some extent in the Finnish SME-policy. Services and products of the public financiers like Finnvera[11] and Tekes[12] (Technology Development Centre) as well as services of the Employment and Economic Development Centres[13] are organised on a life-cycle basis. Sudden growth jumps are typical in the company life cycle. These "total adjustment" cases include growth stage after initial growth after start-up, internationalisation, companies seeking to export and expansion to other geographical areas. Discontinuities[2] and sudden growth jumps in the company life cycle are stages where there is need for external capital injection in the firms and thereby these stages have potential for needs to be financed with BDL. Also the lack of collateral often hinders access to finance of growing firms. This is eased with Finnvera's risk loans like the BDL. Projects financed with the BDL are typically very important for the future competitiveness of the firms. They focus on objectives that change the competitiveness of the firm in a very fundamental way. Projects are often large compared to the size of the firm and as a result entering to new level of operations is enabled for the firm. To mention one example, after operating a few years part of the firms will enter to growth stage where production processes have to meet increased demand and these firms typically invests in machinery and new premises. These projects also include development elements that are eligible targets for BDL.

The company analysis reports provided information for classifying development projects by type of use of BDL. Largest share of the BDLs have been granted to R&D projects that can be further split to product development and process development. Development of processes often follows product development when the product is in the commercialisation phase. A typical combination is R&D associated with commercialisation and development of marketing. According to Moore[2] this is the phase where small high-technology firms face major problems in obtaining and managing finance. In the new technology-based firm the long R&D period has exhausted company's financial resources already before selling the first product. Operating firm has better resources for product development, because it has continuous cash flow. Product development projects financed with BDL can also be divided to projects of starting companies and projects of operating companies. Based on the company analyses continuation of product development and commercialisation of the product were the most typical targets for the loan. It is common that product development is financed partly with grants and when the

product enters to commercialisation phase the development deeded is financed with loans. Loans are more appropriate instruments for financing commercialisation, because it returns to lender as amortisation and thereby market distortions are avoided.

Internationalisation - establishing a position on the new market or seeking for export – were other large group of projects that were financed with the business development loan. Of the analysed projects 1/3 were related to internationalisation and also majority of companies that have used BDL were exporters. Companies were in different phases in their internationalisation process. A part of the firms were seeking to export, some companies were conducting a market research in a new market area and some companies were opening marketing channels in the new market. These firms may have prior experience on exporting and this time activities focus on the new market area. BDL is a suitable instrument for financing all these phases of export activities. Starting of exporting is related to the growth of the firm and it is a typical "step change" [2] in the firm's life cycle. The scope of the activities of the firm will be essentially larger than before. Simultaneously, growth also requires investments into the production capacity in order to meet the increasing demand.

Marketing was a typical development target in the companies and it was linked to many types of projects. In Finland, in many studies most common development needs and problem areas are related to marketing [14]. Some of the analysed projects concentrated on specific targets like development of advertising or preparation of sales promotion material. Marketing development was often related to the commercialisation of products and start of export as well as development of processes in the firms. This reveals that BDL has been applied not only to one need, but a bundle of needs, which describes the diversified nature of business development. These costs of intangible investments do not provide collateral and thereby financial resources like the BDL are important for the companies facing step changes. However, marketing is not among the most familiar targets to use external capital.

2.5.1 What is considered as business development in the firms?

One part of the study was related to nature of business development in the companies. Our question was how entrepreneurs conceive business development and how do they react on financing it with external capital? General principle is that investment decisions should be based on the expected future returns[15]. If these returns are to be realised in the long run also the length of the finance of these investments should match on the expected revenues. Today's generally accepted accounting principles call for the immediate expensing of R&D costs. However, intangibles often produce rich future rewards and R&D projects, products under development meet the

criteria of identifiable and measurable benefits and thereby could be amortised according to the expected duration of their benefits [15]. From the financiers' point of view it is sometimes problematic when the companies start developing projects that are financed from the short-term assets, usually from the working capital. Development projects are quite often considerably large so they effect on the liquidity of the firm. These problems could be avoided by starting to discuss with the financier at an earlier phase and selecting an the appropriate length of the financing for these projects.

We will also illustrate our text with some comments from the interviews of the entrepreneurs in order to give the reader an idea of the original thinking of the entrepreneur. We could say that the culture of financing intangible investment with external capital is under development in Finland. Some of the development targets are more easily financed with external capital. These projects include R&D and internationalisation and of course the scope of investment also influences on the capital requirements. Marketing development and personnel development are not typical investment targets that will be financed with external capital in the first place. From the interviews, it can also be noted that the severe recession in Finland in early 90's still influences firm's willingness to use external capital.

> *"It is more familiar to use external capital to new product development. It is the most important target. Finnish character is of this type that the entrepreneurs want to develop personnel and marketing with their own funds. In new product development there is more risk involved and therefore external capital is needed."*
>
> *"In the conceptual level nearly all activities in the firm could be included into business development. There is a certain caution for applying for a loan. It is related to fact, that certain things are experienced as such, that a firm should be able to finance from the funds generated from operations. And if not, it is thought that we will postpone those until we are able to finance them with income financing"*
>
> *"Development of marketing and personnel are so new areas to use external capital in a way that those things are seen as development targets and projects. Applying external financing for personnel training does not come to my mind, because it has not been possible before"*

Business development was considered as a very wide area in the firms and its importance for the long-term competitiveness of the firm was stressed. However, it is not easy for entrepreneurs to find development targets in their operations. Actually they seem to know what has to be done, but forming projects from strategic plans and to separate smaller development objectives seem to be difficult. It is a matter of scope in a sense that entrepreneurs see small development objects but binding them all together to larger projects would produce better results in faster implementation and better use of capital.

> *"Developing a business is very important, because it enables a firm of this size to survive in the EU. It takes a lot of funds. We do not get it, that we could have a loan (BDL), when we form packages of smaller things. We could have them more efficiently realised, financed."*

Firms are not willing to apply for external capital, because it is not familiar to use it for business development in some areas like marketing or personnel development. It is also typical that projects are financed from the income financing, which is not the best solution because the time for the implementation may be delayed or the other alternative is that projects are realised undersized due to limited reserves. On the other hand, necessary working capital is tight into development and it is usually not recognised until the liquidity of the firm weakens that realises the need for external capital. The following comments represent typical responses from the interviews and illustrate ideas of entrepreneurs on business development.

> *There are many areas (in business development): product development, product improvements, keeping products up to date and development of activities, personnel education, developing of computer system. It is the whole business scope.*

Keys to identification of projects are the size of the project compared to the resources of the firm as well distinction of it compared to normal activities of the firm. If the results of the development projects are not concrete enough or if the results are hard to measure the identification of development is more difficult. Personal contacts of the business analysts with the entrepreneurs create opportunities for identifying development projects in the firms. When a company applies financing for the investment, also development elements will be searched by the business analyst. Targets for the development are often found in informal discussions between the entrepreneur and the business analyst. If there is a clearly defined product development, technology development or quality system project starting in the company the need for external capital is recognised more easily in the firm. In these projects also grants are often applied from other public financiers.

2.5.2 Problems in defining development projects and the role of business analysts in this process

Business analysts form a very important link between the entrepreneur and the financier. Gibb[2] stresses the importance of the pursuit of certain projects as a focus for growth. He notes that such projects often involve combinations of new product development, new customer or market development, exploitation of new geographical areas or adoption of new production process or broader management system technology. These projects are very typical targets for the BDL.

Old customers of Finnvera create large share of the demand of the BDL, but for the new customers the idea of purpose and eligible targets for the loan need to be illustrated personally. Old customers are "easier" for the financier because they have recognised development projects in their operations and they have, in a sense,

internalised the idea of business development. Many companies face these challenges of "step changes" [2] for the first time and Finnvera's business analyst is the external advisor who makes this "hidden potential" or possible solution to problem visible to the entrepreneur and describes how it can be implemented. In many cases, need for the development is actually recognised in the firms but it does not move over to action.

One example of the consultation between the entrepreneur and the business analyst is described below. The idea of financing some development investments with the external capital is not familiar to the entrepreneurs but consultative role of the business analyst has influenced the way the entrepreneur sees the investment decision.

> *In the first place I did not consider external financing. This came up as a sum of other coincidences. We were discussing with the Finnvera business analyst of the previous BDL and he asked me if I have though that I could also consider external financing for the development and building up of an environmental system. I have not applied for the financing yet, but I might apply, because I do not tie working capital into it.*

Gibb also points out that there is very close relationship between business development, organisation development and management development in the SMEs. Development occurs when the process of solving problems and grasping opportunities takes place on a "need to know" basis and when the process is contextual to their own business[2], [16]. Consultative role of the business analysts enables SMEs to develop their activities in their own "home field" more efficiently. There are several elements and positive "triggers" in the interaction between the business analyst and the entrepreneur. Firstly, search for resources - in this case financing - is a situation where entrepreneurs are open to changes. Secondly, working is problem oriented and closely related to context of the firm. Thirdly, business analysts can give answers to "know how" problems and after conducting a business analysis may bring forward threats and opportunities on industry specific basis[2]. Unpacking strategic plans into action, forming a schedule for implementation and finding resources for the development are the keys to find out needs for the development financing.

Development in the companies is not only conceived as financing companies in their needs but also discussion and also in some extent consulting with the entrepreneurs. This extends the traditional role of the financier. Learning starts from what the entrepreneur already understands, knows and internalises. Business development takes place in entrepreneur's own environment, so the context of learning is as near as it can be. It means optimal circumstances for improving the potential for small business to develop. Gibb describes this 'need to know', 'how to' and 'who with' learning. It seems that the relationship between the business analysts

and the entrepreneur meet these criteria. Entrepreneurs learn with their business analysts and also from their business analysts. The following example describes this situation.

> *It was nice when the business analyst contacted us some times. The analyst could, for example go through his customers four times a year. Discussion does not have to be something extraordinary, but one always gets new ideas from the discussions from both sides.*

This learning partnership has a potential of reduction of transaction costs between the financier and the entrepreneur. Open discussion with the financier also provides fruitful ground for reducing the risk of financing with weak collateral by extracting more accurate information on firms.

Financial decisions are closely related to strategy and visions of the firm. Understanding the importance of long term development is often realised in discussion with the business analysts and the entrepreneur. Another strength of the consultative role of the business analysts is that it can create a strategic focus out of firm specific contextual problems. Granting of the BDL is based on a development plan and reporting after the project is concluded. Some entrepreneurs considered reporting bureaucratic in the first place but were in favour of the reporting after completion of the project. Typical answer was the following:

> *It is good to make a plan, because one has to know what will be done and in what time. It is possible to evaluate that the plan makes sense. It is also good to make a summary in order to conceive what was achieved*

Another good example to promote long-term development in the companies is to prepare a business plan or to update a business plan while applying finance for a new development project. Business plan ties long-term development projects together, because development projects can be anchored as “incremental steps“ into it. Some respondents mentioned that strategy based thinking is insufficient in small firms and preparing a business plan and a development project based on it help to create iterative steps from vision to action[2]. The entrepreneur may have a clear vision but the practical organising of how to reach these objectives stumble. How to turn visions and strategies to concrete plans and projects that can be implemented? The following comments from the entrepreneurs give more insight to the problem. It also describes entrepreneur’s openness to personal recommendations in step changes.

> *I have understood that there are also other things that are development, not only product development.* ***And why was that?*** *It came from Finnvera when I discussed with the business analyst and then realised that we can develop our business by doing a plan for some time scale and then proceed according to plan. When we put small things to together it becomes a big thing.*

> ***(interviewer's comment) You have a clear vision and a strategy of what the company will be in five years time, but it is difficult to turn this into projects and into action. Do you think this is a problem?*** *I have had similar problems. Basic functions should be developed, but it is about taking the first step. One is not sure if the resources that we have are enough or where to find additional resources. Are the resources mental or financial or what? Somebody should taunt the entrepreneur that you have a clear need to develop your activities and that there are methods available of how to do it. Problem arises from the fact that the entrepreneur is aware of the problems, but no-one does anything, because of the fear of costs and if it is going to succeed or not.*

Development work in the companies is not recognised as business development in a similar way than it is recognised by the financier. Possible explanation is that financing for the business development has not been available widely before. Stressing the importance of business development is a work from which the results are realised in the long run. The key issue here is that the financier may also have a very central role in promoting long term development of the firms. The idea of importance of the business development has many times been internalised as a result of the discussion between the business analysts and the entrepreneur. In the companies business development is realised through projects "iterative acts" that are based on strategic objectives of the firm. They provide a discussion partner for the entrepreneurs and help them to recognise and make development projects visible. Starting point for the owner-manager seeking external support for management development is recognition of needs[2]. It can be improved and exchanged with close relationship between the financier and the entrepreneur.

2.6 Case example of business development loan

In this following section, we will provide an example of the financial package from a real case in Finnvera. Finnvera's business analyst can build different financing packages based on Finnvera´s products suitable for the company or the project in question in order to spread the risks and also in order to lower the effective level of interest rate and to lower the level of accomplishment in the profitability calculations of the investment by using BDL as in the following example:

A client is applying for a 3.000.000 FIM investment loan half of which from Finnvera and the other half from the bank in order to build a new factory building and a new assembly line, because current machinery cannot fulfil the quality standards of the major customer. The firm has self-financing of 700.000 FIM. (1 EUR equals 5,94 FIM, 1 USD equals 5,79 FIM)

Financial Plan 1

Building project	2.000.000 FIM
Assembly line	1.200.000 FIM
Working capital	500.000 FIM
Total	3.700.000 FIM

The project is divided into subprojects during the business analysis and discussion with the entrepreneur:

-lay out changes	200.000 FIM
-ISO 9000 quality standard process and implementation	150.000 FIM
-training of personnel into using new machines	100.000 FIM
-salaries to personnel during mentioned phases	400.000 FIM
-development of new production method	250.000 FIM
Total	1.100.000 FIM

Table above presents costs that usually are unnoticed by the SMEs, because companies feel that these costs are a part of daily routine. The BDL may cover 70 % at maximum of this total sum that equals 770.000 FIM

Financing

Bank	1.115.000 FIM	Euribor + 2 %
Finnvera		
-investment loan	1.115.000 FIM	Euribor + 2 %
-development loan	770.000 FIM	Euribor + 0,5 %
Company	700.000 FIM	
	3.700.000 FIM	

Collateral

Mortgage to the new building maximum 70 % collateral value = 1.400.000 FIM

Order of priority	
1. Bank	500.000 FIM
2. Finnvera	500.000 FIM
3. Bank	500.000 FIM
4. Finnvera	500.000 FIM
	(small extra risk)

(all as collateral to investment loans)

Mortgage to company assets

Order of priority	
1. Bank	200.000 FIM
2. Finnvera	500.000 FIM

Advantages to firm, bank and the Finnvera

-The BDL offers a possibility to take more risk in form of weaker collateral to Finnvera

-Finnvera receives a proper 500.000 FIM mortgage and investment loans interest rate decreases and because of the state support overall interest reaches the same level as in a bank loan.

- the bank gets satisfactory security and the level of interest rate is best possible

- customer is paying interest (if Euribor is 3 %) during the first year approximately 140.000 FIM and is also given at least from one to two year free from amortisation to BDL

Without BDL:

Financing

Bank	1.500.000 FIM	Euribor + 4 %
Finnvera		
-investment loan	1.500.000 FIM	Euribor + 3 %
Company	700.000 FIM	
Total	3.700.000 FIM	

Collateral

Mortgage to the new building maximum 70 % collateral value = 1.400.000 FIM
Order of priority

1. Bank	500.000 FIM
2. Finnvera	500.000 FIM
3. Bank	500.000 FIM
4. Finnvera	500.000 FIM
	(small extra risk)

(all as collateral to investment loans)

Mortgage to company assets
Order of priority

1. Bank	200.000 FIM
2. Finnvera	500.000 FIM

Conclusion:
-The Bank has shortage in collateral. The customer or entrepreneur is obliged to arrange extra collateral in the value of 300-400.000 FIM and the interest rate generally increases by 1-2 %
-Finnvera has also the same situation despite of the smaller part in the financing package and Finnvera increases interest rate by 1-2 % depending from customers risk rating level
-the customer is paying interest during the first year approximately 180-210.000 FIM and has usually start paying amortisations to the whole loan amount
-loss to the customer is approximately 130-220.000 FIM to loan package of five years maturity
-BDL has a direct impact on competitiveness of the firm.

3 CONCLUSIONS AND RECOMMENDATIONS

Business development is vital for the long term-competitiveness of the firm. We argue that the close relationship between the financier and the firm produces results that encourage and foster SME's willingness to grow and develop. Evolutionary development of firms is often characterised by step changes in the company life cycle. Examples of these changes are, for example, internationalisation, new product or production process development. These step changes or discontinuities are also characterised by the need of external capital. Lack of collateral may hinder SMEs' access to finance, especially when we consider intangible investments that do not cumulate collateral. Lack of collateral is especially relevant problem for starting firms, high-technology firms and rapidly growing firms and it leads problems in mediation of financing. The BDL has undoubtedly contributed to rapid development of Finnish high-tech companies by softening up financing. It has also been a good tool to tackle the problem of lacking collateral in the fast growing companies.

The Business Development loan is targeted to meet the needs of growing and developing firms that prerequisites both willingness to grow and ability to grow and develop the firm. Close relationship enables the business analyst and the entrepreneur to stand on the same side. This relationship is based on trust that also enables risk transformation where the higher risk (due to weak collateral) is compensated with better knowledge on industry, deeper knowledge of the firm and the project at hand as well as knowledge on the entrepreneur.

Consultative role of the business analysts also helps in turning strategic plans into concrete actions and thereby it also helps finding new development projects in the firms. The relationship between business development, organisation development and management development in SMEs is very close. Financier is actually involved in all of these three areas. We argue that the relationship is closer than in some organisations that provide expert services for SMEs, since the relationship is based on mutual trust. It is also important to notice that the business development is realised through projects, incremental steps, which can be promoted with appropriate financing.

Financing intangible investment with external capital is a strange alternative for some entrepreneurs, especially regarding to investments in marketing and personnel development that are “soft” investments. Importance of the long-term development based on the strategic objectives of the firm is promoted by the consultative role of the financier. Business analysts have helped to form concrete plans and projects that can be implemented more efficiently. We argue that this has promoted the growth and development of firms that have been financed with the BDL and we argue that it is a successful course of action for a financier and it should be adopted in a larger scale.

Good practises of the BDL included:

- It encourages long-term business development that is based on the strategic objectives of the firm. Even if helping new customers to use the instrument takes time it is worth it.
- It matches the length of financing to the expectations on the future revenues of the intangible investment
- It ensures the liquidity of the firm during discontinuities (death valley)
- It shares the risk of financing between the banks and the public financier
- It implements flexible collateral requirement (company mortgages, weak collateral and even no collateral accepted)
- Takes advantage of extensive business analysis in order to manage risks associated with financed projects (risk transformation)

- In Finland there are also grants available for business development. Compared with the grants the operational range of the loan is wider and cost incurred can be included more freely.
- Entrepreneur has always “home field advantage”. That is the reason why a financier knowing the business sector is easily felt as a partner, whose ideas and questions are heard

Financing for R&D is mainly directed to high-tech companies. We argue that the BDL is important instrument in financing business development also in the traditional sectors. Business development, new product and process development is equally important in these sectors where other financial instruments for financing intangible investments are not available due to non high-tech nature.

Business development is a complex phenomenon and that makes the use of the BDL also complex. Often factors are related to other factors, like marketing development was related to commercialisation of products. This reveals that the BDL has been applied not only to one need, but a bundle of needs. Thereby, the common nominator is the whole scope of the development project. We strongly recommend financiers to strive for closer relationship to their customers.

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Small Firm Competitive Strategy: A Conceptual Model and Research Propositions

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Summary

The contribution of small firms to the economy has been well documented. However the small firm landscape is littered with failures which pinpoints to the need for research the small firm strategy formation activity. However much of the research efforts in this direction have been aimed at examining the presence or absence of strategic planning in small firms whilst small firms survive and grow without formal strategic plans. Research into small firm competitive strategy provides a viable and alternative path to examine the strategy formation characteristics of small firms. The capability-based theory of sustained competitive advantage (*SCA*) which has gained prominence in the competitive strategy literature over the last decade provides a sound theoretical foundation for this purpose. The capability-based theory suggests that firms possessing distinctive organisational capabilities gain *SCA*. Distinctive capabilities are developed and nurtured by the strategic leadership of the firm. This paper presents a capability-based model of organisational innovation and small firm competitive strategy. Organisational innovation is conceptualised as a learning process of which organisational learning capabilities are the antecedents. The model argues that entrepreneurial firms pursuing the innovation-based competitive strategy posess distinctive learning capabilities and these capabilities lead to higher innovation intensity and *SCA*. Key theoretical constructs within the model are explored and research propositions are presented.

Small Firm Competitive Strategy: A Conceptual Model and Research Propositions

1. Introduction

The contribution of small firms to the economy has been well documented. However contrary to expectations of policy planners and small firm stakeholders, small firm growth has been characterised by a high incidence of failures. Much of the research efforts in this direction have been spent on determining the failure rate rather than factors causing failure. On the other hand much of the research into small business strategy-formation activity has been aimed at examining the presence or absence of strategic planning in small firms. This research thrust has reached a dead-end where most of the researchers confirming that only around 20 per cent of small firms engage in formal strategic planning (e.g. Mulford et al. 1988; Robinson & Pearce 1984; Glen & Weerawardena 1996). However there is ample evidence to suggest that small firms continue to survive and grow without strategic plans.

Researchers argue that small firms are not smaller versions of large firms and they differ in their strategy-formation characteristics (Dilt & Prough 1989; Hills & La Forge 1985). Particularly, 'resource poverty' constraints the number of strategic options that can be pursued by small firms (Welsh & White 1981). On the contrary, research on Australian high-tech exporting firms suggest that small firms challenge the conventional wisdom by entering global markets and gaining sustained competitive advantage (*SCA*) with highly innovative products (McKinsey & Company and AMC 1993). Therefore innovation-based competitive strategy provides a viable and alternative research path to examine the strategy formation characteristics of small firms. The capability-based theory of *SCA* that has gained prominence in competitive strategy research during the last decade provides a sound theoretical foundation for this purpose. Interestingly capability-based theory has not been fully explored in the small firm competitive strategy literature. The framework presented in this paper examines the role of distinctive capabilities in small firm innovation-based competitive strategy.

This paper is organised into six sections. First, the links between organisational innovation and small firm *SCA* are examined. Second, a brief overview of *SCA* theory is presented. Third, the significance of distinctive organisational capabilities in gaining *SCA* is examined. Fourth, the foundations of the capability-based model of small firm competitive strategy are developed. Particular attention is given to exploring the key theoretical constructs and developing a core set of research propositions. Next, issues relating to operationalisation of the model are discussed. The paper concludes with a discussion on implications of the model for small firm competitive strategy.

2. Organisational innovation and sustained competitive advantage

Porter (1990) suggests that firms create competitive advantage by conceiving new ways to conduct activities of the value-chain for delivering superior value to the customers which is an act of innovation. This suggests, firstly, that innovation and the competitive advantage process are inter-connected. Secondly, innovation can occur in any value-

creating activity of the firm. Therefore innovation can be conceptualised broadly incorporating both technological and non-technological value-creating activities of the firm. Thirdly, all types of innovation can lead to *SCA*.

Empirical evidence supporting the view that innovation leads to *SCA* comes from several sources. Research examining the innovation and firm performance suggests that innovation lead to higher performance (Soni et al.1993; Lengnick-Hall 1992; Lefebvre et al. 1993). Innovative capabilities distinguish the more successful from the less successful growing small and medium-size enterprises (Statistics Canada 1994). Literature on export market penetration strategies suggests that innovation enables small firms to enter export markets and maintain or increase those markets once entry has been made (BIE 1993; Brush 1992). Successful innovation can play a critical role in small manufacturing firm export performance (Macpherson 1992; Kleinschmidt & Cooper 1990; Ong & Pearson 1982) even over the short run.

Although the literature on small firm innovation and SCA has grown in volume during the last two decades, much of the research is biased toward technological innovation. However, small firms undertake both technological and non-technological innovation (AMC 1995; BIE 1993;ABS 1995) and there is evidence to suggest that all such innovations lead to *SCA* (AMC 1995; Hyvarinen 1990). A growing number of researchers emphasise the need to adopt a broader definition of innovation in the competitive strategy research (BIE 1993; Hyvarinen 1990; Rothwell 1992).

3. The theory of sustained competitive advantage

Simply stated, competitive advantage is the ability of a business to derive abnormal profits or rent in a competitive industry (Aharoni 1993), based on a value-creating strategy not simultaneously implemented by any current or potential competitors. Competitive advantage grows out of the way the firm organises and performs discrete activities of the value-chain. This competitive advantage is sustainable when the advantage resists erosion by competitors' actions (Porter 1985) that are unable to duplicate the benefits of the strategy (Barney 1991).

During recent decades there have been two dominant models of competitive advantage (Lado et al. 1992). First is the environmental model of competitive advantage (Bain 1956; Hill 1988; Porter 1985). The other is the resource-based model of competitive advantage (Barney 1986; 1988; Dierickx & Cool 1989; Lippman & Rumelt 1982; Reed & DeFillippi 1990). In contrast to the environmental model that suggests that competitive advantage is market driven, the resource-based competitive advantage is driven by the specialised resources deployed to create a privileged market position. Both models assign a limited role to the key decision-maker of the firm in the *SCA* process and fail to offer a satisfactory explanation of the value-creation and service delivery processes.

The inadequacies of these models have paved the way for the capability-based theory of competitive advantage. The capability-based theory suggests that a firm can achieve competitive advantage through distinctive or core-

capabilities possessed by the firm (Stalk et al. 1992; Grant 1991; Prahalad & Hamel 1990; Mahoney & Pandian 1992; Long & Vickers-Koch 1995; Hayes et al. 1996) and the firm must constantly re-invest to maintain and expand existing capabilities in order to inhibit imitability (Mahoney 1995). In the current study organisational distinctive capabilities are defined as follows.

> Distinctive capabilities refer to the organisation's capacity to perform a range of organisational routines (sequence of coordinated actions) for the purpose of delivering products and services to the market in a manner that outperforms competitors. Distinctive capabilities are information-based knowledge systems.

The capability-based theory effectively explains the value creation process by assigning a proactive and dominant role to the strategic leadership of the firm. Distinctive capabilities that enable firms to gain competitive advantage are developed consciously and systematically by the wilful choices and actions of the firm's strategic leaders (Lado et al. 1992; Child 1972; Smircich & Stubbart 1985; Weick 1979; Grant 1991; Hayes et al. 1996). Therefore strategic leadership occupies a proactive and dominant role in the value creation process.

The competitors' inability to duplicate the distinctive capabilities is suggested as the key source of sustainability under the capability theory of competitive advantage (Grant 1991; Hayes et al. 1996). Coyne (1986) and Hall (1993) concur with this view and suggest that sustainability of competitive advantage rely on the 'capability differential' on which competitive strategy is founded. This view is strengthened by the concept of 'causal ambiguity' by Reed and Defillip (1990) which suggests that ambiguity over the factors responsible for a business's superior performance creates a barrier to imitation by competitors.

Given that the strategist plays a vital role in building and nurturing organisational capabilities, the capability-based theory provides a meaningful framework to examine the role of organisational innovation in the small firm competitive strategy. Innovations cannot occur in the absence of an entrepreneurial owner/manager who engages in building and nurturing innovative capabilities and integrating new knowledge into the value-creating activities of the firm. The capability-based theory therefore facilitates the examination of the behavioural antecedents of the innovation process and their role in gaining *SCA*. Interestingly the capability-based theory has not been fully explored in the small firm competitive strategy research. The extant literature is limited and fragmented (e.g. Stoner 1987; Haahti 1988; Lefebvre et al 1993; Acar 1993; Houlden 1986) and there is a need for a framework which will facilitate the formation of a consistent body of knowledge on small firm competitive strategy.

4. Learning processes and organisational innovation

The antecedents of organisational innovation are determined by the manner in which the innovation process is conceptualised. Premised on organisational learning approaches to innovation (Brown, 1992; Tushman & Nadler, 1980; Day, 1994: Dodgson & Bessant, 1996), this paper conceptualises organisational innovation as a learning

process in which the new knowledge acquired by the firm is integrated into value-creating activities. The firm's learning capabilities play a crucial role in generating innovations (Sinkula, Baker & Noordewier, 1997).

Organisational learning theory suggests that there are two learning levels that lead to organisational change: adaptive learning and generative learning. Adaptive learning or 'single-loop' learning is the most basic form of learning and occurs within the learning boundary of the firm (Argyris, 1977; Senge, 1990). The learning boundary constrains organisational learning to an adaptive variety which normally is sequential, instrumental, and focused on issues or opportunities that are within the traditional scope of organisational activities (Slater & Narver, 1995). In contrast, generative learning or 'double-loop' learning occurs when the organisation is willing to question long-held assumptions about its mission, customers, competitors, and strategy (Argyris, 1977; Senge, 1990). Importantly, generative learning is a potential source of *SCA* (Sinkula, 1994; Slater & Narver, 1995). Generative learning involves changing the firm's knowledge-base, firm-specific capabilities and routines, and is analogous to the firm's intellectual skills.

The degree of innovation reflects the extent of new knowledge embedded in an innovation (Dewar & Dutton, 1986; Ettlie, 1983). Single-loop learning is associated with incremental innovations, whereas double-loop learning is associated with discontinuous or radical innovations (McKee, 1992). 'Radical and incremental pertain to distinctions along a theoretical continuum of the level of new knowledge embedded in an innovation' (Dewar & Dutton, 1986: 1423). Under the radical innovation strategy, effective learning systems become critical, as Tushman and Nadler (1986: 76) observe: 'As innovation moves from incremental to discontinuous, there are higher risks and greater uncertainty. It becomes increasingly important for organisations to function as effective learning systems, benefiting from both failure and success.'

Radical innovations imply that a firm is engaging in generative learning levels, the highest level of organisational learning. The firm should fulfil several requirements in order to scale the summit of generative learning which include learning from both external and internal sources, the presence of entrepreneurship, and unlearning. Organisations must continually balance learning from internal sources (i.e., exploitation) and external sources (i.e., exploration) to be effective learning systems (March, 1991). The presence of entrepreneurship facilitates generative

learning. A culture that values entrepreneurship and innovation provides the environment in which learning from exploitation and exploration is most likely to occur (Prahalad & Hamel, 1991; Sykes & Block, 1989). Similarly, unlearning is critical to attaining high levels of generative learning (Slater & Narver 1995; Leonard-Barton, 1992; Levitt & March 1988; March, 1991; Schein, 1990). Essentially, unlearning refers to regularly reviewing unsuccessful past learning efforts and communicating the results within the organisation (Day, 1994).

In summary, entrepreneurial firms pursuing an innovation-based competitive strategy build and nurture distinctive learning capabilities. The degree of entrepreneurship, the extent of learning from both external and internal sources, and unlearning will influence the firm's ability to achieve generative learning levels. The extent of generative learning is reflected in the degree of organisational innovation pursued by the firm.

5. A Capability-based model of small firm competitive strategy: System of relationships and research propositions

The capability-based model of organisational innovation and small firm SCA is illustrated in Figure 1. The model incorporates six key theoretical constructs. The entrepreneurial intensity is an exogenous construct and the endogenous constructs include market-focused learning capability, internally-focused learning capability, relational learning capability, organisational innovation intensity, and *SCA*. Innovation intensity plays the role of an intervening construct between the capabilities and *SCA*. This paper argues that small firms pursuing the path of innovation-based competitive strategy possess distinctive learning capabilities that are built and nurtured by the strategic leadership of the firm. The strategic leadership of the firm is conceptualised in terms of entrepreneurial intensity. The paper distinguishes between three key learning processes: market-focused learning capability, internally-focused learning capability, and relational learning capability. These learning capabilities capture the domain of the small firm's knowledge base.

Out of the three learning capabilities incorporated in the model market-focused learning capability and relational learning capability capture small firm's capacity to learn from external sources. Internally-focused learning capability reflects the firm's ability to learn from internal sources. The model therefore suggests that innovative small firms learn from both internal and external sources. The entrepreneurial owner/managers in their distinctive

learning capability building efforts also undertake active unlearning. The model therefore fulfils the requirements for reaching generative learning level.

In summary, the model suggests that small firms with higher levels of entrepreneurial intensity will possess distinctive learning capabilities. In turn, these distinctive capabilities lead to higher innovation intensity and *SCA*.

Insert Figure 1 about here

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6. Entrepreneurial intensity and distinctive capabilities

Much of the strategy literature suggests a positive association between 'entrepreneurship' and the growth-oriented efforts of the firm. An entrepreneur is an owner/manager who possesses innovative abilities and makes strategic decisions for his/her firm (Collins & Moore, 1970; Miller 1983; Shapiro, 1975). A firm's entrepreneurial orientation is a crucial factor in determining its competitive orientation (Merz & Sauber 1995). Entrepreneurial organisations often initiate actions to which competitors then respond, and are frequently first-to-market with new product offerings (Khandwalla, 1977).

Rizzoni (1991) establishes a link between small firm entrepreneurship, organisational capabilities and innovation. According to him, a firm pursuing an innovation-based strategy accumulates specific capabilities, which distinguish the firm from its competitors and enable it to face the viability of the environment. Premised on the capability-based theory, the model argues that a link exists between small firm entrepreneurship, organisational capabilities, and organisational innovation. In our view, the survival and growth of the firm are based on its ability to develop a position of superiority in the development of organisational capabilities. The proposed relationships between small firm entrepreneurship and distinctive organisational learning capabilities are discussed in the following sections.

7. Market-focused learning capability

Innovations arise as the result of a perceived and sometimes clearly articulated customer need. This position is known as the “market-pull” or “need-pull” approach to innovation that emerged in the 1960s. To be effective innovators, organizations should constantly scan the horizon for new opportunities to satisfy their customers (Levitt, 1960). Generating innovative ideas through market-focused learning is the starting point of organisational innovation and competitive strategy (Khan & Manopichetwattana, 1989; McKinsey & Company, 1993; Foxall & Fawn, 1992; Sinkula et al. 1997). This position is reflected in much of the research on market orientation and organisational performance. Because a market orientation reduces the degree of incompatibility of new products with customer needs, it is likely to enhance the adoption and success of innovations (Kohli & Jaworski, 1990; Webster, 1988; Cooper & Kleinschmidt 1987). Researchers argue that small firms compared to large firms are quick to react towards the changes in markets and new possibilities (Rothwell 1983; 1986).

Building on the key learning processes suggested in the literature (Huber, 1991; Sinkula, 1994) small firm market-focused learning capability is defined as the capacity of the firm, relative to its competitors, to acquire, disseminate and use market information for organisational change. This definition of market-focussed learning extends the concept of market orientation. It is argued that entrepreneurial small firms possessing high levels of market-focused learning capability not only learn from markets but also disseminate such knowledge within the firm. These firms integrate the waves of knowledge acquired into value-creating activities of the firm. The following relationship between entrepreneurship and market-focused learning capabilities is proposed.

P1: Small firms exhibiting a higher degree of entrepreneurial intensity possess more distinctive market-focused learning capabilities than those exhibiting a lesser degree of entrepreneurial intensity.

8. Internally-focused learning capability

Organisations learn either by experience and/or strategic choice (Child, 1972). This paper conceptualizes internally-focused learning capability as small firm’s capacity of the small firm to learn through strategic choice. This includes key mechanisms for internally generated learning such as experiential learning (i.e., trial and error) and experimental

learning (i.e., finding new ways of doing things). A commonly pursued experimental learning activity in manufacturing firms is in-house research and development (*R&D*) activity. *R&D* can be viewed as a search process to learn and generate cumulative technological advances (Durand, 1988; Hyvarinen, 1990). In-house R&D is an important source of knowledge acquisition, and there is a good deal of empirical evidence supporting the position that in-house *R&D* is essential for effective innovation (Macpherson, 1992; Kim, Kwangsun & Lee 1993). There is supportive evidence for the existence of formal *R&D* units and *R&D* expenditure in small firms (Hyvarinen 1990; BIE 1993). However, Australian firms use the terms *R&D*, product development and 'problem solving' interchangeably (AMC 1995). Therefore the current model conceptualises the internally-focussed learning activity broadly to cover all experimental activities aimed at enhancing small firm's technological and non-technological knowledge base. Internally-focused learning capability is defined as the capacity of the firm, relative to its competitors, to internally generate, technological and non-technological knowledge, and to disseminate, unlearn, and use this knowledge for organisational change. This definition moves beyond the scope of the firm's traditional *R&D* activity. Small firms possessing internally-focused learning capability not only learn from internal sources but also disseminate such knowledge within the firm. These firms actively undertake unlearning and integrate internally-generated knowledge into innovations. The following relationship between small firm entrepreneurial intensity and internally-focused learning capabilities is proposed.

P2: Small firms exhibiting a higher degree of entrepreneurial intensity possess more distinctive internally-focused learning capabilities than those exhibiting a lesser degree of entrepreneurial intensity.

9. Relational learning capability

Exploiting external knowledge is a critical component of innovative activities (Cohen & Levinthal, 1990). Though in-house *R&D* and other forms of internally-focused learning may be necessary, firms have to access external resources and modify them in order to develop the capabilities needed to respond to changing market conditions effectively. Collaborative linkages or "networking" improve the innovation potential of the organisation (Achrol 1997; Contractor & Lorange, 1988; Mowery, 1988). External technology linkages are frequently employed strategic alternatives to internal R&D efforts in highly innovative firms (Rothwell 1989; Kurokawa, 1991; Rothwell & Dodgson 1991). Fast-growing innovators are the most extensive users of external technological linkages. External

linkages supplement the development of new products and processes of small firms which tend to suffer a marked disadvantage in material and human resources required for technological innovation (Rothwell & Dodgson 1991; Kim, Kwangsun & Lee 1989). This paper distinguishes relational learning capability from market-focused learning capability. Market-focused learning capability reflects the firm's capacity to learn from customer and competitor behavior, whereas relational learning reflects the firm's capacity to learn through links and networks formed with external institutions and firms. Relational learning capability is defined as small firm's capacity, relative to its competitors to acquire technical and non-technical knowledge through external linkages, and to disseminate, unlearn and use such knowledge for organisational change. This definition explicitly recognises the role of inter-firm networks for knowledge acquisition. Small firms possessing high levels of relational learning capability not only learn through networks but also disseminate such learning within the organisation, actively engage in unlearning and integrate the new knowledge into the firm's value-creating activities. Based on this discussion, the following proposition regarding small firm entrepreneurial intensity and relational learning capability is advanced.

P3: Small firms exhibiting a higher degree of entrepreneurial intensity possess more distinctive relational learning capabilities than those exhibiting a lesser degree of entrepreneurial intensity.

10. Distinctive learning capabilities and small firm innovation intensity

As noted, innovation and competitive advantage research is biased towards technological innovation and the need for a definition of innovation that covers a broad range of organisational activities is well-recognised (Damanpour, 1991; Hyvarinen, 1990; Rothwell, 1992; Dewar & Dutton, 1986). There is evidence to suggest that small firms including 'micro-businesses' pursue all forms of innovation simultaneously in the competitive strategy (BIE 1993; ABS 1995). McKinsey & Co. (1993) observes several types of innovation including product, process, and business systems innovation. Broadly defined, organisational innovation involves the application of new ideas in any of the firm's activities. Specifically, innovation has been conceptualised in terms of two notions: the "newness" of an innovation (Damanpour, 1991; Hyvarinen, 1995; Tushman & Nadler, 1986) and the "total value created" by the innovation (McKinsey & Co. 1993). The notion of newness refers to what is perceived as new by the relevant unit of adoption (Dewar & Dutton, 1986) and the degree of newness reflects the new knowledge embedded in innovations. Based on this discussion, organisational innovation is defined at the level of an individual firm, as the application of

ideas that are new to the firm, to create added value either directly for the enterprise or indirectly for its customers, regardless of whether the newness and added value are embodied in products, processes, work organisation and management, or marketing systems. Based on this discussion the following propositions regarding the learning capabilities and organisational innovation intensity is advanced.

P4: Small firms possessing high levels of distinctive market-focused learning capabilities achieve higher degrees of organisational innovation intensity than those with low levels of market-focused learning capabilities.

P5: Small firms possessing high levels of distinctive internally-focused learning capabilities achieve higher degrees of organisational innovation intensity than those with low levels of internally-focused learning capabilities.

P6: Small firms possessing high levels of distinctive relational learning capabilities achieve higher degrees of organisational innovation intensity than those with low levels of relational learning capabilities.

11. Organisational innovation intensity and *SCA*

There is little consensus among researchers on the term 'sustained competitive advantage' (Day & Wensley, 1988). However, competitive advantage can be conceptualised as a superior 'marketplace position' that captures the provision of superior customer value and/or the achievement of lower relative costs, which results in marketshare dominance and superior financial performance (Hunt & Morgan, 1995). Much of the existing research uses superior financial performance or 'rent' as an indicator of competitive advantage (Aharoni, 1993; Jacobson, 1988; Porter, 1985). Sustained competitive advantage is believed to be simply a competitive advantage that lasts a long period of calendar time (Jacobson, 1988; Porter 1985). These views have attracted criticism from recent literature (Barney, 1991; Day & Wensley, 1988) and there is a need to conceptualise this construct incorporating well-founded and realistic indicators of *SCA*. This paper concurs with Day and Wensley (1988) who do not totally discard financial indicators of *SCA* but suggest comprehensive indicators of market advantage should include financial indicators.

SCA exists when current and potential competitors are unable to reproduce the value creation strategy adopted by the firm (Barney, 1991). A competitive advantage can only be sustained if it continues to exist after efforts to duplicate

that advantage have ceased (Rumelt, 1987). The concept of 'competitive duplication' that has been used as key criteria of sustainability in the environmental and resource-based models, has been used specifically in the capability-based theory in the context of distinctive organisational capabilities. The inimitability of distinctive capabilities or the 'capability differential' is a key source of sustainability under the capability-based model (Grant, 1991; Hayes et al. 1996; Coyne, 1986; Hall, 1993).

Our early discussion of innovation-based competitive strategy revealed evidence suggesting that innovation is a source of small firm competitive advantage. It was observed that past research has been biased toward technological innovation, although there is some evidence suggesting that small firms use all types of innovation to gain *SCA*. The following proposition regarding organisational innovation intensity and *SCA* is advanced.

P7: There is a positive relationship between small firm organisational innovation intensity and SCA.

12. Operationalising the model: Issues

As in any relatively new area of theory building, there are a number of obstacles to surmount in the translation from theorising to measurement and testing. The proposed model is premised on the capability-based theory of *SCA* and draws heavily from the organisational learning approaches to innovation. The literature in both these areas has grown in volume over the last decade. The capability-based theory, in particular, has reached the stage where theoretical constructs need to be measured and key theoretical propositions need to be tested to progress the small firm competitive strategy theory. As noted, evidence regarding the antecedents and antecedents of organisational learning is primarily anecdotal (Slater & Narver, 1995; Garvin, 1993). Organisational learning theory has received the attention of small firm innovation researchers only during recent years (e.g. Gibb 1997; Raffa & Zollo 1994; Hyvarinen 1995). In general, there is a need for both fine-grained and coarse-grained research to answer important questions relating to learning relationships suggested in the literature (Slater & Narver, 1995). This paper advocates the theory-testing path to examine the theoretical relationships proposed in the model, which will move the capability theory beyond its current fragmented status. The resultant framework will facilitate future research and contribute towards the formation of a consistent and well-founded body of knowledge on small firm competitive strategy.

For testing the proposed theoretical model we advocate the use of quantitative methods including structural equation modelling (SEM) techniques. Testing such a model would involve the development of measures for each theoretical construct and testing the relationships in the theoretical model. The theoretical constructs incorporated in the model are latent variables that cannot be observed directly. Given the nature of the constructs in the model, and the multiple interdependence relationships that have been specified, SEM appears to be appropriate method for estimating the proposed model (Anderson & Gerbing, 1988). In view of the relatively under-developed nature of the empirical base of the capability-based theory it is advocated to use the 'two-stage' approach to SEM for the development of measures for theoretical constructs and test the theoretical relationships proposed in the model. In this approach measurement models are first estimated prior to estimating the structural model. This approach enables researchers to maximise the interpretability of both measurement and structural models (Anderson & Gerbing, 1988; Hair et al. 1995; Kenny, 1979; William & Haser, 1986).

As noted earlier, distinctive learning capabilities that enable the firm to achieve *SCA* are built and nurtured by the strategic leadership of the firm. In the current model small firm strategic leadership is conceptualised in-terms of entrepreneurial intensity. However there is no commonly accepted definition of entrepreneurship. Small business research frequently fails to distinguish explicitly between entrepreneurial behaviour and the behaviour of small business ownermanagers (Jennings & Beaver 1997). For example some researchers challenge the past belief that the creation of a small business, does not require entrepreneurial activity as an essential prerequisite. The artisan who drifted into small business ownership, perhaps on the basis of the 'unfriendly push' or through 'no alternative' may have absolutely no intention or desire to maximise profits and growth through risk taking strategic management (Birley 1989; Jennings & Graham 1997).

It is therefore recommended that this construct is operationalised using recent behavioural approach to entrepreneurship. This approach focuses on the behaviour of small firm instead of the behaviour of ownermanager. Entrepreneurial firms display three characteristics in their managerial decisions, namely, proactiveness, innovativeness and risk-taking (Slater & Narver 1995; Covin & Slevin (1986); Gartner 1988; Miller 1983; Stevenson & Jarillo 1990). These characteristics form the basis of the entrepreneurship scale developed by Covin

and Slevin (1986) who argue that behaviors rather than psychological attributes give meaning to the entrepreneurial process. Behavioral manifestations of entrepreneurship can be reliably, verifiably, and objectively measured enabling researchers to differentiate between firms with different levels of entrepreneurial intensity. The scale developed by Covin and Slevin (1986), was found to be positively related to performance and business strategy (Covin & Slevin, 1986; Schafer, 1990). Similarly, the components of the entrepreneurship scale were found to be positively related to other performance related outcomes, for example, risk taking, proactiveness, and technological innovation (Khan & Manopichetwattana, 1989; Lefebvre & Lefebvre, 1992). This approach to operationalising the entrepreneurial intensity construct suggests a multi-dimensional measure in which each dimension originates from a separate set of indicators. We propose using the indicators used by Covin and Slevin (1986) for this construct.

The model incorporates three learning capabilities: market-focused learning, internally-focused learning, and relational learning. These constructs were defined in earlier sections. These definitions encompass the key components of learning processes suggested in the literature, namely information acquisition, information dissemination, unlearning and integration of learning into organisational change (Huber, 1991; Sinkula, 1994). In the generation of indicators for the learning capability constructs, the fourteen-item measure for market-focussed learning suggested by Day (1994) provides valuable guidance. This measure operationalises market-focussed learning capability in terms of the four learning activities outlined above. In generating indicators for the internally-focused learning capability, researchers will benefit by using the measure for *R&D* capability developed by Atuahene-Gima (1993). However, our approach to conceptualising this construct encompasses both technological and non-technological learning. Therefore, in adapting the Atuahene-Gima (1993), measure it will be necessary to incorporate both learning activities. As an additional measure of the distinctiveness of each of the capability constructs we propose that respondents are asked to indicate the extent to which a particular capability has been instrumental in outperforming competitors. This approach to measuring the distinctiveness of organisational capabilities is based on the work of Snow and Hrebiniak (1980).

Next, organisational innovation is conceptualised as both technological and non-technological innovation. The literature suggests two key elements in measuring the degree of innovation, namely, ‘newness’ and ‘value-creation.’ We propose that a composite measure incorporating both the degree and type of innovation will not only capture

small firm innovation intensity of but also provide researchers with a comprehensive and realistic measure of small firm innovation. The degree of innovation can be operationalised as a continuum ranging from incremental to radical innovations (Lipparini & Sobrero, 1994; Dewar & Dutton, 1986; Ettlie 1983). The type of innovation can be operationalised in terms of technological and non-technological value-creating activities of the firm (Porter, 1985; Schumpeter, 1934; Rothwell, 1992). Based on recent empirical evidence (AMC, 1995), we propose expanding the two categories of innovation to include product and process (i.e., technological) managerial and marketing (i.e., non-technological) innovations.

Our discussion on the *SCA* construct revealed the weaknesses of existing measures of *SCA* and suggested a number of paths, which can be pursued in assessing competitive advantage. This paper proposes using market performance indicators, strengthened with customer centred measures such as customer loyalty, along with other criteria suggested in the literature such as the inability of competitors to duplicate the firm's competitive strategy (Barney, 1991; Grant, 1991; Coyne, 1986; Hall, 1993). Accordingly, we suggest that the SCA construct be operationalised in terms of three elements: (1) extent to which organisational innovation has enabled the firm to gain market advantages, (2) whether it is possible for competitors to duplicate innovations, and (3) whether it is possible for competitors to duplicate distinctive capabilities on which advantages have been founded.

Appropriate key informants for future empirical studies in this area include ownermanagers of small firms. The chief executive officer is typically familiar with all aspects of the company's operations, influences the strategic direction of the company, and plays a key role in technology adoption decisions (Hambrick, 1981; Miller & Toulouse, 1986). There is a clear and documented evidence of a consistent decline in strategic awareness towards the lower levels of the management hierarchy (Hrebiniak, 1981).

13. Conclusions

The proposed capability-based model of organisational innovation and small firm *SCA* incorporates key theoretical propositions from the competitive strategy literature. First, the model suggests that a firm can achieve *SCA* through the distinctive capabilities in its possession. Second, distinctive capabilities do not merely accrue to the firm but are consciously and systematically developed and nurtured by the firm's strategic leaders. Next, the model suggests that

competitive advantage can be gained by creating superior value for customers, and can be achieved by performing the activities of the value-chain in an innovative manner. Fourth, firms reaching higher levels of organisational innovation intensity are likely to gain *SCA*. Furthermore, the manner in which the key theoretical constructs are conceptualised suggests their interrelationships have important implications for small firm competitive strategy theory and practice. Our discussion is organised around the following four themes: (1) strategic leadership, (2) learning capabilities, (3) organisational innovation intensity, and (4) *SCA*.

The capability-based theory implies that distinctive capabilities are built and nurtured by the strategic leadership of the firm. As noted earlier the literature on small firm distinctive capabilities has been limited and few attempts have been made in past research to conceptualise this construct in a testable manner. In the framework presented in this paper strategic leadership is conceptualised in terms of the entrepreneurial intensity of the firm. In contrast to traditional trait-based or psychological approaches, entrepreneurial intensity parallels the more recently adopted behavioral approach to measuring entrepreneurship (Covin & Slevin, 1986; Naman & Slevin 1993). According to this approach, entrepreneurship is a behavioral phenomenon that exists when a firm displays high levels of innovativeness, proactiveness, and tolerance for risk in strategic decision-making. Though the link between entrepreneurship and small firm performance has been examined, the proposed relationship between entrepreneurship and small firm capability building activity has not received the same degree of attention. This proposition, which is a key feature in the capability-based theory of *SCA* has not been tested in prior research, particularly in a small business context. This proposition also provides new research directions for the theory of small firm entrepreneurship.

The manner in which entrepreneurship is conceptualised has implications for practitioners. The model presented here implies that any small firm can adopt an entrepreneurial posture by displaying innovativeness, a high tolerance for risk-taking, and proactiveness. In our theoretical framework, entrepreneurs are not ‘born’ as suggested in conventional theories, rather small firms can be guided and educated to become entrepreneurial in their decision-making through strategic leadership. This interpretation has important implications for policy planning. For example, small ownermanagers can be educated and trained to engage in firm-level entrepreneurship.

As such, the model presents small business practitioners with a feasible path for building SCA. Small firms striving to gain competitive advantage should pursue an innovation-based competitive strategy. Innovation is conceptualised as a learning process and small firms pursuing an innovation-based competitive strategy must develop and nurture distinctive learning capabilities. However, firms pursuing this path should recognise that building learning capabilities can be an expensive and tedious undertaking (Hayes et al. 1996). The process involves first developing certain abilities, then selecting a few of these abilities and devoting the time and resources necessary to develop them into capabilities, and finally polishing and refining a very few capabilities to the point where they become the basis for competitive advantage. Hayes et al. (1996: 505) summarise the process:

> Converting an ability to a real capability does not happen by accident: it takes time (not just man-hours, elapsed time) and consumes resources. And building such a capability into something that can become the basis of a competitive advantage requires a dedication that approaches fanaticism; the time and resources required often well exceed what one can logically justify.

These views imply that a small firm cannot be world-class in everything it does and strategists should recognise the implicit trade-off in building distinctive capabilities. More generally, high levels of learning capabilities will enhance the overall knowledge base of the firm, and this in turn will be reflected in an acceleration of organisational innovation intensity. The model also suggests that small firms seeking higher degrees of innovation must fulfil the prerequisites for higher-order learning, that is, an entrepreneurial posture in decision-making, learning from both external and internal sources, and active unlearning.

The three learning capabilities, and the theoretical relationships between these capabilities and organisational innovation intensity have important implications for future research. Though there is a growing body of literature that addresses organisational learning, the relationship between different levels of learning and their antecedent conditions has not been fully explored, particularly in a small business context. Generally speaking, empirical research on organisational learning is limited and much of the evidence regarding the benefits and antecedents of organisational learning remains largely anecdotal (Slater & Narver, 1995). The relationships in the theoretical model and the proposed approach to conceptualising the organisational learning capabilities should guide empirical research and contribute to our understanding of small firm organisational learning.

Another important contribution of the conceptual model is the manner in which organisational innovation intensity is conceptualised. In a clear departure from the existing literature, which is biased towards product-based technological innovation, the model implies that innovation can occur in any of the firm's value-creation activities. All forms of innovation are potential sources of *SCA*. This approach encourages small firms to explore all paths to innovation including not only new products, but also new marketing methods, employee reward schemes, and new organisational structures.

With regard to *SCA*, the capability-based theory suggests that the inimitability of distinctive capabilities is a key source of sustainability (Grant 1991; Hayes et al.1996). An obvious implication stemming from this proposition is that small firm ownermanagers pursuing competitive strategy must invest in building and nurturing distinctive capabilities that will enable them to gain *SCA*. Again, the tacitness, complexity, and specificity of the capabilities possessed by the firm can produce causal ambiguity regarding the firm's actions, which in turn create barriers to imitation.

The proposed capability-based model of organisational innovation and *SCA* is aimed at examining the role of distinctive capabilities in small firm innovation-based competitive strategy. The model specifies the fewest necessary constructs, which exert the greatest relative impact on organisational innovation and SCA. Therefore, the model is sufficiently bounded and conforms to the guidelines suggested in the literature for the formulation of conceptual models in the social and business sciences (Keats & Bracker, 1988; Rumelt, 1984). By presenting theoretical propositions we facilitate the formulation of hypotheses that researchers might wish to explore. The model provides a novel formulation of the relationship between entrepreneurship and small firm competitive advantage. The model also adopts realistic approaches to operationalism the two constructs, reflects recent developments in the literature, and addresses the need for well-founded measures of the key constructs. Similarly, the approaches suggested operationalising the learning capability constructs make an important contribution to organisational learning theory, which currently lacks a strong empirical base. Though the literature on the capability-based theory of competitive advantage is growing in volume, most of the key theoretical constructs have not been operationalised nor have the central theoretical propositions been synthesised in a single framework. Particularly, the literature on small firm competitive strategy has not been fully explored in a small business context. The

framework presented in this paper provides researchers, a realistic research path to examine the small firm strategy formation activity. As noted earlier the research efforts in this research thrust has saturated to some extent due to its over-emphasis on strategic planning. The model captures the critical role of strategic decision-makers in the development and selection of firm strategies. Drawing attention to organisational innovation and the role strategists can play in this process is particularly important given the rapidly changing terrain of today's small firm competitive landscape.

14. References

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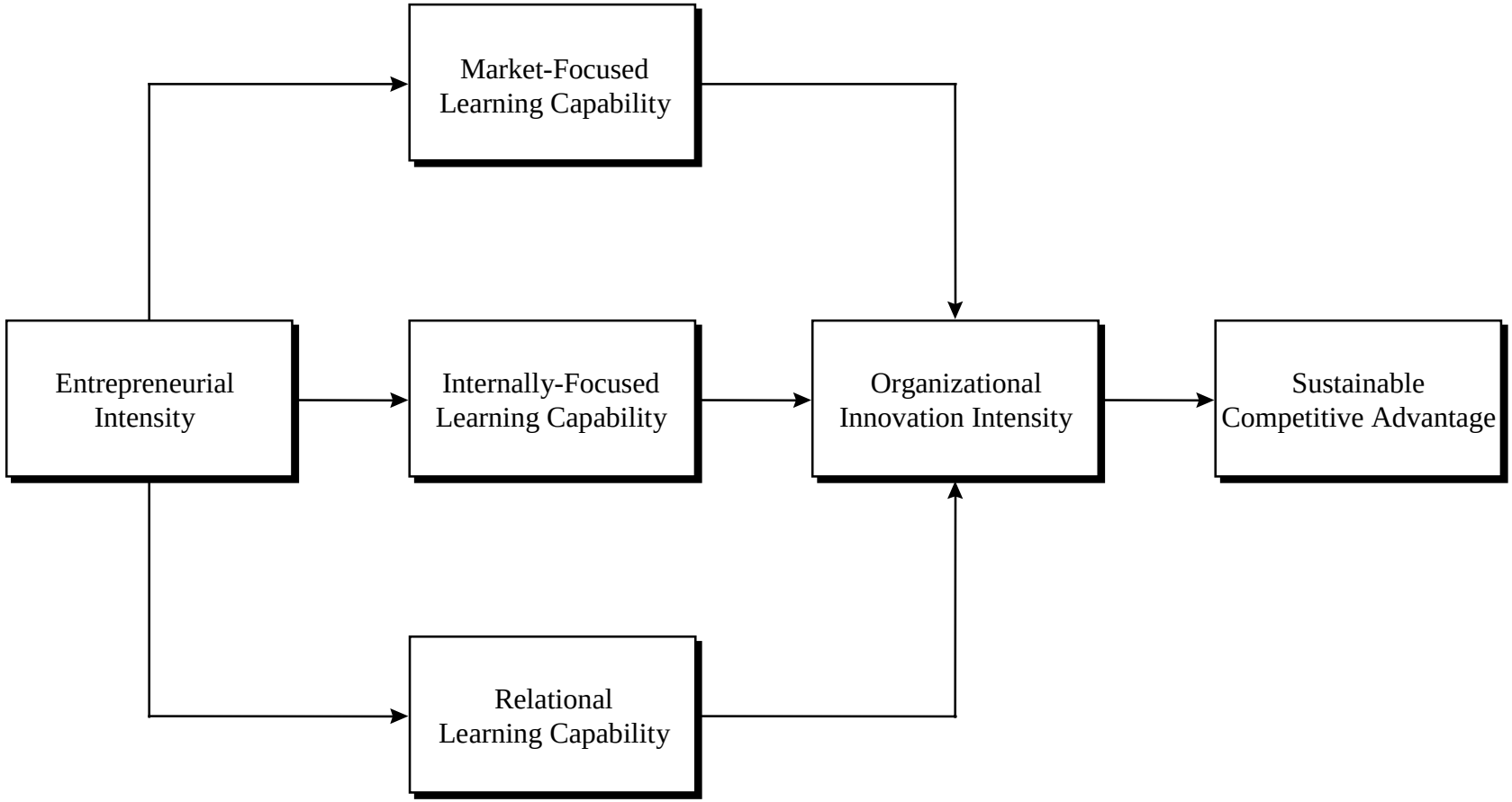
FIGURE 1

A Conceptual Model of Small Firm Organisational Innovation and Competitive Strategy



Structuring Family Business Succession

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ABSTRACT

This article examines the perception of potential family business leaders from a behavioral economics theory perspective. The findings suggest that high financial and behavioral sunk costs, as well as the requirement to 'earn' the right to lead the family business results in the future leader valuing the business more highly. Only financial sunk costs lowered the successor's proclivity to take risky action after acquiring the business. Therefore founders should structure succession so that the future leader incurs both financial and behavioral sunk costs as well as hold the future leader to stringent performance requirements prior to the succession.

INTRODUCTION

Family businesses are important to most capitalist economies. Eighty to ninety percent of all businesses in the US are family-dominated [17, 30] generating approximately half of all employment and half of the Gross Domestic Product [18, 43]. One issue that troubles family businesses is that of succession. Succession *is the process during which the business is transferred from one generation to the next*; it includes the dynamics preceding the actual transition as well as the aftermath of the transition.

The process of succession has implications for the various stakeholders of the business and represents a period of danger to the survival of the family business - - 70% of family businesses fail to survive through the second generation and 90% through the third generation [30]. These statistics on business failure do not necessarily indicate that succession is the cause of business failure or even whether these failure rates differ from those of non-family businesses. Despite incomplete statistical evidence that poorly managed succession can cause failure, common wisdom proposes that succession is a major issue to family businesses and is evidenced by the many studies that have investigated succession related issues.

The research into succession issues facing family businesses has investigated the development of formal succession plans [52]**;** the interpersonal relationships between family members [30,52] and issues of power and politics [24, 25]. Although scholars agree that a strong succession plan is best for a smooth transition, a number of factors can interfere. First and foremost, to initiate succession planning means to acknowledge one's own mortality [30]. This is not only difficult for the parent, but can cause conflict within the succeeding generation

as well. Thus, many people wish to avoid thinking about succession altogether. Therefore, succession is typically a process versus an event [25]. As the eventual heir takes on more responsibility, the founder relinquishes duties.

Choosing the appropriate successor from one's own children can be problematic [24,30]. Resentment, jockeying for position, overt and covert sabotage all hinders smooth succession. Handler [23] suggests that successful transition is a function of both mutual respect between generations and accommodation of respective roles among the second generation. A common underlying theme of these studies is the importance of creating a set of shared values in order to have a smooth and successful succession [19]. However, Handler [24] notes that there has been a general lack of investigation on how the second generation perceives the family business.

Given the emphasis on values and the need for research on perception it is surprising that researchers to date have not investigated succession from a more cognitive perspective. What effect does the structure of succession have on the important decisions that the new family business leader will make? For example, the second generation needs to address important decisions such as whether to harvest the investment in the business (sell the business) and/or whether to pursue a new strategic direction [11,13]. Such decisions reflect, in part, the new leader's perceived value of the family business and their attitude to risk (uncertainty).

In this article we make a contribution to the family business field by applying theory and practice from behavioral economics to explore the decision policies of future family business leaders and the factors that might alter their perceptions of ownership. Such an approach addresses Brockhaus' [10] concern that there is a lack of theories for hypothesis testing in family business research. We also focus on the future leader's perception of the family business they are about to take over.

Based on the behavioral economics literature, we argue that the way succession is structured will effect the next generation's perception of ownership. This leads to two related questions: (1) Does the manner in which family business successions are structured effect future leaders' perception of value of the business? and (2) Does the manner in which family business successions are structured effect future leaders' willingness to undertake risky activities?

The paper is structured as follows: First, the behavioral economics literature is reviewed (and contrasted with standard economic theory) and hypotheses are developed. Second, the research method used to test the hypotheses is described. Third, the results are detailed and discussed. Finally, the implications of this study's findings for researchers and practitioners are offered.

LITERATURE REVIEW

Standard economic theory proposes that ownership of an asset will not affect the valuation of that asset (assuming no information advantages). Consistent with this belief is the argument that a rational decision maker will not consider sunk costs in their future decisions [8]. However, there is substantial evidence that the ownership of an object can affect valuation [28,32] as can sunk costs [29,38,45]. The behavioral economics perspective of ownership arose out of this dissatisfaction with the assumptions of standard economic theory [47].

A robust finding from the behavioral economics literature is the endowment effect [28,49]. The endowment effect *refers to the propensity of people to value what they have more dearly than they would a corresponding opportunity to acquire the same good* [27]. For example, 89% of a sample (n=76) refused to exchange a coffee mug for a bar of chocolate of similar price. The students in the sample had been given the coffee mug before answering a long questionnaire, the purpose of which was simply to allow time to pass so as to make sure that the students accepted the gift as their own. Ninety percent of another group (n=87) refused to exchange the bar of chocolate (they had been given before compiling the questionnaire) for the mug [31]. People place a higher value on an object that they have owned.

The endowment effect can be thought of in terms of Prospect Theory [28,31]. Prospect theory argues that people perceive losses differently than gains - - people gain greater marginal disutility from a loss than the marginal utility from a gain of the same nominal value. Therefore, prospect theory provides an explanation for the endowment effect; namely, when a person already owns an object its loss has greater value than the ability to acquire the object prior to ownership for equal value.

If we apply the endowment effect to family business succession we would expect that once the successor owns and controls the family business they would value the business more than they did prior to ownership (a shift of values towards that of the previous family business leader). This represents an ‘instant endowment effect’. However, the new leader’s perceived value of the business is unlikely to be in line with the past leader as the endowment effect has been found to increase with the duration of ownership. In other words, the past leader who is handing over control of the family business is likely to place greater value on the business than is the new leader. While there is little that can be done in structuring the succession to accommodate this knowledge, the behavioral economics literature suggests that the relationship between ownership (endowment) and value is also moderated by: (a) the amount of sunk costs and (b) how the object was obtained. Each is now explored.

Sunk Costs

The economic perspective of the rational decision maker, discussed above, argues that only incremental costs and benefits should affect decisions about future events - -honoring sunk costs is irrational. The only instance where using sunk costs may be rational is when a party is a buyer and (s)he recognizes that the seller's sunk cost will impact the negotiations [16]. On the other hand, there are numerous examples where sunk costs are used irrationally [29,38,45]. The sunk cost effect is when people tend to let their decisions be influenced by costs made at an earlier time in such a way that they are more risk seeking than they would be had they not made these costs (explained by Prospect theory in Kahneman and Tverrsky [29] and by Zeelenberg and van Dijk [55]). Thaler [49] provides an example of how sunk costs affect decisions under uncertainty: "A family pays $40 for tickets to a baseball game to be played 60 miles from their home. On the day of the game there is a snowstorm. They decide to go anyway, but note in passing that had the tickets been given to them, they would have stayed home." They appear to believe that they have too much invested to quit [48]. Why does this happen?

It appears that sunk costs increase a person's aspiration level (aspiration level refers to the outcome we anticipate in accordance with our inputs [55]. It is argued that those that have invested sunk costs perceive those outcomes below the aspiration level as more negative. Zeelenberg and van Dijk [55] find that participants that have high sunk costs are more likely to choose the safe option. They propose this is due to an increased aspiration level (due to the investment of sunk costs) and therefore a choice between an option that satisfies the aspiration level under all circumstances to one that provides circumstances in which the aspiration level may not be met. In other words, sunk costs increase the aspiration level and this encourages people to be more uncertainty averse.

The above review of research from the behavioral economics literature suggests that sunk costs can be either financial or behavioral and both influence the assessment of value and risk. In the context of family business succession, financial sunk costs would include the "Buy In" costs – *the money the future leader had to invest into the family business in order to obtain management control*. For example, the son or daughter incurs buy in costs if he or she has to purchase equity in the company before he or she can take over. Behavioral sunk costs would include the "Time and Effort Invested" - - *the time the heir apparent had to invest into the family business in order to obtain management control*. For example, if the offspring had to work her way up the organization and spent time working for the organization over summer breaks from university, she would have invested significant time and effort. If, on the other hand, the offspring jumped immediately into a management

control position without "paying her dues," then she wouldn't have invested significant time and effort. The above discussion leads to the following hypotheses:

Hypothesis 1: *The higher the costs for the future leader to 'buy into' the family business the:* **(a)** *greater the perception of value and* **(b)** *lower the willingness to undertake risky activities.*

Hypothesis 2: *The higher the investment of 'time and effort' in the family business by the future leader the* **(a)** *greater the perception of value and* **(b)** *the lower the willingness to undertake risky activities.*

How the Business was Obtained

Previous research has shown that a person's attachment to an object depends on whether the object was obtained by their own efforts or attained by a chance outcome - - this phenomenon is referred to as source dependence [36]. For example, windfall gains are spent more readily than other types of assets, presumably because they are valued less [1]. The key feature of windfall gains *is that such gains are unearned*. The findings suggest that unearned gains are not perceived to be as valuable as earned gains and are therefore more readily spent (or gambled). Arkes et al. [1] conclude that in order to predict behavior towards risk (or gambling) it is not sufficient to only have the traditional components of normative choice (the probability of winning, the probability of losing, the amount for a win and the amount for a loss) but also the source of the funds put at risk. Mellers et al. [37] propose that these findings have implications for public policy - - policies that give homes away to lower income families may be less effective at improving neighborhoods than policies requiring families to purchase homes, even at extremely low prices.

In sum, an important aspect of source dependence is the perception that the object was obtained through the recipient's own actions [1]. In the family business context we investigate whether the future leader had to earn the right to take over management control of the family business. Earning this right could include performance requirements *which refers to the future leader's quality of output in specified areas and whether that output matched or exceeded certain acceptable levels or benchmarks in order to obtain management control (e.g., achieving good grades at business school).* The above discussion leads to our final hypothesis:

Hypothesis 3: *The higher the performance required to take over the family business the* **(a)** *greater the perception of value and* **(b)** *lower the willingness to undertake risky activities.*

In sum, borrowing from behavioral economics we make a first step towards understanding how to structure succession so that the future leader places greater value on the business and their attitude to risk is more conservative (to more closely coincide with that of the previous owner [e.g., parent]). We propose that the investment of financial sunk costs (H1), the investment of behavioral sunk costs (H2) and how ownership was

obtained (H3) all effect the future leader's perception of the business. We now describe the research method used to test these hypotheses, followed by the results and a discussion of these findings.

RESEARCH METHOD

Limitations of much of the previous family business research have included inadequate research designs and the absence of statistical techniques [10]. This study follows suggestions by Shepherd and Zacharakis [44] that cognitive theories can be investigated through a decision-making framework using conjoint analysis and experimental designs. Conjoint analysis *is a general term referring to a technique that requires respondents to make a series of judgments based on profiles from which their 'captured' decision processes can be decomposed into its underlying structure* (i.e., the attributes' significance in the judgment, how these attributes affect the judgment and the relative importance of each attribute in the decision process). A profile is simply a combination of all the attributes where each attribute is described by one of its levels (a level is an assigned value for an attribute).

Conjoint analysis and policy capturing have been used in hundreds of studies of judgment and decision making [21,46]. These studies vary from research into consumer purchase decisions [33], manager's strategic decisions [26,40] and expert judgment [14]. Therefore conjoint analysis represents a robust technique for decision modeling research providing structured insight into a future leader's decision policy. The research method is now detailed in terms of the sample used, the decision making task, the research instrument, and how the analysis will be conducted.

Sample

The sample for this study included people who represent the possible future leaders of a family business (i.e., of a business in which ownership and policy making are dominated by members of an "emotional kinship group" [see 12]). The sampling frame included people who considered themselves as part of a family business and were currently completing their final year of business education in one of two North American universities. Fifty-nine potential family business leaders participated in the study. Smaller sample sizes are acceptable for conjoint analysis and this sample size compares with other conjoint studies (e.g., Zacharakis and Meyer's [53] sample size of 53).

In the entrepreneurship literature there is skepticism in studies that utilize student samples. The use of students, in this study, however, is well justified. This research is positioned in the behavioral economics paradigm where the use of student samples is common [1,5,7,20,28,31,36,47,55].. Moreover, the research

question itself directs our attention toward the perceptions of potential family business leaders when faced with various succession structures.

How do these potential family business leaders differ from those not captured by the sample? The most obvious difference is that this sample is likely to be more educated than potential family business leaders in general since they are currently working towards a business degree. How would this affect the results? If anything, we would expect that business school educated people would be more likely to conform with standard economic theory - - think more 'rationally' about succession - - and therefore be less likely to provide support for this article's hypotheses. Thus, this sample can be considered a conservative test of the proposed hypotheses.

Decision-Making Tasks

There are two decision-making tasks. In the first decision making task respondents evaluated a series of hypothetical conjoint profiles which describe a succession path and market value of the business in terms of three attributes, each with two levels. Discussions with (potential) future leaders, family business managers and academics confirmed the face validity for both the attributes and their levels. Definitions of the attributes are provided in the literature review section above and the levels are now displayed.

(1) Buy in price **High**: *In order to obtain management control of the family business you had to use all your personal savings ($25,000) to buy some equity from your parents.* **Low**: *In order to obtain management control of the family business you did not have to buy any equity from your parents - - it was given to you.*

(2) Personal Involvement **High**: *Up until obtaining ownership and management control of the family business, you have worked in the business in your spare time, including weekends and summers during college.* **Low**: *Up until obtaining ownership and management control of the family business, you rarely worked in the business in your spare time.*

(3) Performance Requirements **High**: *In order to obtain management control of the family business you had to meet or exceed reasonable performance levels, these included good grades in school and an ability to effectively manage your personal income.* **Low:** *There were no performance levels that you had to achieved in order to obtain management control of the family business.*

(4) Market Value of the Business **Held Constant**: *Business valuers suggest that the prices they may be able to achieve if the business was sold today are: 20% chance of over 12 million; 40% chance 11-12 million; 40% chance of 10-11 million; and 20% chance of lower than 10 million. (The business has 9 million in debt).*

The potential family business leaders were asked to evaluate each scenario based on its description (i.e., the levels of attributes presented) and to assess the willingness to accept an offer, by a competitor, to purchase the business for $11.25 million. The offer and expected market values for the business remain constant across all profiles (i.e., the profiles only differ based on the attributes of the succession process).

In the second decision making task, the three attributes of the succession process (the buy in price, personal involvement and performance requirements) were again used but the constant "market value of the business" was replaced by the constant "current situation" - - current profits are $350,000 per year. In this task the future leaders were asked to evaluate each scenario based on its description (i.e., the levels of attributes presented) and to assess the willingness to accept a specific offer - - *You have the chance to be the first to purchase and use an innovative technology. If it works as expected, profits are likely to increase by 50% to $525,000. Although if it does not work as expected profits are likely to decrease by 50% to $185,000. There is a 50% chance that the technology will work as expected and a 50% chance that it will not work as expected.* The offer and current situation for the business remain constant across all profiles - - again the profiles only differ based on the attributes of the succession process.

For both decision making tasks the potential family business leaders were asked to indicate their willingness to accept an offer. Willingness to accept is a common operationalization used in studies of the endowment effect [25,28] and was measured on an 11 point scale anchored by "very low willingness to accept" to "very high willingness to accept".

Research Instrument

The research instrument contained a cover letter, task instructions, two conjoint decision making experiments and a post-experiment questionnaire that asked respondents to answer questions regarding characteristics of themselves and their family business. Once instructions were understood, respondents considered each profile and provided an indication of their willingness to accept the offer (whether it be the offer by a competitor to buy the business or the opportunity to purchase and use the innovative technology). For both conjoint experiments, a 2^3 fractional factorial design was used consisting of four profiles [22]. A fractional factorial design was used to reduce the number of profiles required to test the main effects (based on theory and a small pilot study there was no reason to test for interactions or non-linear relationships). The design was orthogonal ensuring no multicollinearity.

Each group of profiles (the four original profiles for decision task one, the four original decision profiles for decision task two, the four replicated profiles for decision task one and the four replicated profiles for

decision task two) was randomly assigned to avoid order effects. The order of profiles within each experiment was also varied to avoid order effects. A practice case was used and familiarized respondents with the task. Therefore, the experiment presented (potential) family business leaders with 17 profiles to evaluate. The experimental design enabled both individual subject level and aggregate subject level analyses.

ANALYSIS

Regression analysis is used to decompose a respondent's decisions in to their underlying structure. To identify attributes statistically significant at the aggregate level, the regression coefficient (B) for each attribute (derived from the individual-subject level of analysis) are averaged across individuals with the sign of the regression coefficient indicating the nature of the relationship [50]. The mean regression coefficients represent a model of the sample's decision making - - a constant and a regression coefficient for each of the independent variables. A Z-score was used to test for significance at the aggregate level. A Z-statistic *aggregates the t-statistics derived from the individual-subject analysis for that attribute in order to identify whether a particular attribute is significantly used by the sample* [15]. For example, a Z score for an independent variable that exceeds 1.645 indicates significance at $p < .05$.

The eight replicated profiles (from both task 1 and 2) were used in a test retest measure with the original eight profiles (from task 1 and 2) using Pearson R correlations to test the consistency of responses for each respondent. Although two or more attributes may significantly affect the decision process, it is unlikely that those attributes will be of equal importance. Therefore, the significance at the aggregate level of analysis is supplemented with a ranking of relative importance - - a comparison of the beta coefficients (Beta). Beta coefficients are the regression coefficients when all variables are expressed in standardized (Z-score) form. Transforming the independent variables to standardized form makes the coefficients more comparable since differences in the units of measurement are eliminated.

RESULTS

The study's findings provide support for 4 of 6 hypotheses. The findings provide evidence that people do use sunk costs and their decisions about an object depend on how that object was obtained. Specific to family business succession, future family business leaders value that business more when they have invested both financial and behavioral sunk costs and earned the right to take over the family business. The later attribute being of primary influence. Financial sunk costs also effect decision-makers in decisions involving risk. The results are now detailed.

Individual level Analyses

Analyses at the individual level reveals that twenty (34%) of the potential family business leaders were influenced by the investment of financial costs, 36% were influenced by the investment of behavioral costs and 48% by whether their position was earned by good performance. Three respondents produced incomplete responses and could not be included in the analysis. Of those that used financial costs in their assessment of the family business' value 67% were in the direction hypothesized - - the higher the financial sunk cost the higher the value. Thirty-three percent of those that used financial sunk costs did so in the opposite direction to that hypothesized - - the lower the financial sunk cost the higher the value. The findings were more consistent for behavioral sunk costs and 'earned by good performance' (only three respondents were significant in the opposite direction to that hypothesized). The perceived value of the business increased with higher behavioral sunk costs and by higher performance requirements. The mean test retest correlation on the 8 replicated profiles across all (potential) future family business leaders was .65. The mean explanatory ability for the models of valuation (R^2) was .736.

As for the second experiment (decision to invest in risky new technology) the mean test retest correlation on the 8 replicated profiles across all (potential) future family business leaders was .59. The mean explanatory ability for the models of risky decision (R^2) was .561. The results indicate that 25% of the respondents used financial costs, 21% used behavioral costs and 14% used whether the ownership was earned in their decision to pursue risky new technology. Seventy nine percent of those that used financial costs in their decision on the new technology demonstrated the sunk cost effect. For the other two variables only approximately half the significant responses were in the direction hypothesized (40% for behavioral sunk costs and 50% for earned performance). The aggregate results will now be reported.

Aggregate level Analyses

At the aggregate level, Table 1 indicates that all attributes had a significant effect ($Z>1.645$) on the decision making of the (potential) future family business leaders in their assessment of the value of the business. Whereas, only financial sunk costs were a significant effect on the proclivity of risky decisions. The mean regression coefficient for each significant main effect was positive. This indicates that (potential) future family business leaders when assessing value demonstrate the sunk cost effect (both financial and behavioral) and if their position must be earned then they also place a higher value on the business. Financial sunk costs also negatively affected the willingness to undertake a risky investment. The direction of these findings is consistent

with expectations and supports hypotheses 1(a), 1(b), 2(a) and 3(a). There was no support for hypotheses 2(b) and 3(b).

Table 1: Aggregate Results for Experiments 1 and 2

	Experiment 1: Value			**Experiment 2: Risky Investment**		
Attribute	**B**	**Beta**	**Z score**	**B**	**Beta**	**Z score**
Buy In	.209	.095	3.111**	.407	.124	3.539***
Involvement	.962	.271	7.004***	.000	-.003	0.218
Performance	.647	.204	7.023***	-.009	-.009	-0.657
Constant	5.436		6.333			

*** p<.01
** p<.05

While two or more attributes may significantly affect the decision process of future family business leaders, it is unlikely that those attributes will be of equal importance in their evaluative strategies. Therefore, the significance at the aggregate level of analysis is supplemented with a ranking of relative importance - - a comparison of the beta coefficients (Beta). This analysis of the relative importance of the attributes of family business succession demonstrates that behavioral sunk costs (beta .788) are more important in the future family business leaders' perception of value than is how the business was obtained (beta .204) and financial sunk costs (beta .095). The relative importance of these succession attributes is different for the decision on whether to undertake a risky activity - - where financial sunk costs was of primary importance and it appears that behavioral sunk costs (beta -.003) and how the business was obtained (beta -.009) were of minimal importance.

It must be noted that the use of a mean beta as an aggregate measure of relative importance may mask the importance of these succession attributes if the attribute is not used in the same way by respondents (i.e., we know from the individual level of analysis that behavioral sunk costs and how the business was obtained were significantly used in the decision of whether to undertake a risky activity although half the people used a attribute one way and the other half the opposite way). This will be investigated further in the discussion section below.

DISCUSSION

The present study provides insight into the decision making of future family business leaders. Behavioral economics literature was used to identify and predict the effect of sunk costs and how the object was obtained would influence the decisions of a family business leader. The results demonstrate that, consistent with findings in the behavioral economics literature, the decision making of these leaders is inconsistent with the assumptions of standard economic theory - - they are not 'rational'. They do consider sunk costs in their decisions about future events - - future events of selling the business and undertaking risky investments. For the

decision of selling the business, decision-makers demonstrate the sunk cost effect with financial sunk costs (investment of money) and behavioral sunk costs (investment of time and energy). This study, representing a 'real world' problem of family succession, supports recent laboratory research of Zeelenberg and van Dijk [55] on student willingness to take gambles after incurring behavioral sunk costs.

The article also investigated source dependence - - how the object was obtained affects the future leader's plans for the future. Again our findings support studies in behavioral economics and challenge the basic assumptions of standard economic theory. Future family business leaders indicate that their choices are not fungible. Fungible refers to the proposition that the source of money should make no difference in its consumption [51]. How they obtained the business influenced their assessment of value of the family business - - if they earned the right to run the business then they valued the business more. We have extended the recent research on source dependence by moving away from the laboratory involving small monetary or small gift gambles and into the context of family business succession where the stakes are high and we know findings can be of practical importance.

Other interesting findings in this study are those that did not provide support for the hypotheses. At the aggregate level there was no behavioral sunk cost effect for risky decisions nor did future family business leaders consider how the business was obtained when making risky decisions. As alluded to earlier, the aggregate level of analysis appears to be masking some interesting findings. If the magnitude of the t-statistics had been used to determine the aggregate Z statistic (signs were eliminated) then both attributes would have been significant (behavioral sunk costs with a Z score of 6.627; source dependence with a Z score of 6.251). Therefore, these attributes are significantly used, however for both attributes only approximately half of those that used the attribute did so in the way hypothesized (and the other half in the opposite direction).

What possible explanations are there for these findings? Maybe those that used the attribute in the opposite direction to that hypothesized did not understand the manipulation described in the experiment. This is unlikely as a pilot study indicated this understanding was present. Further, respondent's understood the same attribute for the other experiment (those relating to the dependent variable of willingness to sell the business) and it was used consistently. Another explanation is that people were affected differently by the manipulation of this attribute when faced with a decision under uncertainty.

The literature supports the direction hypothesized. What could explain behavioral sunk costs encouraging the decision maker to pursue the risky (uncertain) alternative? Maybe these decisions under uncertainty are influenced by expectations of regret - - choosing not to purchase the new technology only to later

find out that a competitor did and you are now at a competitive disadvantage. Feedback is one of the determinants of regret [3] and this feeling of regret can be anticipated and encourage risk taking behavior [3,35,42,54]. Baron [2] finds that entrepreneurs are more likely to feel regret over things they did not do than things they did (even if those actions did not work out well).

Risk taking behavior may be encouraged as the utility gained from the 'right' decision is less than the regret of following the 'wrong' one [4,7,34,54]. Zeelenberg and Van Dijk [55] argue that people feel there is more at stake when they have invested sunk costs and when feedback is present - - choosing the safe option will be more painful if it is wrong and therefore they will opt for the risky option (pg. 684). There is clearly a need for more research into the effect of behavioral sunk costs on risky decisions when outcome feedback is likely.

Why would the future family business leader, who has earned the right to lead the company choose a more risky alternative? Family businesses might represent a unique situation where the self is wider than just the individual and this could, in part, help explain the above finding (finding of support for the opposite direction to that hypothesized). When the leadership was not earned but given to the family rather than seeing it as a windfall gain the family business leader may believe their obligation to the family has increased. This obligation may be so strong that the new leader feels constrained. Whereas if they have been required to earn the right to make these decisions the obligations to others is less even to the extent that they believe they have earned the right to make risky decisions and put their stamp on the strategic direction of the organization. They still value the business higher when they have earned the right but feel it is theirs to risk.

Potential Limitations

Conjoint analysis was the research method used to investigate the decision making of potential family business leaders under various succession structures. Conjoint analysis, as with all techniques, has its own limitations. Throughout the design and administration of this study, attempts were made to minimize these limitations. First, reliance on hypothetical succession structures may reduce the external validity of the study compared to if the study used 'real' successions and 'real' decisions about the future (i.e., real offers to buy the business and/or real decisions under uncertainty involving, for example, the adoption of new technology). There is evidence however, that hypothetical representations are useful for capturing real policies [9,39,41]. Conjoint analysis has demonstrated external validity.

A further limitation of the study may be that providing dichotomous attributes may eliminate perceptual requirements from the task, thereby placing less emphasis on judges' ability to extract attribute information. While this criticism of conjoint analysis has merit and does represent a limitation of the technique, the inclusion

of attributes that are both theoretically justified and have face validity when pilot tested mitigate any negative impact they might have. Further, this study's use of conjoint analysis offers a complementary research method to the simple experiments used in behavioral economic research to date.

As discussed above with the description of the sample, there may be questions regarding the generalizability of the findings beyond the sample, namely, beyond business graduates who are potential family business leaders. We would expect that business graduates would be trained to think 'rationally' and therefore less likely than the wider population of future business leaders to demonstrate the sunk cost effect and source dependence. Given the strength of the findings, especially under the preceding assumption, care still must be taken in generalizing these results beyond the business graduate population. It is expected that business graduates still represent a sizable and significant portion of those people who become family business leaders, therefore even if the results are only generalizable to the business graduate population a contribution to the literature has been made.

CONCLUSION

The practical implications of this research is on the way that a current business leader may structure the succession so that the new leader will more highly value the business and may be more risk averse (likely attributes of the current leader and ones that (s)he would value in the new leader). To this ends the findings of this research suggest that the succession should be planned so as to encourage the future leader to invest financial and behavioral resources. As operationalized in this study's experiment this could represent a dollar amount to represent a 'buy into' the business and time and effort invested in the business prior to succession.

Succession planning should also consider this study's finding that if the leader was forced to earn their new position they will value the business more. However, we must be aware that the investment of behavioral sunk costs and an earned position as leader for a number of people may increase the likelihood of choosing a risky decision. This represents a fruitful line for future research - - an empirical investigation of why some people prefer a risky (uncertain) situation? As discussed earlier, such research should also investigate the possibly moderating role of feedback and also feelings of commitment to ones family under varying levels of sunk costs and how the business was obtained. Another important question is whether there are other factors that influence the perception of business value or affect decisions under uncertainty? We know duration of ownership is important? Is it possible to plan succession so that the future leader feels part of ownership prior to succession? The success of family business succession depends on the values of the future business leader (and

the current/past leader). There is much research to be done in understanding these relationships and the ‘best’ structure for succession.

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Organisation of Successions of Small and Medium Sized Enterprises within the Family

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Abstract

The succession of a small or medium sized company creates a life long dilemma for an entrepreneur! Who would like to be reminded of his or her death by the children's claim on the family company? Still, we know that the best way to enhance an accumulation of the value of the enterprise normally, due to family idiosyncrasy etc., is to make sure that the ownership remains within the family. Due to other considerations formal rules tend to hamper the possibilities to make transfers within the family simple. How to plan and organise transfers of ownership of SMEs within the family during the lifetime of the owner has, therefore, become a very complicated matter. These difficulties are described and analysed in the paper, especially in relation to the Swedish law system and the practical options that are available to a Swedish entrepreneur. Furthermore, some suggestions are given about how to enhance successions of SMEs within the family facing a new millennium.

1. Introduction

In most countries a majority of the firms are not listed on a stock exchange. Many of these non-listed firms are family-owned and there are plans for the children in the future to take over the ownership, and perhaps also the management. Furthermore, some of these firms have already been family-owned for more than one generation. That firms stay within the family for generations have not received much attention in economics literature. There seems to be a lack of theoretical explanations as to why a succession of firms to heirs would be rational. There is also a lack of case studies that can guide us in the quest for a theory of intergenerational family successions.

Two main questions are addressed in this paper. The first question is: Are there any reasons why firm value would be positively affected by succession instead of the sale of a family firm to new non-family owners"? A transaction-approach will be used to show why there might be such efficiency reasons for intergenerational successions of firms. This approach will also be used in a discussion of how well the Swedish inheritance and tax laws are adopted to foster efficiency reasons for succession within the family. In the second question it is assumed that there are efficiency reasons (for society) for a succession within the family. What are then the succession options available for keeping the firm within the family?

In order to achieve these objectives the study is structured so that it begins in Section 2 with the statistics and lack of statistics about succession of firms in Europe and the policy recommendation of the European Commission. Section 3 presents a transaction cost approach to the problem of succession. The inheritance law and tax system that provide the institutional framework for succession in Sweden are described in Section 4. The question about options available for a planned succession is addressed in Section 5. The paper ends with a discussion of what lessons that can be learned from the study in Section 6.

2. An European background

In 1992 there were around 16 million active enterprises in the non-agricultural market sectors of the European Union and 99.8 % of these enterprises were SMEs employing fewer than 250 people. The share of SMEs of total employment was almost 70 %.[1] SMEs have thus the biggest potential in creating new jobs.

A study from the United Kingdom showed that only 24 % of family business were transferred to the second generation and that merely14 % survive to the third generation.[2] Of all petitions for bankruptcy in the Community an estimated 10 % are filed as a result of badly managed successions. These threaten at least 30,000 enterprises and 300,000 jobs every year.[3] It has

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[1] European Commission, Enterprises in Europe 1996 pp 8 and 26-27 and European Commission, Communication, Background to 94/C 400/01 p 2. Compare The European Observatory for SMEs 1996 pp 183-193.

[2] The study was carried out in 1989 by Stoy Hayward Consulting in association with the London Business School and is referred to in European Commission, Communication, Background to 94/C 400/01 p 2. For references to other studies confirming the result, see Handler 1994 pp 147-148.

[3] European Commission, Communication 94/C 400/01 p 1.

been estimated that about 6.3 million jobs in Europe are threatened in the near future because of poor preparations for the transmission of businesses.[4]

On the other hand, research results seem to show that if a business survives to the second generation the probability that it will also survive the following successions increases substantially.[5] Of the fewer than one third of the family businesses that survived the transition to the second generation, approximately 50 % survived from the second to the third generation and more than 70 % of these firms were passed on to the fourth generation. The increasing degree of survival can, among other reasons, be due to the experiences from earlier rounds of successions, which shows, that it is beneficial to have the next generation working in the company and that a succession should be initiated, planned and carried through in due time.[6]

Studies within the Community show that a majority of the entrepreneurs has not taken the necessary steps to plan and carry out coming successions. As an example, a study of 35 family businesses in England shows that only about 25 % had chosen a successor to the present CEO.[7] Around one third of the owners of small companies are over fifty years of age.[8]
It therefore seems urgent to find measures to make successions more efficient.

It seems remarkable that successions are not planned in due time since many studies show that most entrepreneurs wish the ownership and management of the family business to remain in the family.[9] This is further emphasised by the fact that succession of a family company, fully implemented, can demand three to five years.[10] A shift in generation of owners and management has to be initiated, planned and executed, and it often necessitates a change in company culture. This all requires time.

The unwillingness or incapability to initiate and plan the inevitable succession of the family business can be a result of the entrepreneur being too busy running and controlling the firm.[11] Also fears of losing a central role in the family can result in an owner postponing the unavoidable.[12] He or she can further develop excuses of various kinds, more or less connected to feelings of rivalry and jealousy, and so on, towards potential successors, to avoid retiring.[13] Yet another reason for postponing the succession is that an entrepreneur associates retirement with his or her own mortality.[14] Though succession of ownership can be mainly a question of incentive from the owner, it seems clear, since most entrepreneurs do not carry it out in due time, that other factors, such as those mentioned, are dominating.

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[4] The European Observatory for SMEs 1996 p 186.
[5] Greenwald 1993 and 1994 (Reference in Schulze and Dino 1996 pp 191 and 206.)
[6] See further Schulze and Dino 1996 pp 187-207.
[7] Kirby and Lee 1996 pp 75-85. For further examples, see references in The European Observatory for SMEs 1996 pp 184-185 and European Commission, Communication, Background to 94/C 400/01 p 3.
[8] The European Observatory for SMEs 1996 pp 184 -185.
[9] Kirby and Lee 1996 pp 75-85. For further examples of studies, se The European Observatory for SMEs 1996 p 187. Compare The European Forum on the Transfer of Business 24/3/97 pp 6-7.
[10] Compare Deegan 1986 pp19-23.
[11] Poe 1980 pp 23-27.
[12] Lansberg 1991 p 103.
[13] Jacobs 1986 p 26.
[14] See Poe, Lansberg and Jacobs in previous footnotes. Compare Seymour 1993 p 267. For several more examples in research of reasons for entrepreneurs to resist handing over the ownership and the management of the family firm, see Handler 1994 pp 137-139 and 144-147.

One study of SMEs shows that an average of 25 % of EU-enterprises expect a change in owner-structure within 3-5 years. Another 15 % expect a change after six years or more.[15] Of these companies 32 % are expected to be sold to a third party and 24 % to be handed over to the next generation of family members. Intergenerational succession of the family company in Sweden is expected to occur in 24 % of the cases, while the same figure for Germany is 60 %. A staggering difference, to which we today have no conclusive explanation.

To what extent then are family members ready to take over the business? One study, among university students in different countries, shows a relatively low degree of willingness to take part in the family business.[16] Most (66 %) expressed a less than 50 % possibility that they will join the company. Among the European participants 75 % of the males and 50 % of the females expressed less than 50 % chance that they would take part in the family business. Most of those that wished to join the company wanted to become president/CEO or manager. Participators that did not want to take part in the company gave many reasons. One of the most important was that they wanted to start their own businesses. Also other studies show approximately the same lack of interest among children to join their parent´s business.[17]

Research on transfer of ownership in companies seems to show that there are four main problems that hamper an efficient change of ownership. The first difficulty is the valuation of the enterprise. Secondly financing the take-over can be a bottleneck. The legal dispositions are the third problem. Taking account of different legal arrangements, e.g. inheritance, company and taxation law, is crucial when preparing a transmission. Last, but not least, the personal and emotional aspects can give rise to various difficulties.[18] This paper deals mainly with succession of a family company during the lifetime of the owner or, more specifically, the main legal dispositions used in Sweden as methods for handing over the ownership of a business to a new generation.

The European Commission regards only being aware of the main problems concerning succession as insufficient. It recommends a number of solutions in the legal and fiscal field. In 1994 the Commission issued a non-binding recommendation, since the member states have very varying legal and other conditions of importance for transfer of enterprises.[19] The recommendation contains 10 articles. A few of them are briefly dealt with in the following:

Businessmen should be provided with appropriate instruments which will allow the best preparation of transfer. To this end, the Commission requests the Member States (art. 4):

a) ”independently of the obligations stemming from Community law, (to) apply the principle of fiscal neutrality to operations for the preparation of transfers such as transfers of assets, mergers, divisions and exchanges of shares; the principle of fiscal neutrality shall also apply to stamp duties, registration fees and other similar taxes.”

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[15] Grant Thornton International Business Strategies Ltd 1996.
[16] Stavrou and Winslow 1996 pp 253-273. See also Stavrou 1996.
[17] Referred in The European Observatory for SMEs 1996 p 187. See also Handler 1994 pp 140-143.
[18] See further in The European Observatory for SMEs 1996 pp 188-189.
[19] European Commission, recommendation 1994 O.J.n L 385. Compare European Commission, Communication 94/C 400/01 p 2. Compare also The European Observatory for SMEs, 1996 pp 189-193 and The European Forum on the Transfer of Business (24.3.1997) pp 1-7.

The survival of the enterprise within a family should be ensured through appropriate fiscal treatment of succession and gifts. Member states are invited to (art. 6):

b) ”reduce the taxes on assets exclusively used for the business in the case of transfer by gift or succession, including inheritance tax, gift tax and registration fees, provided that the business is genuinely kept as a going concern for a minimum period;

c) ”offer the heirs the possibility of spreading or deferring payment of the gift or inheritance taxes, provided that they keep the business as a going concern, and shall grant interest exemptions;”

d) ”ensure that the tax assessment of the business can take account of how the value of the business changes some months after the death of the owner.”

When a transfer cannot be made in a family, the businessman should be encouraged to consider a transfer before death to third parties. Member states are invited to:

e) “ waive taxation on at least part of the revenue from the added value or capital gains arising on the assets of a business in the event of sale, in particular when the businessman has reached the age of 55; provide tax incentives for the reinvestment of the profits made on the sale of a business in another enterprise not quoted on the stock exchange and actively engaged in the production or sale of goods and services: “

The recommendation reflects the previously mentioned problems concerning transfer of ownership in companies. An evaluation has been made concerning which steps that have been taken by the Members in accordance with the recommendation. Some improvements have been made, e.g. measures taken aiming to reduce inheritance and gift taxes.

The studies mentioned above and the EU-recommendation raise many questions. Why do more entrepreneurs not carry through a succession during their lifetime and why does not a qualified majority of children wish to take over their parents businesses? How do we explain the variation between the disposition of entrepreneurs in different countries to hand over the company? Why does each country not make the various ways of carrying through a succession as easy as possible, e.g. concerning legal dispositions and financing take-overs?

As far as we know, there are, today, no coherent theories that can guide us. This third paper is a continuation on a journey which we hope will lead to a new theory that can connect and explain the disposition of the older generation to hand over the family business, and the propensity of the younger generation to take over.

3. A transaction cost approach to succession

In all family firms the problem of succession has to be faced at some point. When that time comes, the decision to let a younger generation of family members take over or sell to new non-family owners has to be made. A lot of different factors of a pecuniary and non-pecuniary

character may be influential in the choice between these two alternatives. Let us make the assumption that intrafamily successions are voluntary transactions (i.e. no coercion). Welfare would then be increased if obstacles to such transactions are removed. The obstacles focused upon in subsequent sections of this paper are the inheritance laws and the tax system.

To simplify matters we will here make the assumption that the objective in a succession decision is to maximise wealth. Decision factors of a more sentimental character will thus be disregarded. The decision problem in successions then boils down to a question of under which circumstances is it likely that the present value of a firm is higher in a succession of a firm to heirs than what can be received in a sale to non-family owners.

In answer to this question an explanation must be provided of how firm value can be fostered by a succession within the family. The analysis of the problem has both a macro and a micro dimension. At a macro level, norms, laws (tax laws etc) and regulations which constitute the institutional framework, within which succession transactions take place are considered.[20] The institutional framework will differ between countries and regions. This macro aspect of the succession problem will be shortly addressed in the end of this section.[21] We start the analysis with the assumption of a given institutional framework. In other words, there is a focus on the micro aspects of the succession problem.

In a micro-explanation two key elements are knowledge idiosyncrasy of a family character and uncertainty/complexity. These are two factors of a transaction environmental character that are likely to be decisive in the choice of succession mode.[22] Special attention will be paid to knowledge idiosyncrasy as the central explanatory variable. Knowledge idiosyncrasy possessed by a family member is claimed to be the basic reason for succession within the family to be a wealth maximising strategy.

Family idiosyncratic knowledge is acquired in a learning by watching and doing fashion. Growing up with the owner entrepreneur of a family firm gives an inside position that may give specific knowledge of how to run the firm in a profitable way. In many trades of a more craftsmanship character this knowledge is, to a large extent, tacit. It is acquired over time by observing and listening to the older generation and by practising what thereby has been learned.[23] The younger generation is in a unique position to acquire such idiosyncratic knowledge. They spend 24 hours each day with parents- entrepreneurs. They see them at work and listen to the discussions of the firm's problems within the family circle. The discussion in

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[20] See Davis & North (1971) and North (1990).

[21] See Section 4 for more about this aspect.

[22] Williamson (1975) lists different human and environmental factors that are decisive in choice of transactional mode. The bounded rationality of the human being and the complexity /uncertainty of the environment are two primary sources of transactional problems in contractual relations. Because of bounded rationality complexity/uncertainty is important in analysis of transaction costs. Williamson pays special attention to the case where bounded rationality are paired with bilateral dependency (lack of competition). (Knowledge idiosyncrasy of the type here described is one reason for bilateral dependency.) Uncertainty/complexity and bounded rationality give rise to situations with asymmetrical distribution of information about exchange conditions. Bilateral dependency invites in such situations to opportunistic behaviour in arm's length transactions and make them costly. Succession of a family firm to heirs is not an arm's length transaction. The family ties are likely to weaken the incentives for opportunistic behaviour.

[23] See Polanyi (1962).

such an environment is likely to be more candid than in other circles. The family members can trust each other and are more likely to reveal secrets to a larger extent.

Illustrations of how the learning by watching and doing take place are provided in the management literature. The process character of succession from one generation to another is stressed. Reviews of this literature can be found in Dyer and Handler (1994) and Brunåker (1996). Both these overviews depict a similar pattern with a gradually increasing involvement of the family member in a process that if it is planned ends with the next generation family member being the decision-maker and the predecessor the consultant. In an unintentional succession due to the predecessor's death the process will, of course, be more abrupt.

Among the reviewed studies Longenecker and Schoen (1978) can serve as an illustration of how idiosyncratic knowledge is acquired. The different stages in a father-son succession are described. Before being the manager and finally de facto leader of the family firm the successive stages of learning are characterised by terms as "aware of some facts of business, exposed to family members´ jargon, works part time in business, works full time in business with non managerial jobs" (Longenecker and Schoen 1978, p. 4). In Handler (1989) these stages of successive learning are characterised by terms as "No Role, Helper, Manager and Leader"

An historical study of how family succession in an American textile company, the Doak Company, was planned through education and business experience is provided by Scranton (1986). Besides a detailed description of how the heir in question was trained in education and practice, Scranton also makes a remark about the fact that the gradual involvement of offspring in the family business does not have to result in succession. "Fathers could evaluate their sons´ prowess and potential, their effectiveness and aptitude for directing the firm. In the worst case, a decision to "sell out" might be reached as an alternative to certain ruin of the business by an inept successor" (p.61). In other words "sell out" could be chosen if succession within the family despite acquired idiosyncratic knowledge, did not turn out to be a wealth-maximising strategy.

There is also an idiosyncratic knowledge of a network character that is likely to be acquired by growing up within a family business that will be further developed in the next section. The argument is that good personal relations with a well functioning business network can be inherited since customers, supplier and businessmen within the same trade tend to know all the members of the family and learn also to trust the family members through these encounters.[24] It is also to be expected that offspring will be concerned about not tarnishing the reputation of the parents. Consequently, the new generation can, in many cases, start their work in an environment of trust that facilitates business transactions in a way that is not immediately available to others.[25]

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[24] The remarks made by Marshall (1898) in his discussion of localised industries are apposite. Marshall writes: "When an industry has thus chosen a locality for itself, it is likely to stay there long: so great are the advantages with people following the same skilled trade get from near neighbourhood to one another. The mysteries of the trade become no mysteries; but are as it were in the air, and children learn many of them unconsciously." (Ch. X, § 3).

[25] The trustworthiness of sons and daughters is a reflection of the advantages of family governance of activities compared to other forms of governance. According to Pollak (1985) these advantages "can be grouped into the four categories: incentives, monitoring, altruism, and loyalty." Incentives for behaving trustworthily are fostered by consideration of both the family honour and concern for coming generations. Monitoring is facilitated by the

In the choice between letting the new generation take over or "sell out" there is an incentive problem of a principal-agent character that must be addressed. This incentive problem is of special importance if there is idiosyncratic knowledge that is possessed by only family members. In such a case, the only way to take advantage of benefits from idiosyncratic knowledge is to have the firm managed by a member of the original entrepreneurial family. The two alternatives of interest will be (1) a succession to the firm of a family member or (2) an arrangement where the firm is sold to an outsider with a son/daughter remaining in the firm as a salaried manager. The succession problem in the choice between these two alternatives boils down to a question of the incentive effects of a separation of ownership and control. Will the value of the firm be affected by the son/daughter being just a salaried manager instead of both owner and manager?

The classic article by Jensen and Meckling (1976) provides an answer. The manager will behave differently as a salaried manager (agent of the new non-family owners) than in the roles of sole owner and manager combined. As an agent he/she will be less interested in running the firm in a value increasing fashion. Opportunistic behaviour expressed by using the resources of the firm to one's own private advantage will be more interesting as the costs of such consumption on the job will be shared with the new outside owners. The more complexity and uncertainty about future events that characterise the operations of the firm, the more leeway for opportunistic behaviour of this sort there will be and the more negatively firm value will be affected by a change of ownership to outsiders. This fact reinforces the argument that idiosyncratic knowledge of family members is likely to be a very important reason for succession of firms within the family.

However, even if sons and daughters might be in a superior position of acquiring idiosyncratic knowledge about how to run the business successfully and have a unique access to important network relations within the business society, it is not certain that their capacities, aptitudes and talents will match these advantages. The best man/woman as a leader of the firm may have to be found outside the family circle because of a lack of these virtues. In such an instance, sale of the firm will be more attractive than succession of the younger generation.

The complexity of certain types of business and the uncertainty about the future often mean that there is an asymmetry in the information available to the different parties in a transaction. The presence of asymmetric information about the firm value (represented by the present value of the expected cash flows from the assets of the firm) is a factor of special importance for the succession decision of family firms. The present owners are likely to have superior information about how large these cash flows can be expected to be. A family firm is in general not listed on a stock exchange. Consequently, there is up to the time of succession no outside estimation of cash flows and firm value. The information gap between outsider and the insiders, the family owners, is therefore wider than in other cases.

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intertwining of economic and personal relationships. Altruism make the family members less opportunistic vis à vis each other. Furthermore, a sense of loyalty for the other family members makes family reputation very important and thereby curbs opportunism (see following section).

In sales to outsiders an Ackerlof type of 'lemon problem' has to be solved.[26] When the information gap between insiders and outsiders is wide the transaction costs of transmitting information about the firm value will, in some cases, be so large that it is impossible to get a fair price for a family firm with respect to present value of expected cash flows. As a result there will be no functioning market for sales of family firms. In some cases, it might only be possible to receive the liquidation value in a sale.

In an explanation of how institutional environment and idiosyncratic knowledge in succession matters, two aspects of the institutional environment are thereby of special importance. Firstly, the institutional environment at the local level in form of rules for human conduct can be of a type that makes idiosyncratic knowledge a very important factor in achieving competitive advantages. Secondly, the institutional environment on a larger jurisdictional level as the state/federal/country level can be of a kind that either foster, prevent or not affect the spontaneous emergence of the above mentioned rules of conduct at a local level favourable to family succession.

Before going into a discussion on these two aspects, what is meant by an institutional environment or an institutional framework first has first to be defined.[27] The institutional framework (the institutional environment) can be defined as "constitutions, statutes, regulations, norms, enforcement, and sanctions" that "constrains and directs" economic actors (Eggertson 1996, p. 8.).[28] In other words, the institutional environment, or framework, consists of both formal rules in the nature of different kinds of laws, and informal rules in the nature of norms. It is also to be noted that "the institutional framework defines and limits the set of practicable forms of economic organisation available to actors" (Eggertson 1996, p 10).[29]

Let us now look at the impact of the formal rules on intergenerational idiosyncratic knowledge. The formal rules constraining economic behaviour can serve as complements that promote the efficiency of informal rules or have the opposite effect of weakening and changing informal rules (North 1990, Ch 6). Laws, regulations and taxes are examples of formal rules. These rules are, to a large extent, determined by political decisions in jurisdictions encompassing the whole country or regions of differing size. The outcome of the political process through which the formal rules are decided and implemented is of relevance in deciding means of succession in family firms. Taxes, inheritance laws and business policy in general can make intergenerational succession unattractive in spite of the network and other idiosyncratic knowledge advantages of continuing to run the firm with unchanged family ownership. Some observations of how Swedish laws can be expected to influence the succession decision is the subject of the next section.

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[26] Ackerlof (1970).

[27] The concepts institutional environment and institutional framework are used as synonyms.

[28] A first definition is offered in Davis & North (1971, pp. 6-7).

[29] A comparison can be made with Williamson´s concept atmosphere which " is intended to make allowance for attitudinal interactions and the systems consequences that are associated therewith " (Williamson 1975, p.37) Williamson depicts graphical atmosphere as a as a circle within which transactions are embedded. It does not seem too far-fetched to replace atmosphere with the concept institutional framework.

4. The Swedish inheritance law and tax system

When an unmarried entrepreneur dies intestate, the estate is inherited by the children, or in the case of their death, by the grandchildren. If the entrepreneur has no descendants the parents or, if one of them is dead, the siblings or, if any of them is deceased, the nephews and nieces will inherit the estate.

The total inheritance consists of the net fortune, including the value of the shares in the family firm, less inheritance tax. The total value and the property is distributed among the heirs according to agreement or, if they cannot agree, in accordance with the Inheritance Act.[30] If the heirs cannot agree, e.g. on distribution of the property, a court can appoint a person to divide the property.

If the deceased was married, the first step is a division of the matrimonial property. According to the main rule the surviving spouse takes half of the total net value of the common property, including the shares in the family firm. The property is distributed according to agreement between the surviving spouse and the heirs. The latter has a right of priority to the property which was owned by the deceased spouse, e.g. the family company. If they cannot agree, a court can appoint a person to distribute the property.

According to the main inheritance rule, the surviving spouse inherits all the estate (after division of the matrimonial property), if the deceased spouse left no will. The children born into the relationship inherit from their deceased parent only after the death of the remaining parent, if the latter does not waive his or her right to inherit. Children of the first deceased spouse, that are not children of the surviving spouse, have, however, priority. They inherit their share from their biological parent, thus partially excluding the right to the inheritance for the surviving spouse (step parent).

The first deceased spouse could have made a will totally disinheriting the surviving spouse. For small estates there is, however, one exception, which is of no importance for this paper. He or she cannot make a will totally disinheriting the descendants. A child can always claim his or her lawful portion, which is half of what the child would have inherited without the will.

There is no inheritance tax on the surviving spouse´s share of the matrimonial property. The remaining property (the estate of the deceased spouse) is in most cases fictitiously distributed by a court according to the Inheritance Act and the inheritance tax is calculated on each share. A basic amount can be inherited without tax. For a surviving spouse 280,000 SKr (around 31,000 Euro) and for a descendant 70,000 SKr (approximately 8,000 Euro).

The property in an estate is valued according to certain rules in the Inheritance Taxation Act. Shares in small and medium-sized family-owned and unlisted companies are mostly valued in accordance with a certain method (”substance value method”), aiming to reach a market value, and the result is reduced to 30%. This is done in order to facilitate succession of these firms.

[30] For a comparison between estate laws in the US, Finland, Chile and Taiwan, see Davies, Swartz, Blakely, Chang, Eyzaguierre, Mattsson and Pettker 1996.

A life insurance that is paid out in a lump sum upon the death of the entrepreneur is regarded as an inheritance. A designated beneficiary can without taxation inherit a relatively high amount.[31]

Example: The man A is married to X. They have three children B, C and D. A has also a son E from a previous relationship. A is an entrepreneur and sole owner of a company with a ”substance value” of 24 million SKr (around 2.7 million Euro). The total matrimonial property has an estimated value of 8 million SKr. A dies intestate. The first step is to divide the matrimonial property, including the company. X´s share amounts to (24+8):2=16 million SKr. The other half becomes the value of the estate of the deceased A, which will be the subject of inheritance. If X wishes to have her whole share and if she first takes the total matrimonial property, she will, as a result of the division of that property, have a claim on shares in the company up to a value of 8 million SKr. Further she can, due to inheritance, claim shares up to a value of (16:4x3=) 12 million SKr. If the children (B, C and D) want to continue the business as the only owners they will have to compensate X with money. Further, E has a right to inherit from A before X. E´s share amounts to 16:4= 4 million SKr. To buy him out will be costly for B,C and D. All together they will have to pay 8+4= 12 millon SKr, if X waives her right of inheritance (12 MSKr). Their only reasonable chance (if any) to take over the company is thus to convince X to waive her right to inherit from A.

5. Options for succession of the family business during the life time of the owner

If the optional rules governing the result when the owner dies without having planned and carried out a succession are not acceptable, the owner and the family will have to initiate a succession process. If the owner is not willing to reveal who is going to take over the business, he can make a will. The substance value method is used for the valuation of the shares and the result is lowered to 30 per cent. The taxation will thus be the same as in the case of intestate succession. A will could also be seen as a way of waiting with the succession, which gives raise to certain problems, as we have demonstrated in a previous paper.[32]

If the owner is willing to reveal who is going to be the new owner, let us say B, he has several options: A gift of the shares to somebody in the next generation will be taxed the same way as on testate or intestate succession. However three legal conditions have to be fullfilled to gain a lower taxation: All the shares have to be given at the same time and without conditions. Further, B has to keep the ownership (a majority) of the shares at least for five years. The conditions are supposed to hamper tax planning. There is thus a fiscal neutrality when it concerns handovers through a gift, a will and on intestate succession, however with some conditions in case of a gift. Other methods of carrying through a succession do not show any fiscal neutrality.

With tax neutrality we refer to the idea, or principle, that similar transactions should be taxed the same way or, if it is not possible, that the tax amount should be equivalently high. In other words, that individuals should not be encouraged by tax rules to choose one method of carrying through a

[31] A sum of six times the social insurance base amount is exempt from inheritance tax (in 1999 approximately 220,000 SKr; around 26,000 Euro).

[32] A Game-Theoretic Approach to Strategic Decision Making in Intergenerational Successions of Small and Medium Sized Enterprises. ICSB World Conference Naples, Italy 20-23 June 1999.

succession.

A sale from the father A, of all the shares in the family company X Ltd, to somebody in the next generation, say the daughter B, will normally be done at a price lower than market value. The same goes if the shares in X are sold to a company, Y Ltd, owned by B. If the shares are sold to the daughter and if the price per share is lower or equivalent to A´s cost per share, he will have made no profit on the sale as a whole. Still, A will have to pay capital gains tax. If the price for all the shares is equivalent to 30% of the market value, the same proportion of the shares will be seen as acquired through a purchase, the rest as a gift. B will have to pay gift tax on the difference between the market value (often the "substance value") and the price she has paid. If X is sold to Y, for a price maximum A`s cost for acquiring the shares, the main differences are that there will be no capital gains tax for A and that the cost per share, in case of a future sale, will be equivalent to A`s cost, even if Y has paid less.

An example: Suppose A owns all the shares (1,000) in the unlisted family owned X Ltd. He bought them for 100 each, in total 100,000. At a market value of 200/share he sells all the shares to his daughter B for 60,000 (60/share). Of the total market value, 200,000, B has paid 60.000 (30 %). Thus 30% of the acquisition is considered as sale, with a revenue for A of 60,000 – 30,000 (30 % of his cost when he bought the shares) = 30,000, on which he will have to pay capital gains tax. B:s gift has a value of 200,000 (total market value) – 60,000 (actual price) = 140,000, on which she will have to pay gift tax. B`s cost per share, in case of a future sale, will be 60,000 (price) + 70,.000 (A`s price on the proportion of the sale that is seen as a gift) = 130,000.

It should be said that the cost per share for A (100) can be raised. One example is if he takes no dividends from X. Then a part of the fictitious dividend will be accumulated to the cost per share. However, if such an increase is calculated as a part of planning a succession, it can demand several years before it will make a substantial difference.

Usually a sale of the shares to B is not advisable if the purchaser has to take loans to finance the shares. The company profits will be taxed at a rate of 28 per cent and a dividend is taxed at 30 per cent, without deduction due to the first taxation. Hence there is a double taxation on company profits. If B chooses to take out a salary to pay the loans it will be taxed at 57 per cent (above a certain lower level), which is deductible for the company. However it has to pay an additional 30 per cent (on the salary) in social costs.

The double taxation is avoided by selling the family company to a (perhaps new) business Y Ltd owned by B. This way the company profits are taxed only once (28 per cent) before the loans, financing the purchase of the family company, can be paid. The interest is deductible. Within the concern the affiliated company (the former family business) can give dividends to the parent company in order to finance mortgages. Also the interests can be financed by the affiliated company. An alternative to avoid the double taxation is to sell the assets of the family company to a new business Z Ltd, established by the older generation, then sell the remainder (profits) of the family company to a third party and finally give the shares in Z to the next generation. By this procedure the substance value can also be considerably lowered, as well as the gift taxation.

In one case X Ltd was owned by three companions A (38%), B (30%) and C (30%). A´s children, D, E and F, owned minor parts after gifts from their father. All shareholders, except F, was working in X. Also F´s wife G, as well as B´s son H and C´s daughter I, were working in the company. A, B and C formed the board in X. The substance value was approximately 2,400 SKr/share. With the purpose of carrying through a succession D, E G, H and I started a new company, Y Ltd. They each owned one fifth of the shares and took part equally on the board. Y bought the whole of X for 2,100 SKr/share. The purchase was partly financed by bankloans and partly through promissory notes from A, B and C. The affiliated company (X) gave dividends to Y in order to finance mortgages and interest.

If the substance value is high (a million Euro or more), depending on the circumstances, the above mentioned alternatives may be difficult to use due to high taxation. The only reasonable alternative may prove to be a succession by starting a trust or similar. The main advantage of this method is that the succession problem can be solved once and for all. The (family) trust will be the owner of the company. There will however be gift taxes on the transfer of the assets to the trust and the beneficiaries will have to pay taxes on the dividends.

An insurance that is paid out as a lump sum on the death of the entrepreneur can cover the inheritance tax of the new owner in case of inheritance or make it possible to purchase shares in the company. Such an insurance is costly.[33] Another obstacle is the valuation of the firm. If the value increases over time, the insurance has to be, more or less, constantly changed on order to reflect the higher inheritance tax or the higher share price in case of a purchase of the company.

When an entrepreneur has two or more children who wish to take over, however not jointly own, the family company the situation will become even more complicated. If the family business can be split up in two or more independent businesses, there are legal possibilities to sell the assets to companies belonging to the children.

If the entrepreneur and other family members concerned decide to hand over the company to the next generation, they have thus to choose from several options. It seems like these options are mainly a question of financing the handover and avoiding excessive costs, not least taxes. Concerning taxes it should be the other way around. In other words: They should be abolished or considerably lowered, through a low valuation of the property or otherwise. At least a tax neutrality should be created, especially for handovers through a gift, a will and on intestate succession. There should also be possibilities to make a gift conditional on the receiver paying up to perhaps 20% of the market value of the shares, without hampering tax neutrality. That would make it possible for the older generation to get some money to provide for their welfare.

With such a tax system planning would be made much easier and consequently less costly and time consuming. It would not force the older generation to make more than a foreseeable minimum of reservations (in funds, insurance etc), due to a future succession, which otherwise can hamper investments and riskwillingness.[34] Further such a system would provide the older generations with fewer reasons to wait with the succession, which can contribute to avoiding risks and costs that are connected with successions that are executed to late.

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[33] Examples of insurance for expected tax liability are given in Astrachan and Tutterow 1996 pp 311-312.

[34] Compare Astrachan and Tutterow 1996 pp 305-313.

6. Lessons to be learned

The complexity facing the owner and the family when they wish to plan and carry out an intergenerational succession within the family is overwhelming. Personal as well as economic factors can be difficult obstacles. The older generation has to be willing to hand over the business and the younger generation has to be willing to take over. If the owner is not willing to reveal who is going to be the new entrepreneur, he can make a will. If he is willing to reveal the successor, he can choose to do nothing, and let the optional inheritance rules and agreements between the issue be decisive of the outcome. If the owner does not accept this uncertainty and costs due to potential rent-seeking behaviour etc, he and the family have several options planning the succession.[35]

All methods of planning and carrying through an intergenerational succession within the family, as presented in chapter 5, during the lifetime of the owner will be costly. Taxes have to be paid. Engaging consultants to plan the succession and to avoid excessive taxes will be expensive.[36] The succession procedure is also time consuming.[37] Further the procedure will result in uncertainty concerning the ownership and management, which can hamper business relations.

The taxes for handing over the company on intestate taxation should, as been said in the last section, be considerably lowered or abolished. The same goes for testate succession and gifts.[38] There should be established a strict tax neutrality, at least when it concerns successions through a gift, a will and by intestate succession. Taxes have nevertheless to be paid during the lifetime of the owner and a successful new owner will continue to pay, which the whole society will benefit from.

To make it possible to sell the company to the next generation the double taxation should be abolished, at least when a sale is made in relation to a succession. A sale will give money to the older generation to secure their standard of living and make it possible to compensate siblings who will not take over the ownership, which is not possible in the case of a gift.

> It is also possible in a legal system to provide incentives for the entrepreneur to provide for and make a succession in due time. As an example, if a country finds that it cannot abolish taxes on gifts etc., it could at least lower the tax rate and make the tax especially low if the company is handed over before the entrepreneur has reached a certain age.

There are several good reasons supporting the above mentioned changes of the tax law system

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[35] Rent seeking as an effect of intestate succession are dealt with in Bjuggren-Sund 1998 and effects of the entrepreneur deciding to wait with the succession in Bjuggren-Sund 1999.

[36] In one study the owners of the family firms reported an average of more than USD 33,000 on estate planning. These were expenditure on accountants, attorneys and financial planning. Astrachan and Tutterow 1996 p. 311.

[37] Astrachan and Tutterow, 1996, find that family members spent more than 167 hours on estate planning issues over a period of six years.

[38] How estate taxes can hamper business is shown in several papers, see i.e. Soldano 1996 and Astrachan and Tutterow 1996.

etc. As pointed out above the owner and the family are nonetheless facing several difficulties in the succession process. Why make it more complex, since we are all dependent on successful family businesses? They create jobs and income for the community. Since most intergenerational successions do not seem to be initiated, planned and carried out during the lifetime of the entrepreneur, it is urgent to adopt rules that make the complex procedure as easy as possible.

Further, as has been pointed out in a previous paper[39], it is important to enhance the possibilities for the children of the entrepreneur to take over the family business, since (on average) they can be most expected to show loyalty to the family, the company and the local community by putting an emphasis on successfully running the family firm. This complex and, especially for business, important loyalty cannot be expected from an outsider if the firm is sold to a third party. Showing loyalty to other persons, other companies and other communities as well as rewarding themselves with excessive wages are not unfamiliar phenomena. Further the importance of idiosyncratic knowledge, created within the family and often within the local community in interaction with other (family) businesses, should be stressed. This knowledge can be most easily given to the next generation within a family. To us there are therefore several good reasons for promoting intergenerational successions within the family.

> A third party can as a potential new owner, however, more easily see business alternatives or be more able to make the necessary, albeit unpopular, cutbacks, as well as be an important person in promoting a coming succession. These qualities can be acquired by the company by hiring a third party as a member of the board, not as an owner or a manager. This will enable the family to keep the loyalty qualities within the family.
>
> If an entrepreneur hesitates in initiating and planning the handover, due to excessive taxes and other obstacles hampering the possibilities to carry through a succession within the family, it will unavoidably lead to difficult situations when the next generation has to choose between starting their own businesses or becoming an employee and perhaps taking part in wasteful rent-seeking behaviour. All this incurs costs and uncertainty, concerning who will own and manage the business, which in turn will lead to unnecessary threats to the employees and risk of undue bankruptcy (among other things).[40]

An additional reason for making gifts of shares in particular to the next generation tax free is that if the taxes are high it will lead to tax consultants finding other ways of planning and executing the succession. These methods will be more complicated and thus more costly and time consuming. This in turn will lead to more cases where there are no initiatives taken or taken to late. Further, money and time will have to be spent on non-productive efforts. It should instead be devoted to investments.

At least the above mentioned EU-recommendation should be consistently carried through. It would make succession easier for owners and new family owners of the company.

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[39] Bjuggren-Sund 1999.
[40] See Bjuggren and Sund 1999.

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The Relation of Training Practices and Organizational Performance in SMEs

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The Relation of Training Practices and Organizational Performance in SMEs

Abstract

To determine whether training programs produce real benefits for small and medium-size enterprises (SMEs), we must investigate the relationships between those programs and their effects on the business performance of SMEs. Although a number of previous studies have attempted to accomplish this task, serious inadequacies, such as inconsistent definitions of training and "rough" methods of training classification and measurement, have raised doubts about the validity of their findings. To remedy these inadequacies and more accurately assess the relationships between training and training effectiveness, this study employs a comprehensive measurement of training including training organization, expenditure, duration, process, and delivery methods. Its findings show that firms with sophisticated training systems and strong management support for training are most successful at maximizing the effectiveness of their training programs.

Introduction and Research Objective

An educated and well-trained work force is considered to be essential to the maintenance of a business firm's competitive advantage in a global economy. It is also believed that training can and should be a powerful agent to facilitate a firm's expansion and the development of its capabilities, thus enhancing profitability (Cosh, Duncan, and Hughes, 1998). However, Westhead and Storey (1997) suggest that employees in small and medium-size enterprises (SMEs) are much less likely to receive training than their counterparts in larger organizations. They offer two possible explanations to account for this phenomenon. One is "ignorance," which suggests that small business owners are not aware of the benefits of training and consequently provides less than an optimal amount of it to their employees. Another is the "market-forces" explanation, according to which business owners provide a less-than-optimal level of training because they anticipate that the costs associated with training may exceed the benefits (returns) to be derived from it.

These two opposing arguments have important policy implications. If ignorance is the major reason for inadequate training, then either owners/managers are poorly informed or training programs have not been marketed with sufficient vigor, or both. Such a situation would justify government intervention in the form of minimum training requirements or direct training subsidies for SMEs. If, on the other hand, the market-forces explanation is found to be superior, then government intervention could prove totally ineffective. If we are to intelligently decide which policy direction to follow, we must first carefully examine the relationship between training programs and business performance, and determine the type and extent of benefits which training brings to SMEs.

Despite the growing importance of SME research during the last decade, very little attention has been paid to the effectiveness of training programs for small and medium-size businesses. Cosh, Duncan, and Hughes (1998), Marshall et al (1993, 1995), and Westhead and Storey (1996, 1997) have attempted to rectify this situation. However, their studies are inconclusive and their focus is strictly limited to Western society. Consequently, additional research on this issue from a greater variety of perspectives has been encouraged (Westhead and Storey, 1996).

In a survey of 1,480 SMEs in Canada, Baldwin et al (1994) found both the proportions of employees receiving training and training expenditure per employee to be negatively correlated with business profitability. They also discovered that the most successful firms tend to train fewer workers than less-successful ones. A study by Wynarczyk et al (1993) of fast-growth SMEs in the UK showed an insignificant relationship between the provision of training and firm performance when other related variables were controlled. Another survey conducted by the Cambridge Small Business Centre in the UK (1992), found no clear link between firm growth and the provision of training. Storey and Westhead (1994) after examining previous research on the relationship between training and small-business performance, concluded that the association between these two variables is not well established. Finally, Marshall et al (1995) suggested that management-training projects have little effect on the performance of small firms, though they may be successful in larger companies with greater management skill and capacity.

Westhead and Storey claimed that the studies they had reviewed (1997) had failed to substantiate an alleged link between training and improved performance. Noting that

training in SMEs may vary according to knowledge or skills conveyed, duration, proportion of the work force participating, and modes of delivery, they advocated studying the effects on firm performance of training programs classified according to their specific contents.

More recently, Cosh, Duncan, and Hughes (1998) investigated a sample of 1,640 UK SMEs that had participated in surveys in 1991 and 1995. As a result of their investigation, they found a positive link between training and firm survival, but one that was not statistically significant. The authors also examined the relationship between formal training and business performance in terms of employment growth and profitability. They found that training was strongly related to employment and sales growth, but unrelated to profit margins. In a subsequent review, Kitching (1998) faulted this investigation for defining "formal training" in a manner subject to differing interpretations by respondents. In addition he criticized the assignment of firms to trainer and non-trainer categories, based on the presence or absence of formal training programs, as "too rough" a system of classification. Kitching suggested a more sensitive conceptualization of the term "training investment," one which takes account of differences in the nature and duration of training and the extent of employee coverage.

Like earlier research by Westhead and Storey (1997) and Kitching (1998), this study seeks to examine the relationship between training systems and their effectiveness. However, it employs a concept of training that is more comprehensive than that of other studies, one that includes training organization, expenditures, duration, employee coverage, and delivery methods. A key aim is to profile differences in the training

practices of SMEs in Taiwan and in the effectiveness of training programs conducted by such firms.

Methodology

1. Data Source

The population from which our sample was drawn is the "name list of manufacturing firms in Taiwan," an electronic file maintained by the Ministry of Economic Affairs. This list contains data on 7,686 firms with a work force of between 50 and 300 employees. Six hundred firms, randomly selected from the population to ensure representation by all size categories, were sent questionnaires regarding their training practices. Of the 568 questionnaires received by these firms (32 were undeliverable), 144 completed questionnaires were returned, for an effective response rate of 25.4%. A comparison of participating firms with non-participating ones showed no significant difference in firm size.

The average number of employees per sample firm was 146. Classified by ascending order of scale, 30.8% of the sample firms had fewer than 100 employees, 36.3% had between 100 and 200 employees, and 32.9% had between 200 and 300 employees. The typical sample firm had been in business for 22 years. Trade unions had been established at 31.6% of the respondent firms, but not at the remaining 68.4%. Ninety-six percent of the sample firms are privately owned, and the remainder are state-owned enterprises.

2. Classifying Respondent Firms by Training Effectiveness

Respondents were asked to rank the performance of their establishments with regard to ten aspects of training-related effectiveness, in accordance with a five-point scale

ranging from “very good” (5) to “very bad” (1). The ten aspects are: product or service quality, work motivation, ability and knowledge, operational safety, profitability, work efficiency, job satisfaction, and the reduction of material wastage and absenteeism. Using the scores for these training-effectiveness indicators, this study employed cluster analysis to categorize the responding firms into “better” and “worse” performance groups. (See Table 1.) As a result, 84 firms were placed in the better training-effectiveness category and 46 in the worse category. (Since 14 of the sample firms did not complete the questionnaire, only 130 firms were classified in this manner.) The two groups were seen to be significantly different with regard to performance on the ten training-effectiveness indicators ($p<0.01$). The cluster analysis procedure showed that the average scores of the firms in the better group were all higher than firms that in the worse group.

Is training effectiveness related to organizational characteristics? Data show that although the average number of employees per firm in the better training-effectiveness group (155) is a little higher than that of the worse group (141), there is no statistically significant difference between them. The better training-effectiveness group also has a larger amount of capital per firm (US$69 million) than the worse group (US$11 million); however, there is no significant difference here either. The only significant difference is that the average firm age (22 years) in the better group is considerably greater than that in the worse one (17 years). The implication is that perceived training effectiveness is not related to firm size as represented by employee number and amount of capital, but that older SMEs seem to achieve better training results than younger ones.

Training Organization and Expenditures, and Training Provisions

Training consists of organized learning activities capable of improving individual performance through changes in knowledge, skills, or attitudes (Nadler, 1980). The training process includes such activities as identifying employee-training needs, designing annual training plans, devising training objectives, choosing delivery methods, implementing training programs, evaluating training results, and documenting training records. As an organizational subsystem (Goldstein, 1993), training must be closely coordinated with overall business strategy and the activities of line departments. Therefore, setting up a specific department within a firm to organize and implement employee training and development may result in more effective training.

Twenty-seven firms (33.8%) in the better training-effectiveness group responded "yes" to the question of whether they had set up a unit or department in charge of training affairs, while only eight firms (20.0%) in the worse training-effectiveness group did so. The proportion of firms establishing an independent training unit is significantly lower in the worse-effectiveness group than in the better one. This finding implies that establishing a specific department responsible for training does have a positive impact on training effectiveness. However, before taking action on this finding, an SME should first conduct a careful cost-benefit analysis to determine whether it is large enough to reap economies of scale from establishing a separate unit responsible for training.

We may also expect the size of the training budget to be related to training effectiveness. The present study shows that the average annual training expenditure per employee for the better training-effectiveness group was US$182, higher than the US$138 spent by the worse training-effectiveness group. However, the difference

between the two amounts was not statistically significant. Another important indicator is the percentage of total payroll spent on training. The mean percentage for this indicator was 0.93% for the better training-effectiveness group and 0.84% for the worse one, although the difference was not significant. One possible explanation why no strong positive relationship emerged between training expenditure and training effectiveness is the way that training expenditure was calculated in this study. Specifically, the cost of maintaining an independent training staff, which was found to be more prevalent in the better training-effectiveness group, was not factored into the total cost of training. This practice would obviously place a downward bias on training expenditures incurred by larger firms, those, which are likely to spend the most on training, and thereby weaken the statistical relationship between training expenditure and training effectiveness.

In a comparison with training expenditures in other countries (Lynch, 1994), this study found that the percentage of total payroll spent on average by Taiwanese firms on training exceeded that of Japanese firms (0.4%) and roughly approximated the average percentage spent by Canadian firms (0.90%). However, the 0.93% of payroll expended by the average Taiwanese firm on training was well below the 1.8% spent by the typical firm in the United States (including large firms), 1.8% in West Germany, 1.5% in the Netherlands, and 1.7% in Australia. The percentages for these other countries were obtained by surveys taken ten to 15 years ago (1984-89), and we may expect that in the interim the gap in training expenditure between Western firms and Taiwanese SMEs have, if anything, widened even further.

This study found a statistically significant relationship between the percentage of employees that received training and training effectiveness ($p<0.1$). Firms in the better

training-effectiveness group reported that 45.7% of their staff had received some type of training in 1998, versus 36.3% for the worse group. Differences were also reported according to position and job function. In the better firms, managers and supervisors received an average of 33.5 hours of training in 1998, professional and technical employees 32.4 hours, and clerical and manual workers 20.8 hours, respectively. The corresponding figures for firms in the worse group — 27.2, 22.0, and 14.2 hours —were considerably lower. However, the only job position to show a statistically significant difference ($p<0.1$) in training time across the two types of firms was that of professional and technical employee. Data used in this study indicate that the extent of training coverage and emphasis on technical training are closely related to training effectiveness, especially in the manufacturing sector.

Managing the Training Process and Enhancing Training Effectiveness

The training process includes such items as needs assessment, the setting of goals and objectives, the delivery of training services, the evaluation of results, and the coordination of training activities with other HRM functions. All of these steps are essential to the success of a training program.

Assessing the need for training is particularly important, because if this is not done an organization cannot be assured that the right type of training is being provided to its employees. As Table 2 indicates, there is a significant positive relationship between needs assessment and training effectiveness ($p<0.1$). About 70% of the SMEs in the better training-effectiveness group had conducted needs analysis, while only 64.0% in the worse group had done so.

Training objectives provide a link between needs and results, helping to identify the type of instruction required in order closing performance gaps. Training objectives also serve as benchmarks against which to evaluate progress achieved in the realization of organizational goals. This study finds a significant difference ($p<0.05$) between the proportion of firms in the better training-effectiveness group that designate training objectives (75.6%) and that in the worse group (57.8%) that do so. The implication is that firms that have a clear vision of their training objectives and know for what purposes training is being provided are more likely to achieve better training effectiveness.

This study does not find a significant relationship between results evaluation and training effectiveness, even though firms in the better training-effectiveness group are more likely to evaluate the effectiveness of their training programs than those in the other group are. However, the proportion of firms that submit the results of training evaluation to higher-level management is markedly greater ($p<0.01$) in the better training-effectiveness group (78.5%) than in the worse one (48.8%). Similarly, the practice of applying the results of training evaluation to other HRM functions (promotions, job assignments, and the determination of compensation) is much more common in the better group (38.7%) than in the worse one (14.3%). This finding suggests that while there may not be a strong linkage between the evaluation of training results and training effectiveness, the manner in which SMEs employ evaluation results may have an important impact on the success of their training programs.

Categories of Training and Delivery Methods

There are three major venues for the delivery of training services: on-the-job, on-site off-the-job, and off-site off-the-job. Schuler and Jackson (1996) suggested that decisions concerning delivery sites and methods might be constrained by the type of learning that is to occur, as well as by considerations of cost and time. Table 2 lists three venues and 14 delivery methods employed by firms participating in this study. Respondents were asked to report the frequency with which their organizations adopted each method, with 1 standing for "never," 2 for "seldom," 3 for "sometimes," 4 for "often," and 5 for "always." Also presented are mean frequency scores and ANOVA test results for firms in the better and worse training-effectiveness groups.

On-the-job training allows trainees to learn how to perform their jobs under direct supervision. This type of training can be implemented by using such methods as apprenticeship training, job rotation, and assignment to a task-force team. Data indicate that SMEs in the better training-effectiveness group consistently employ all three methods of on-the-job training more frequently than do those in the worse group. However, the only statistically significant difference between the two groups was found to occur in the frequency with which they adopted the task-force-assignment method.

Many methods can be used to deliver training at the workplace but off the job, ranging from the traditional lecture to high-tech Internet learning. Firms in the better training-effectiveness group were seen to employ all nine off-the-job-training methods more frequently than did those in the other group. Moreover, there were found to be statistically significant differences in the frequency with which these groups employed all nine methods, with the exceptions of case studies and Internet teaching.

Two common methods by which Taiwanese business firms deliver off-site training services to employees are enrolling them in college courses part-time and sending them to participate in workshops overseas. Since off-site training tends to be quite expensive, Taiwanese SMEs employ it far less frequently than on-the-job or on-site training. Firms in the better training-effectiveness group are more likely to use both of the off-site training methods mentioned above than are firms in the worse group. This implies that the breadth and depth with which firms apply methods of delivering training are strongly and positively related to training effectiveness.

Management Support and Training Effectiveness

SME owners and managers play a pivotal role in making decisions relating to the provision of formal, job-related training (Matlay, 1996). The literature suggests that owners and managers of smaller firms tend to demand less training than those of larger ones do (Westhead and Storey, 1997). One possible explanation of this tendency is that time-related pressures and the high direct cost of training may make SMEs reluctant to invest in training or to allow their employees to attend training courses. If top management does not provide support for or undertake a commitment to employee training, a firm may focus little attention on training activities. We may thus expect a strong correlation to exist between the degree of management support for training and training effectiveness.

The present study poses two questions designed to evaluate the degree of management support for training. The first one asks whether line managers in a respondent firm encourage subordinates to participate in training programs. Possible

response range from 1, “strongly disagree” to 5, “strongly agree.” The second question asks whether, during business downturns and economic recessions, top management usually gives priority to cutting training expenditures in an effort to reduce operating costs. Responses to this question are: 1, “strongly agree”; 2, “agree”; 3, “it is hard to say”; 4, “disagree”; and 5, “strongly disagree.” (Note that the order of ranking responses is the reverse of that used for the previous question.) The mean score for responses to these two questions is used to indicate management support for training. The mean score for firms in the better training-effectiveness group (3.69) is markedly higher than that for firms in the worse group (3.26), and an ANOVA test indicates that the difference between the two is significant at $p<0.01$. Thus management support is shown to be strongly related to training effectiveness.

Research Implications

The findings of this study have important implications for both academic researchers and training specialists. Previous studies attempted to estimate the impact of training on firm performance but did not achieve consistent findings. One of the major reasons for this inconsistency is the widely varying definition of training that these studies employed. Many of them measured only the amount of training provided. However, the provision of training may vary in the types of knowledge or skills conveyed, duration, numbers and percentages of employees covered, and modes of delivery. As a result of such variances, some types of training are more effective in improving individual firm performance than others improve. This study presents evidence that firms that have achieved greater effectiveness in training tend to have a more sophisticated training organization and training system than do those firms whose training methods have been less effective. The

implication is that future studies seeking to investigate the relationship between training and performance should take special care in measuring training effectiveness. Simply determining whether formal training is offered and the amount of it that is provided to employees is not adequate, since poor training programs, even those that provide many hours of instruction, may not benefit individual employees or firm performance at all.

To managers and training specialists in SMEs, the findings of this study provide clear direction and guidance. Maintaining a separate unit responsible for training affairs helps improve training effectiveness. However, owners and managers of SMEs should evaluate the costs and benefits of establishing such an independent training unit before they take that step. Amid intensifying global competition and rapid technological change, expanding the proportion of the work force that receives training and increasing training hours, especially for professional and technical staff, are also conducive to better training effectiveness.

The training process in firms that have achieved better training effectiveness is more comprehensive than that in firms that have been less successful in training. In general, a firm that has conducted needs assessment, devised training objectives, submitted training results to management, and coordinated training activities with other HRM practices is more likely to achieve success in training than are those firms that have not made such efforts. For this reason, instituting a more comprehensive training process in SMEs is strongly encouraged. Also recommended is that training specialists should seek to improve their knowledge of various training delivery methods and apply that knowledge broadly and frequently in implementing training programs.

Finally, but certainly not least important, are the commitment and support of top management for training. This study reveals a very strong relationship between management support and training effectiveness. With the size of the training budget, number of training hours, and proportion of training coverage all varying directly with the degree of management support, support from management may be the most critical element of all in achieving training effectiveness.

Limitations

The training-effectiveness indicators used in this study are based on subjective responses to questions about the impact of training on enhancing product or service quality, work motivation, ability, knowledge, and so on. A few scholars believe that subjective measures may be as reliable as more objective indicators (Dess & Robinson, 1984). However, since objective indicators are believed to achieve greater accuracy, it is hoped that future studies, time and resources permitting, will employ both subjective and objective measures of training effectiveness, so that comparisons can be made between the two.

A second limitation of this study is that a causal relationship between methods of delivering training and training effectiveness has not been established. Since the data used are cross-sectional, the only conclusion that can be made here is that better training systems are strongly correlated with training effectiveness. Longitudinal data must be collected and studied over the long term, or comparison made with an appropriate control group (Westhead and Storey, 1997), if we are to determine whether there is a causal linkage between comprehensive training systems and improved business performance.

Furthermore, even if improvement in training systems leads to more effective training, how can we be certain that the benefits of better training justify its cost? Utility analysis may be helpful in answering such questions. Finally, due to the limited size of our sample, conclusions reached by this study may not be entirely applicable to very small manufacturing firms or service-sector firms in Taiwan.

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Table 1. Results of Cluster Analysis of Training Effectiveness

Aspects of training effectiveness	Cluster mean		
	Better Training-Effectiveness Group (N=84)	Worse Training-Effectiveness Group (N=46)	F-Value
1. Enhanced product or service quality	3.96	3.00	107.6***
2. Inproved work motivation	3.81	3.09	40.9***
3. Reduced turnover rate	3.31	2.70	23.2***
4. Improved ability and knowledge	4.17	3.50	48.1***
5. Improved operational safety	4.07	3.37	51.6***
6. Decreased materials wastage	3.70	2.85	58.5***
7. Improved profitability	3.55	2.76	47.9***
8. Increased work efficiency	3.88	3.00	63.1***
9. Increased job satisfaction	3.77	2.91	68.9***
10. Reduced absenteeism	3.42	2.59	47.1***

Note: The scale ranging from “strongly agree (5)” to “strongly disagree (1)”.
*** : $p<0.01$

Table 2. Mean Frequency of Adoption of Training Delivery Methods by Two Training-Effectiveness Groups

Types of training and delivery methods	Better Training-Effectiveness Group	Worse Training-Effectiveness Group	F-Value
On-job-training			
Job rotation	2.79	2.57	1.39
Apprenticeship training	2.94	2.86	.09
Assigning trainee as member of task force	3.34	2.32	28.68***
On-site off-job-training			
Lecture	3.18	2.67	5.84**
Group discussion	3.27	2.89	4.12**
Role playing	2.27	1.86	5.55**
Sensitivity training	1.88	1.44	7.38***
Videotapes	2.60	2.05	7.90***
Simulations	2.50	2.09	5.18**
Case study	2.91	2.64	1.83
Computer software	2.56	1.95	8.30***
Internet teaching	1.84	1.64	1.39
Off-site off-job training			
Part-time college courses	2.10	1.64	6.47***
Overseas workshops	2.13	1.41	15.53***

Note: The scale is scored as 1 for “never,” 2 for “seldom,” 3 for “sometimes,” 4 for “often,” and 5 for “always.” ** : $p<0.05$; *** : $p<0.01$.

Gazelles in the 1990s: Why did they leap so high?

An analysis of high growth firms from the Australian Business Longitudinal Survey 1994-95 to 1997-98

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Summary

A little over one fifth of Australian firms that operated between 1994/95 and 1997/98 saw their total income grow by more than 40% while a similar number increased their employment by at least 30%. Strongly growing businesses are the subject of intense interest and this paper analyses the characteristics of these firms, sometimes called "gazelles". Using data from Australia's Business Longitudinal Survey (BLS) and a variety of statistical techniques, this paper examines these firms and considers the following questions in particular:

Did gazelles share similar operational characteristics and which industries were they found in?

how small businesses compared to other businesses?

Notation

Employment gazelles (EGs): firms whose total employment grew by more than 30% between 1995 and 1998.

Turnover gazelles (TGs): firms whose total turnover grew by more than 40% between 1994-95 and 1997-98.

Introduction

The Business Longitudinal Survey is unique: it is the only large-scale longitudinal survey of businesses in the world offering such a wide range of data on the characteristics and performance of businesses. Between 1994/95 and 1997/98 (the last year of the survey) the BLS tracked an initial sample of over 5,500 Australian firms which appeared on the ABS Business Register. By 1 July 1998 some 4,200 were still trading and these firms have formed the continuing panel for analysis over the four year period.

Defining a Gazelle

The term *gazelle* has been applied to those businesses that have enjoyed relatively rapid growth. As a first step in this analysis, a statistical definition was required. Business growth can be defined in many ways but two aspects were concentrated upon in this paper: growth in employment and growth in turnover. Although many businesses

that grew in one area saw corresponding growth in the other, this was not necessarily the case and separate definitions for *employment gazelles* (EGs) and *turnover gazelles* (TGs) were formulated.

Total employment growth was measured over the four years June 1995 to June 1998, and growth in turnover between 1994/95 and 1997/98. Gazelles are firms that grew exceptionally strongly, and natural breakpoints in the two distributions of growth were sought. The distribution of turnover growth rose steeply, only beginning to level out when it passed growth of 40%. This seemed the natural point at which to define a *turnover gazelle*. An estimated 26% of firms in the population had a growth in turnover of 40% or more over the period. They were defined as the *turnover gazelles* (TGs).

It was more difficult to find a natural break point in the distribution of employment and so, for consistency, a similar proportion of firms were defined as *employment gazelles* (EGs): an estimated 28% of firms saw their total employment grow by 30% or more between June 1995 and June 1998.

Contribution to total growth

The total growth over the period, amongst all firms in the BLS population, was an estimated 668,000 jobs and $156,000 million in turnover. Amongst those firms that operated throughout the period 1995-1998, there was an estimated growth in turnover of $228,000 million and growth in employment of 961,000 jobs.

The majority of growth was attributable to the gazelles. *Turnover gazelles* saw their total turnover increase by $173,000 million, while the *employment gazelles* created some 866,000 jobs. The net gains of the top 22% of growing firms in each category were therefore considerably greater than the net gains that arose from the entire population of firms. Gazelles also accounted for 75% of the turnover growth and 90% of the growth in employment of firms that operated over the whole period.

Overlap of Employment and Turnover Gazelles

As one would expect, there is a significant overlap between those firms whose turnover has grown strongly and those that recorded employment growth. But the overlap is by no means complete, as Table 1 demonstrates.

Although the association is highly significant, only about one half of *turnover gazelles* were also *employment gazelles*.

***Table 1**: The relationship between the two types of gazelles*

(Estimates for Australia)

		Turnover Gazelle		
		No	**Yes**	
Employment	**No**	212,000	48,000	*260,000*
Gazelle	**Yes**	53,000	47,000	*100,000*
		265,000	*95,000*	***360,000***

Methodology

The BLS collected a variety of information about the way in which firms were organised and run. A number of these factors were thought likely to influence growth and, as a first step, the association of growth with each was considered in turn. A simple chi squared test was performed on data from each cross tabulation of *gazelle status* x *levels of explanatory variable*. For example, in Table 2 gazelle status is cross tabulated with main business location.

***Table2**: Location of Gazelles*

	Employment Gazelles				**Turnover Gazelles**		
State	0	1	*Totals*	**State**	0	1	
NSW	1155	431	*1586*	*NSW*	1163	423	*1586*
VIC	840	323	*1163*	*VIC*	838	324	*1162*
QLD	577	214	*791*	*QLD*	603	189	*792*
SA	234	72	*306*	*SA*	236	71	*307*
WA	187	113	*300*	*WA*	219	81	*300*
TAS	118	33	*151*	*TAS*	111	40	*151*
NT	19	14	*33*	*NT*	19	13	*32*
ACT	53	21	*74*	*ACT*	57	17	*74*
Totals	*3183*	*1221*	*4404*	*Totals*	*3246*	*1158*	*4404*

A chi squared test looks for independence in the two variables by comparing the distribution of observed data with the distribution one would expect if the proportion of gazelles were the same in each level of the explanatory variable (more details are available in virtually any statistics text, eg *Hoel [1]*).

Log Linear Models

Simple cross tabulations are merely a first step, however, as the true relationship between any explanatory variable and the probability of being a gazelle might be clouded or confounded by other factors, most notably business size and industry. For example, it might appear that businesses which operate as a franchise are more likely to be

gazelles than those which are not franchisees. But the probability that a business is a gazelle might also be linked to a firm's size or industry, both of which might also be related to the likelihood of franchising status. Conversely, it is possible that while no *prima facie* relationship is observed between the likelihood of being a gazelle and an explanatory variable, there may be a relationship once the associations between each explanatory variable and the different size and industry groups are considered simultaneously. For instance although businesses in Victoria may appear no more likely to be gazelles than firms elsewhere, it may be that **small** businesses in Victoria were more likely to be gazelles than **small** businesses elsewhere (and larger firms less likely). To consider these possibly complex patterns, a series of log linear models were developed to investigate each variable's effect across different size groups and industries. It was hoped that such models would provide

- a parsimonious description of the data to aid understanding and interpretation; and
- an ability to test whether the apparent association between each explanatory variable and the probability of a firm being a gazelle was both strong and constant across different sizes and industries.

Details of log-linear models can be found in a variety of sources (such as *Everitt* [3]) but a basic explanation is given in Appendix 1. Essentially, each variable was cross tabulated by both size and industry and a log linear model set up. The most parsimonious model fitting the data was examined to see whether

- there was an association between the explanatory variable and the chances of being a gazelle; and
- any association varied between industries or size groups.

Model fit is tested by a log likelihood statistic which, under the null hypothesis of the reduced model fitting the data, should have a chi squared distribution, with degrees of freedom determined by the number of terms dropped in the reduced model. A model with a poor fit will therefore have a low p value, indicating a significant departure from the appropriate chi squared distribution and the null hypothesis. A p value of less than 0.05 suggests that there a reasonable grounds for believing that the model does not adequately fit the data (ie, there is less than a 5% chance that the model is appropriate).

Logistic Regression

While it is interesting to consider each of the associations between size groups and industries with each explanatory variable alone, it is also important to consider the effect of all variables acting together. For example, both training and business planning appeared to have highly significant associations with the chances of a firm being a gazelle. But it might be that the two variables are highly correlated themselves and when used together in a model only one will be useful (that is most businesses that train also used business plans and so the association might be due to only one of these explanatory variables). A logistic regression was run to consider the effects of all the variables acting simultaneously. For these regressions, some variables were defined differently (*eg*, there was a finer breakdown by size and age) and models were built for both *employment* and *turnover gazelles*.

Logistic models have the form Logit $P_i = \log [P_i/(1-P_i)] = alpha + b_i X_i + e_i$ where P_i is the probability that a business is a gazelle, *alpha* is the intercept, b_i's are coefficients, X_i's are the independent variables and e_i is the error term. Lack of space here precludes further details about logistic regression but there are many references elsewhere in the literature (*eg, Dobson [2]*).

Weighting

The BLS sample was drawn using stratified sampling, and so a set of quite complicated weights need to be applied to the data before generalisations can be made about the population as a whole. There is some debate about when and where it is appropriate to use population weights depending on the statistical technique being applied. In this study population weights have been used for most of the analysis, with the exception of the logistic regression models. However, most sample stratification was carried out on the basis of size and industry, and industry and size were used as explanatory variables in the logistic regression models to try to allow for the sample design.

Results

The association between each explanatory variable and the likelihood of a firm being a gazelle was first considered with simple cross tabulations and chi squared tests, then by using log linear models broken down by size and industry and finally in an overall logistic regression. Detailed output from the logistic regression model is at the end of the paper.

Size and Industry

Employment Gazelles

The apparent effect of size alone was first considered across all industries with businesses broken down into four size groups: Micro (0-4 employees), Small (5-19 employees), Medium (20-99 employees) and Large (100+ employees. There were significant variations by business size, with Micro firms significantly more likely than other firms to have become *employment gazelles* over the period.

At first glance there appeared to be strong relationships between particular industrial divisions and the likelihood that a firm was an *employment gazelle*. *Employment gazelles* were more likely to be found amongst the *Accommodation, cafes and restaurants*, *Retail trade* and *Wholesale trade* divisions. They were less likely to be found in the *Manufacturing* and *Property and business services* divisions. These results were significant.

To get a better understanding of the effects of size and industry it was important to consider the two variables together. Different industrial divisions are comprised of different proportions of small firms. For example, if there are more *employment gazelles* in the *Retail trade* division, one needs to consider whether this is because *Retail trade* has an association with high employment growth or because there are proportionally more small businesses in the *Retail trade* division than elsewhere and small business size has an association with high growth.

In order to keep cross classifications to a manageable number and sample sizes relatively large, businesses were split into only two groups by size: Small (those with employment of 1-19 people) and Other (those with employment of 20 or more). When considering the number of gazelles broken down by size and industry, the log linear model with

independent effects of size and industry *(Model (2) above*), did not fit the data. Rather, the proportion of gazelles in each category depended on both the industrial division, the size of firm and the interaction of size and industry. Although Small businesses were more likely to be EGs than larger ones in most industries, this was not true in two industrial divisions: *Construction* and *Property and business services*. Once these two divisions were dropped, the model of independent effects fitted the data. Among the remaining 9 industrial divisions, there was a strong association between firm size and the likelihood of being an *employment gazelle*, with smaller firms more likely to be gazelles than larger firms. Furthermore, amongst these 9 industries, the *Accommodation, Cafes and restaurants* division had a strong positive association with the likelihood of being an EG while firms from the *Finance and insurance* and *Manufacturing* industries had a strong negative association.

A separate model was run solely for the two industries not included in the model above (*Construction* and *Property and business services*). Size did not have a strong association with the chances of being an EG for these firms. *Construction* firms were significantly more likely to be gazelles than those from *Property and business services*. These results were broadly supported by the logistic regression model. Micro firms were significantly more likely to be *employment gazelles* as were firms in the *Construction* and *Accommodation, cafes and restaurants* industries.

Turnover Gazelles

There was no significant association between a firm's size and its likelihood of becoming a *turnover gazelle* over the period.

Before taking account of size, there was a strong relationship (p=0.001) between a firm's industry and its chances of becoming a TG. There were highly significant positive associations between businesses from the *Construction* and *Finance and insurance* divisions. There was an equally strong but negative association amongst *Retail trade* firms.

These findings are further supported after considering the joint effects of industry and size. Once again, size (measured as either *Small* or *Other*) played no significant part in predicting whether a firm would become a *turnover gazelle*. Industry, however, had a strong effect with the *Construction* and *Finance and insurance* divisions strongly associated with an increased chance of becoming a TG and the *Retail trade* division strongly associated with a

decreased chance of being a TG. The results from the logistic regression also highlight a significant positive association amongst *Construction* and *Finance and insurance* firms.

Other Firm Characteristics

Business Practices

In 1995 businesses were asked a number of questions about their managerial practices. In particular, each firm was asked whether it had a documented business plan and whether it compared its performance with other businesses during 1994-95.

Business Planning

There was a highly significant association (p=0.001) between businesses that had documented business plans in 1994/95 and businesses that went on to be either *employment* or *turnover gazelles*. Once the effects of size and industry were taken into account, there was still a strong link between business planning and both types of gazelle. Amongst *employment gazelles*, business planning was strongly associated with the chances of being an EG. The strength and direction of association did not vary between size groups but was different in certain industries. The positive effect was very strong in the *Finance and insurance* division, where business planning was particularly linked to the likelihood of being an EG. But among the *Accommodation, cafes and restaurants* and *Personal services* industries business planning had a negative association with the chances of becoming an EG. In the logistic regression, businesses that planned were 25% more likely to become EGs (p=0.001).

Amongst *turnover gazelles*, a model using industry, business planning and their interaction just fitted the data (p=0.06) . Business planning had a strong positive association with the chances of being a TG in certain industries but not among different sizes of firms. The effect was most marked in the *Retail trade* division. Again, in the logistic regression, businesses that planned were 27% more likely to become TGs than those who did not (p=0.001).

Business Comparisons

Across all firms, businesses that compared themselves with others were rather more likely to be EGs than those who did not (but the association was barely significant with p=0.046). They were, however, no more likely to be TGs.

Once the effects of size and industry were taken into account, there was no straightforward association between business comparisons and EGs, nor were there any 2 way effects (that is the association between whether a business was likely to become a gazelle and whether it made comparisons differed across size groups and industries). The only effects of importance was the three way interaction term of size, industry and whether the firm used business comparisons. There was no evidence of any association, straightforward or otherwise, between business comparisons and the likelihood of becoming a TG. The logistic regression found no evidence of association either.

Franchising

In 1995 the BLS asked firms whether they were operating as a franchise.

Across all industries and size groups, businesses that were operating as a franchise in 1995 were not significantly more likely to be gazelles than those who were not. Once the effects of size and industry were taken into account there was still no link between EGs and whether firms operated as a franchise, with the model containing size, industry and the interaction term fitting the data well ($p=0.43$). However, after allowing for size and industry, franchising status did appear to have a relationship with TGs. Amongst larger firms, those that operated as a franchise had a lower chance of becoming a TG. But the reverse was true for smaller firms, with franchise businesses being more likely to be TGs than those that operated independently. The effects of franchising status were relatively constant across industries. Here the model including only industry, size, franchise status and the interaction of size and franchising status fitted the data ($p=0.15$). These results appear to be contradicted by the logistic regression, which showed a positive association between those that operated as a franchise and those that were EGs. However, in the regression the effect was barely significant ($p=0.047$), while in the log linear model the effect of franchising was only just insignificant ($p=0.087$) so there is little discrepancy.

Family Business

In 1996 the BLS asked firms whether they considered themselves to be family businesses. It seems reasonable to assume that virtually all of those who considered themselves to be family business in 1996 were family businesses over the entire period, but the question was not asked in 1995. Across all size and industry groups it appeared that family businesses were as likely to be TGs as non-family businesses. However there was a significant association

between family business status and EGs: family businesses were highly significantly less likely (p=0.003) to have been an EG over the period.

After allowing for size and industry effects there was still a strong association between family business and *employment gazelles*. Family businesses were less likely to be EGs although the effect varied in intensity across industries, with the negative association being particularly strong in the *Cultural and recreational services* sector. A model containing industry, size, family business status, and the two-way interactions of industry*size and industry*family business status fitted the data well (p=0.92).

Family business seemed to be associated with the incidence of TGs although the strength and direction of association varied between industries. Family business had the greatest influence in the *Construction* and *Transport and storage* industries. In the former industry, family businesses were more likely to have been TGs than non-family. In the latter industry, family businesses were much less likely to have been TGs. Here the model containing only industry, family business status and the interaction term fitted the data well (p=0.36). The logistic regression model suggested that family businesses were significantly less likely to be either type of gazelle.

Training

The survey asked questions in 1998 about whether a business trained its staff during 1997-98. These results compare the performance of businesses that were training staff in 1998 with those that were not. The fact that a business trained its staff in 1998 does not necessarily mean it trained its staff earlier in the period. Indeed, although training levels within a business might influence growth they are also likely to be influenced by growth. An *employment gazelle*, by definition, is a firm that has taken on a significant proportion of new staff and, with new staff, there is often a need for training. In these circumstances it is impossible to decide what is cause and effect but it was felt that training was an important explanatory variable and should be included.

Across all industries and size groups there were highly significant relationships (p=0.001) between whether a firm trained any of its staff in 1997/98 and whether it was a gazelle over the period. Once the effects of size and industry had been taken into account, there remained a very strong association between whether a firm trained its staff in

1998 and whether it had been either type of gazelle over the period. If a firm trained its staff in 1998 it was significantly more likely to have been an EG. The effect varied, and was particularly strong in the *Finance and insurance* and *Personal and other services* industries. But the converse was true among *Retail trade* firms: those training staff in 1998 were less likely to have been EGs. A model including industry, size, training status and the interaction of industry and training fitted the data well (p=0.76).

There was a clear positive association too between whether a business trained its staff in 1998 and whether it was a turnover gazelle. This effect did not vary significantly across industries. Here a model involving only the independent effects of industry and training fitted the data well (p=0.49).

Results for the training variable in the overall logistic regression were not included because of a relatively poor response rate to this question. About a quarter of the sample did not answer it and including the variable in the full model would have cut the sample size dramatically. However, a full logistic regression was run (on the reduced sample) which included training, and the training variable's effect was still strongly positive and highly significant.

Managerial Structure

In 1995 the survey asked about the numbers of managers, working proprietors and total staff employed. For this analysis, businesses were put into three categories according to the proportion of the work force that were either managers or working proprietors. Those with less than 15% of their work force in managerial/working proprietor roles were placed in one group; between 15-30% were placed in another; and a third group was formed where more than 30% of staff were in these roles. This variable will be strongly correlated with size: any business employing less than 6 staff could not fall into the first group, unless it reported having no managers or working proprietors.

Although there was no apparent association between EGs and managerial structure, there was a significant association (p=0.023) between managerial structure and TGs. Businesses with fewer than 15% of their staff in managerial positions had a greater chance of being a TG.

Once the effects of size and industry were taken into account, there was a strong association between managerial structure and EGs which varied across industries. Higher proportions of management tended to be associated with a greater chance of becoming an EG, particularly in the *Cultural and recreational services* industry. But the opposite was true for the *Finance and insurance* and *Property and business services* divisions where lower levels of management were strongly associated with an increased chance of becoming an EG. Here a model containing the three independent effects of industry, size and managerial level, together with the two way interactions of *size*industry* and *managerial level*industry* fitted the data well (p=0.75).

Managerial structure had a significant relationship with the incidence of *turnover gazelles* after the effects of size and industry had been allowed for. A high proportion of managers tended to be associated with a greater incidence of TGs, but the effects varied across industries. The effect was strongest in the *Cultural and recreational services* industry, while the converse was true in the *Retail trade* and *Property and business services* divisions. The optimum model here again involved the three independent effects of industry, size and managerial level, together with the two way interactions of *size*industry* and *managerial level*industry* and fitted the data adequately (p=0.35). The logistic regression showed no strong link between the proportion of managers and the incidence of gazelles which suggests that managerial structure is associated with other firm characteristics.

Exports

Each year the BLS asked whether firms had exported goods or services in the preceding year. For this paper, firms were split into three groups: those that did not export in either 1995 or 1998; those that exported in one and only one year; and those that exported in both 1995 and 1998. These results compare the incidence of gazelles amongst firms according to whether they were exporting at the beginning and/or end of the period.

Across all industries and size groups there was no significant association between whether a firm exported and whether it was classed as a gazelle. This result held true once the effect of size and industry had been accounted for, with optimum models for each type of gazelle not including level of exporting as an explanatory factor. Exporting was not a significant variable in the logistic regression either.

Innovation

Each year the BLS asked a number of questions relating to how innovative firms had been that year. Firms were asked about expenditure on research and development and whether they had introduced new good and services, or new processes for the supply/manufacture of goods or services. Each firm was classed as innovative or not according to their answers. Again, the sample was broken into three groups: those that were not innovative in either 1995 or 1998; those that were innovative in one and only one year; and those that were innovative in both 1995 and 1998. These results compare the incidence of gazelles amongst firms according to whether they were innovative at the beginning and/or end of the period.

There were highly significant relationships (p=0.001) between business innovation and the incidence of gazelles. Businesses that were innovative in both 1994/5 and 1997/8 were more likely to be gazelles than those innovative in only one year, who in turn were more likely to be gazelles than businesses that did not innovate in either year.

After allowing for the effects of size and industry there remained a strong association between the likelihood of a business being an EG and the level of innovation, although the effect varied according to a firm's industry. In general, the more a business innovated the greater the chances that it would have been an EG. The positive effect of innovation was particularly marked in the *Construction* and *Property and business services* industries. However there was a significant negative association between innovation and the chances of becoming an EG in the *Personal and other services* industry. The model involving industry, size, innovation and the interaction terms industry*innovation and industry*size fitted the data reasonably well (p=0.22).

For the *turnover gazelles*, the picture was less clear. There was no independent innovation effect nor any clear two way interactions. Only the saturated model fitted the data, that showed innovation had different effects depending on both the size and industrial division of each business. Innovative Small *manufacturing* firms were particularly likely to be TGs, but the effect did not hold for larger manufacturers. *Property and business services* firms of either size were more likely to be TGs if they innovated. In the logistic regression there were significant positive associations between innovation and both types of gazelle.

Proportion of part-time staff

It was felt that the proportion of a business's employment that was part-time may influence growth, and in 1995 the BLS collected information on the numbers of full and part-time employees. For this analysis, the sample was split into four groups according to whether a firm employed no part-time staff; between 0-20% of staff part-time; 20-50% of staff part-time; or more than 50% of staff part-time.

Across all size and industry groups the proportion of part-time employment at June 1995 did not have a strong association with whether a business would go on to be a gazelle. These findings were supported when a log linear model, which allowed for size and industry effects, was sought. Only the saturated model fitted the data, which implied that the effect of numbers of part-time staff varied across both industries and size groups. In the logistic regression there was a significant negative association between those businesses that employed more than 20% of their staff part-time in 1995 and the likelihood of being an EG.

Business age

The BLS recorded how long each business had been owned or controlled by its present owners or, in the case of public companies, how long it had been in operation. For this study the sample was broken into four groups depending on each business's age in June 1995: those firms that were older than 10 years; those aged 6-10 years; those aged 2-5 years; and those less than 2 years old. There were highly significant associations between age and the chances of a firm becoming an *employment gazelle* (p=0.001) or a *turnover gazelle* (p=0.013). Firms aged between 2 and 5 years were most likely to become gazelles, followed by firms aged 5 to 10 years. The very young (less than 2 years old) or more established firms (older than 10 years old) were less likely to grow quickly. Once industry and size were accounted for, there was still a strong link between the age of a business and its chances of becoming an EG. Once again, firms aged 2-5 and 6-10 years old tended to have a greater chance of becoming an EG, although the effect varied greatly across industries. The model containing the effects of industry, size, age and the interaction of industry*age, fitted the data quite well (p=0.64). It is interesting to note that size and age are both useful predictors of the likelihood of employment growth, even when used together.

Among *turnover gazelles*, the effect of the age variable depended strongly on both the size of the business and, separately, its industry. Differences were most marked among business aged 2-5 years. Here, small businesses aged 2-5 years had a greater chance than their younger and older counterparts of becoming a TG over the period. That is smaller businesses seemed more likely to grow in their first two years or their 5th to 10th years of operation than in their 2nd to 5th years. Larger business aged 2-5 years, however, were more likely to become TGs than those aged 0-2 years or 5-10 years. This seems rather surprising but perhaps many of the larger businesses aged 2-5 years (those that employed 20 or more people) had grown quickly over their first few years to reach that number of employees and so continued to grow (in terms of turnover growth) over the period. Whereas, if a business was already more than 2 years old and did not yet employ 20 people there was more chance that it would stagnate and not go on to achieve rapid turnover growth. Effects again varied across industries, though it was more difficult to draw conclusions here. The fitted model contained the effects of age, industry, size and the interactions of age*size and age*industry. These results are supported by the full logistic regression which used a finer breakdown of age. Younger businesses, particularly those aged 1-10 years in 1995, were significantly more likely to become gazelles than their older and very young (less than 1 year old) counterparts.

State

These results compare the performance of businesses according to their location in 1995. Across all size and industry groups there was no evidence to suggest that businesses had a different chance of becoming a TG according to their State. However, there was a highly significant association between location and the chances of becoming an *employment gazelle*. Businesses in Western Australia and the Northern Territory were strongly out performing their colleagues elsewhere in the country while those in South Australia and Tasmania were less likely to become EGs.

Because there are 8 States, 11 industrial groups and 2 size groups, a full cross classification by State, industry, size and gazelle status would involve a table with 352 cells (8x11x2x2). As a simplification, Western Australia was first compared with everywhere else together to see if it was outperforming the rest of Australia. After allowing for the effects of size and industry there remained strong evidence that Western Australia was strongly associated with the chances of a firm being an EG. Each State/Territory was compared against the rest of the country but there was little evidence to suggest other differences. There was also evidence to suggest that firms from Victoria had a greater

chance of becoming a TG than their counterparts elsewhere. The picture was more blurred elsewhere. For instance, firms from New South Wales had a lower chance of being a TG than elsewhere in the country if they were from the *Transport and storage* or *Cultural and recreational services* industries. But New South Wales firms in the *Retail trade* sector were more likely to have become TGs than retailers elsewhere. While in Queensland, *Construction* and *Retail trade* firms had a lower chance of becoming a gazelle than similar firms across the rest of Australia , although their *Transport and storage* firms had a greater chance of becoming a TG.

It seems likely that State is associated with the other business characteristics considered in this analysis. In a reduced logistic regression (containing only size, industry and State as explanatory variables), there was a significant association between Western Australia and the chances of being an *employment gazelle*. However, once other variables were added to the model the effect was no longer significant

An Overall Model

Details of the logistic regressions used were set out in the methodology section of this paper. The results in Table 3 give information about logistic regression models containing only industry, size and each explanatory variable in turn (the crude odds ratios) and all variables acting together (adjusted odds ratios).

The ***odds ratio*** is often used to compare the relative risks of a certain outcome happening to two members of separate groups. The crude ratio relates to a logistic regression model including only the explanatory variable in question, together with the four size and eleven industry explanatory variables (always included to help allow for the sample design). The adjusted ratio relates to the variable in question being included in a model along with all the explanatory variables, thereby helping to overcome problems of strong association between variables.

Odds ratios were estimated relative to the following set of characteristics. *Industry*: Manufacturing; *Size*: Micro; *Age*: More than 20 years old; *State*: NSW; Did not have a business plan in 1995; Did not make business comparisons in 1995; Did not operate as a franchise in 1995; Was not a family business; Did not train staff in 1998; Did not export in 1995 or 1998; Did not innovate in 1995 or 1998; Less than 20% of staff were managers or working proprietors in 1995; Less than 20% of staff worked part time in 1995.

Table 3: Relative odds of being a gazelle between 1994-95 and 1997-98

	Turnover Gazelles				Employment Gazelles			
Variables	***Crude Odds Ratio*** [1]	***Adjusted Odds Ratio*** [2]	***95% Conf Interval***		***Crude Odds Ratio*** [1]	***Adjusted Odds Ratio*** [2]	***95% Conf Interval***	
Mining	1.30	1.09	*0.57*	*2.05*	0.81	0.60	*0.27*	*1.30*
Manufacturing [3]	1.00	1.00			1.00	1.00		
Construction	***1.87	***2.15	*1.59*	*2.90*	1.32	**1.46	*1.07*	*1.98*
Wholesale trade	1.05	1.08	*0.87*	*1.34*	1.14	1.11	*0.90*	*1.37*
Retail trade	0.89	0.95	*0.71*	*1.26*	*1.27	*1.33	*1.01*	*1.75*
Accomodation, cafes and restaurants	0.99	1.04	*0.69*	*1.56*	1.39	**1.67	*1.14*	*2.44*
Transport and storage	1.07	1.12	*0.77*	*1.64*	1.00	1.07	*0.73*	*1.57*
Finance and insurance	***2.09	***2.09	*1.46*	*2.98*	0.95	0.88	*0.60*	*1.31*
Property and business services	***1.46	***1.43	*1.15*	*1.78*	1.11	1.06	*0.84*	*1.32*
Culture and recreational services	*1.61	*1.56	*1.01*	*2.39*	1.08	1.12	*0.70*	*1.77*
Personal and other services	1.00	0.93	*0.56*	*1.54*	0.93	0.84	*0.51*	*1.39*
Micro (0-4 employees) [3]	1.00	1.00			1.00	1.00		
Other small (5-19 employees)	1.05	1.02	*0.84*	*1.25*	***0.73	***0.71	*0.58*	*0.86*
Medium (20-99 employees)	0.95	0.95	*0.73*	*1.22*	***0.55	***0.51	*0.40*	*0.66*
Large (100+ employees)	1.05	0.99	*0.72*	*1.37*	***0.53	***0.46	*0.33*	*0.64*
Age at 30 June 1995								
Less than 1 year	1.24	1.19	*0.94*	*1.51*	*1.32	1.20	*0.94*	*1.52*
1-2 years	***2.07	***2.01	*1.41*	*2.88*	*1.58	*1.44	*1.00*	*2.08*
2-3 years	***2.06	***2.00	*1.45*	*2.76*	**1.58	**1.55	*1.12*	*2.15*
3-4 years	**1.74	**1.65	*1.13*	*2.43*	*1.54	*1.46	*0.99*	*2.15*
4-5 years	***1.96	***1.86	*1.33*	*2.59*	1.32	1.21	*0.85*	*1.72*
5-7 years	***1.7	***1.69	*1.29*	*2.22*	**1.49	**1.43	*1.08*	*1.89*
7-9 years	*1.39	**1.33	*1.00*	*1.76*	*1.41	1.27	*0.96*	*1.69*
9-11 years	*1.41	**1.38	*1.00*	*1.92*	***1.72	**1.62	*1.17*	*2.23*
11-14 years	*1.33	*1.33	*1.01*	*1.76*	1.16	1.15	*0.86*	*1.52*
14-17 years	1.51	*1.11	*0.77*	*1.60*	1.00	0.96	*0.66*	*1.40*
17-20 years	1.14	*1.17	*0.83*	*1.65*	1.18	1.15	*0.82*	*1.62*
20+ years [3]	1.00	*1			1.00	1.00		
NSW [3]	1.00	1.00			1.00	1.00		
VIC	1.03	1.02	*0.87*	*1.20*	1.05	1.07	*0.89*	*1.27*
QLD	0.99	0.95	*0.77*	*1.17*	1.05	1.02	*0.83*	*1.26*
SA	1.09	1.05	*0.80*	*1.37*	1.09	1.10	*0.83*	*1.44*
WA	1.12	1.09	*0.84*	*1.42*	*1.29	1.24	*0.96*	*1.61*
TAS	0.90	0.95	*0.58*	*1.54*	0.87	0.93	*0.57*	*1.52*
NT	0.88	0.84	*0.39*	*1.84*	0.76	0.73	*0.32*	*1.65*
ACT	0.92	0.79	*0.39*	*1.60*	0.82	0.70	*0.34*	*1.45*
Did have a business plan in 1995	***1.36	**1.27	*1.08*	*1.50*	***1.35	**1.25	*1.05*	*1.47*
Made business comparisons in 1995	1.05	0.98	*0.83*	*1.15*	1.06	0.95	*0.80*	*1.11*
Operated as a franchise in 1995	0.93	0.87	*0.61*	*1.25*	*1.47	1.40	*1.00*	*1.95*
Operated as a family business	***0.79	*0.84	*0.72*	*0.97*	***0.73	***0.78	*0.67*	*0.91*
Trained staff in 1998	***1.53	**...**			***2.30	**...**		
Exported in 1995 or 1998	1.16	1.14	*0.96*	*1.36*	1.05	0.98	*0.82*	*1.18*
Innovated in 1995 or 1998	**1.24	*1.17	*1.01*	*1.35*	***1.45	***1.41	*1.21*	*1.64*
20%+ of 1995 staff were managers	1.11	1.11	*0.92*	*1.34*	1.19	1.18	*0.97*	*1.42*
20%+ of 1995 staff were part time	1.12	1.14	*0.97*	*1.34*	*0.82	*0.83	*0.71*	*0.98*

[1] unadjusted for factors other than size and industry; [2] Adjusted for all factors in the table other than training; [3] The reference group. Odds ratio is 1 by definition.

Statistical Significance is as follows: * P<0.05, ** P<0.01, *** P<0.001

The training variable was not included in the overall model because of a relatively poor response rate to this question (about a quarter of the sample did not answer the question). To have included it in the full model the sample would have cut the sample size dramatically.

Conclusions

The results section of this paper painted a picture of the associations between gazelles and the different business characteristics considered. It examined how these associations differ across size and industry groups. Different statistical models will sometimes give different answers, but in this case there is reasonable agreement between the results of the log linear models and the logistic regressions. Where the two methods agree about an explanatory variable, one can have more confidence that there is a relatively strong association between that variable and the likelihood of a firm being a gazelle over the period.

Firms most likely to be *turnover gazelles* were in the *Construction*, *Property and business services*, and *Finance and insurance* industries. Firm size played no role in predicting strong turnover growth, although younger businesses were more likely to grow strongly. There were strong positive associations between turnover growth and business planning, staff training in 1998 and innovation. Family businesses appeared slightly less likely to have grown rapidly.

Firms most likely to be *employment gazelles*, were in the *Construction* and *Accommodation, cafes and restaurants* industries. The smallest firms were more likely to have recorded strong proportional employment growth while those business aged 10 years or less in 1995 were more likely to have grown quickly. Firms with business plans, that trained their staff in 1998 or were innovative were more likely to have seen employment growth. Family businesses were again less likely to have grown.

The links between most firm characteristics and business growth are complicated. They vary in strength and sometimes direction amongst different industries and size groups. The links described above were particularly notable and, although with the data available it is not possible to prove that these characteristics led to growth, we can conclude that they were strongly associated with it. If policy makers or investors are looking to pick businesses that are likely to grow quickly, this analysis tells us they would do well to pay close attention to young firms (that were not family businesses) who planned and were innovative.

Appendix 1 Log Linear Models

Consider the simplest case of the **i** *x* **j** different probabilities, P_{ij} , of *employment gazelles* being found in each of the 22 categories of industry and size (i=11 industries *x* j=2 size divisions). If the 22 probabilities in the *Yes* column are known, they specify the probabilities in the *No* column, because the two numbers must add to 1 (in each of the 22 categories, a firm is either a gazelle, with probability P_{ij}, or it is not, with probability $1-P_{ij}$).

In order to see whether any effects due to industry and size act independently, one considers the log linear model

(1) $\text{Log}\,(P_{ij}/1-P_{ij}) = A + B_i + C_j + D_{ij}$

where A is the overall mean, B_i is the effect (deviation from the mean) of the i'th industry, C_j is the effect of the j'th size group and D_{ij} is an interaction effect of the i'th industry with the j'th size.

This full (or saturated) model will precisely describe the table above (because it produces 22 equations in 22 unknowns).

Probabilities of being an empoyment gazelle in any particular industry/size group

Industry	***Size***	**Employment Gazelles**	
		Yes	***No***
Mining	*Small*	$P_{1,1}$	$1-P_{1,1}$
	Other	$P_{1,2}$	$1-P_{1,2}$
Manufacturing	*Small*	$P_{2,2}$	$1-P_{2,2}$
	Other	$P_{2,2}$	$1-P_{2,2}$
Construction	*Small*	$P_{3,1}$	$1-P_{3,1}$
	Other	$P_{3,2}$	$1-P_{3,2}$
Wholesale Trade	*Small*	$P_{4,1}$	$1-P_{4,1}$
	Other	$P_{4,2}$	$1-P_{4,2}$
Retail Trade	*Small*	$P_{5,1}$	$1-P_{5,1}$
	Other	$P_{5,2}$	$1-P_{5,2}$
Accommodation, Cafes & Restaurants	*Small*	$P_{6,1}$	$1-P_{6,1}$
	Other	$P_{6,2}$	$1-P_{6,2}$
Transport & storage	*Small*	$P_{7,1}$	$1-P_{7,1}$
	Other	$P_{7,2}$	$1-P_{7,2}$
Finance & Insurance	*Small*	$P_{8,1}$	$1-P_{8,1}$
	Other	$P_{8,2}$	$1-P_{8,2}$
Property & Business Services	*Small*	$P_{9,1}$	$1-P_{9,1}$
	Other	$P_{9,2}$	$1-P_{9,2}$
Cultural & Recreational Services	*Small*	$P_{10,1}$	$1-P_{10,1}$
	Other	$P_{10,2}$	$1-P_{10,2}$
Personal & Other Services	*Small*	$P_{11,1}$	$1-P_{11,1}$
	Other	$P_{11,2}$	$1-P_{11,2}$

One can test to see whether the effects of size and industry act independently (that is whether the D_{ij} terms might really be zero) by comparing this model with the reduced model

(2) $\text{Log}\,(P_{ij}/1\text{-}P_{ij}) = A + B_i + C_j$

One can go on to test whether the effects of size and industry are each significant by eliminating each term and comparing the fit of successive models with the more complex models. Similar, albeit more complicated, models can be generalised for higher dimensions of cross classifications. So if the sample were broken down by *i* industries, *j* sizes and *k* age groups, we would have a saturated model:

(3) $\text{Log}\,(P_{ij}/1\text{-}P_{ij}) = A + B_i + C_j + D_{ij} + E_{ik} + F_{jk} + H_{ijk}$

Once again we can test to see whether the matrix of 3-way interaction terms (H_{ijk}) is zero, and, if so, whether any matrices of 2-way terms are zero.

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FINANCIAL PERFORMANCE AND THE SIZE OF A BUSINESS

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Financial performance of firms, as represented through a number of financial ratios, is analysed to see whether it provides guidance in classifying firms by size. Regression techniques are applied to a large Australian sample of more than 2000 businesses in the manufacturing sector and 844 businesses in the wholesale sector covering the whole range of firm sizes (measured in terms of total employment). The paper concludes that financial performance and firm size are not closely related, although there is some evidence to suggest that the employment-based divide between large and non-large firms in the Australian manufacturing sector might lie around the 80 employees level of firm size. There was no discernable relationship for the wholesale sector.

Introduction

Businesses are classified by size for a multitude of purposes by law makers, researchers, data collection agencies and others. Whatever the purpose, there is at least an implicit intent that businesses which fall into different size classifications will somehow be different from one another.

This paper examines a large Australian database to see whether the size definitions used by the Australian Bureau of Statistics (ABS) reflect fundamental and observable differences in the characteristics and behaviour of firms. In particular, it explores for relationships between firms financial performance and their size to see whether relative financial performance is suggestive of boundaries between different firm size classifications. It follows a similar analysis of the definitions of a small business used by the United States Small Business Administration (Osteryoung *et al*, 1995).

Small Business Definitions

There is no unanimity in the business size definitions used across countries, or even by different organisations and groups within a country (Cross, 1983; Ganguly, 1985). Definitions differ in the break points they employ, and also in the underlying basis used for classification.

Employment is the most frequently used basis for business size classifications, but business assets and sales revenue are alternative measures that are sometimes used. Australian research has shown that these different measures are not interchangeable. Businesses may be classified differently depending on whether employment, assets or sales revenue is used to measure their size (Forsaith *et al* 1994, 1995). This result is not unexpected given the different production functions used by different firms and different industries.

Many people are more comfortable with a qualitative definition of a small business based on common characteristics of the sector. We all know a small business when we see one. The most frequently quoted such definition in Australia is that from the Beddall Inquiry (1990) which suggested that a business is small if it has the following characteristics:

- It is independently owned and operated
- It is closely controlled by owner-managers who contribute most or all of the operating capital; and
- The principal decision-making functions rest with the owner-managers.

Bannock (1981) considers owner-management, where the owners "participate in all principle decisions and will, typically, know what is going on in all parts of their business" (p27), to be a necessary but not sufficient condition for a firm to be classified as small. He argues that it should also have only a small share of its market and should not be able to access the public capital markets.

Osteryoung and Newman (1993) suggested that a business be defined as small if its shares are privately held and are not available to the public at large, <u>and</u> if the owners must personally guarantee all financing of the business.

Exceptions can be found to every rule and expediency has generally required the adoption of some quantitative definition where numbers can be used as the basis for size classification. As Bannock (1981, p28) observes, "small firms are difficult to define because in the market economy the unit organisation of economic activity is a continuum …with no clear break points… In practice, economists and legislators alike are obliged to make arbitrary statistical definitions". Nevertheless, it is important that the definitions chosen are based on as much information as possible, which provides the basis and rationale for this (and other) research on this topic.

Osteryoung *et al* (1995) examined the US Small Business Administration (SBA) definitions for the manufacturing and wholesaling sectors. The SBA defines a manufacturing business as small if it has 500 or fewer employees and a wholesaling business as small if it has 100 or fewer employees. They concluded that both of these break points were too high. Naturally occurring break points based on differences in characteristics, operations and financial performance appeared to be well below those used by the SBA. However, the overall explanatory power of the relationships they tested was low.

The Australian Bureau of Statistics also uses total employment as the basis for business size classifications. For some of their collections, the ABS differentiates between the manufacturing and services sectors. A business is considered small in manufacturing if it employs fewer than 100, while a services business is small if it employs fewer than 20. This definition of small suggests that a single break point between medium and large businesses in Australia could be 200 total employment. In other collections, the ABS uses a larger number of size classifications comprising micro-businesses (0-4 employees), other small businesses (5-19 employees), medium businesses (20-99 employees), and large businesses (100 or more employees).

This paper explores the financial ratios of Australian firms to see whether they vary with firm size and whether financial performance, as measured by these ratios, sheds any light on the appropriateness of firm size boundaries.

Methodology

This study utilised data from the Australian Small and Medium Enterprises Database (AUSSMED). This is a business longitudinal database collected by the ABS, although only data from 1996-97 financial year were used for this study. (This contrasts with Osteryoung *et al* (1995) who used repeated annual observations of the same firms to increase their sample size ten-fold.) Following Osteryoung *et al* (1995), only two sectors, manufacturing and wholesaling, were examined. The sample sizes were 2051 firms in manufacturing and 844 firms in wholesaling.

The AUSSMED survey obtains data on the location, activity, employment operations and financial details of businesses. This enables a number of financial performance ratios to be calculated and for any relationship between the size of the business (in terms of numbers of employees) and financial performance to be examined across all firms in the survey.

The financial performance ratios used in this study are the current ratio, inventory turnover ratio, total asset turnover ratio, profit margin, debt ratio, return on assets and return on equity. These were similar to the financial ratios reported by Osteryoung *et al* (1995), except that the receivables turnover ratio could not be examined because data on accounts receivable were not collected by the ABS. *A priori*, it might be expected that these ratios might vary with firm size; eg , larger firms might be able to economise on inventory holdings, or achieve higher profitability by being able to spread overheads more widely. If such size-related relationships were found to be sufficiently strong, they might provide guidance in classifying firms by size.

Inspection of the sample data showed that the tails of the distributions had extreme minimum and maximum values which had a serious impact on the observed means of the financial ratios. To remove these distortions, winsorisation procedures were applied to the bottom 1% and top 1% of observations. By this technique, these firms were not removed from the sample, but the values of their ratios were constrained to those of the first and ninety-ninth percentile firms respectively. This still allows their low or high ratios to influence the analysis, but not to the full extent that the extreme values of the raw data would allow (Sprent, 1993).

The treatment of employees was also examined to see whether the sample statistics were sensitive to the fulltime/parttime split of employees. This appeared to have no impact on the results and so the distinction has not been made.

The different effects of incorporated and unincorporated businesses on the data was also examined. Sample statistics were analysed for all firms and for incorporated firms. (Unincorporated firms – sole proprietorships and partnerships – were not analysed separately because very few of them are large employers so that an adequate range of business size could not be examined.) This distinction was of no consequence for the current, inventory turnover or total assets turnover ratios, but including unincorporated businesses had the effects of substantially increasing the mean values for the gross profit margin, return on assets and return on equity and decreasing the gearing ratio. Therefore, both the all firms and incorporated firms data sets were included in the study. (Even the incorporated data set alone provides wider coverage of firm size than the Osteryoung *et al* (1995) study which only included publicly traded firms.)

The size category breakdown of these samples is in table 1.

Table 1 Sample Size by Numbers of Employees

Numbers of Employees	Numbers of Firms	
	Manufacturing	Wholesaling
1-5	413 (273)	171 (130)
6-20	537 (486)	232 (220)
21-50	490 (469)	211 (205)
51-100	256 (250)	129 (127)
101-200	122 (120)	45 (44)
200+	233 (231)	56 (56)
Total	2051 (1829)	844 (782)

(sample sizes of incorporated firms only shown in parentheses)

Each of the financial performance ratios listed above was regressed separately on employment to see the extent to which firm size differences explained differences in financial performance ratios. The null hypothesis was that the financial ratios would not be a function of the number of employees.

Next, a series of multiple regressions of different pairs of size groups regressed on all of these financial performance ratios together was performed. This was to see whether financial performance explained the differences in size, and allowed the size boundaries currently used by the ABS to be tested. Firms within a size group classed as small or medium (eg, 1-10, 11-20, 21-30 etc) were given a dummy value of one and those classed as large (eg, having 200+ employees) were assigned a dummy value of zero. Firms not in either of the groups being analysed in a particular regression were given missing values.

To examine whether differences in firm size were related to differences in financial performance, regressions of the following type were performed between each of the small or medium firm size groups and the large firm size group:

$$\text{Size dummy} = a + b_1(\text{current ratio}) + b_2(\text{inventory turnover}) + b_3(\text{total asset turnover}) + b_4(\text{gross profit margin}) + b_5(\text{return on assets}) + b_6(\text{return on equity}) + b_7(\text{debt asset ratio})$$

Other boundaries for large firms of 100, 50 (and for wholesaling, 20) employees were also analysed. The regression output was also examined to see whether alternative boundaries might be more clearly suggested by the financial ratios (ie, “natural” size boundaries were sought).

Results

The sample statistics for each of the samples are presented in Table 2.

Table 2 Sample Statistics

Manufacturing (all firms)

Ratio	N	Mean	Standard error
Current	2051	1.7	0.06
Inventory turnover	1912	37.0	1.98
Total assets turnover	2051	3.5	0.09
Gross profit margin (%)	2051	61.2	0.50
Return on assets (%)	2051	25.9	1.60
Return on equity (%)	2051	31.1	8.07
Debt to assets ratio (%)	2051	63.1	1.43

Wholesaling (all firms)

Ratio	N	Mean	Standard error
Current	844	2.3	0.15
Inventory turnover	844	31.9	3.14
Total assets turnover	828	3.1	0.10
Gross profit margin (%)	844	38.8	0.86
Return on assets (%)	844	10.4	1.37
Return on equity (%)	844	4.5	10.1
Debt to assets ratio (%)	844	63.0	1.63

N = number of firm observation used in each regression

Table 3 shows the results of the regressions of each of the financial ratios on the number of employees. the manufacturing and wholesaling results are shown separately and are the results for all firms. The only equations found to be statistically significant were for total asset turnover and gross profit margin and for the manufacturing sector only. (This was also the case when incorporated firms only were analysed.) Moreover, all of the adjusted R^2 are extremely low. This suggests that the number of employees is a poor explanatory variable for the financial ratios of firms, for both the manufacturing and wholesaling sectors.

These results are reasonably consistent with those of Osteryoung *et al* (1995). While Osteryoung *et al* (1995) found more equations to be significant, only two equations for the wholesaling sector had adjusted R^2 of any worth.

The Australian data shows even less sign of a relationship than the United States data and this could possibly be due to the much wider range of firm size used in this Australian study. As Osteryoung *et al* (1995, pp85-6) acknowledge, their study being confined to publicly traded companies only included firms that on “almost all definitions…would not be considered small”.

Table 3 Regression Analysis of Firm Financial Ratios with Number of Employees

Dependent variable = a + b(number of employees) + error term

Dependent variable	Manufacturing firms			Wholesaling firms		
	a (standard error)	b (standard error)	Adj. R^2 (F value)	a (standard error)	b (standard error)	Adj. R^2 (F value)
Current ratio	1.682 (0.068)*	0.0003 (0.0007)	0.0004 (0.157)	2.301 (0.150)*	-0.002 (0.003)	-0.0008 (0.320)
Inventory turnover ratio	37.29 (2.014)*	-0.016 (0.0007)	0.0079 (13.312)	32.20 (3.242)*	-0.024 (0.0739)	-0.0011 (0.108)
Total assets turnover ratio	3.57 (0.096)*	-0.002 (0.0009)#	0.0021 (5.217)#	3.13 (0.103)*	-0.0006 (0.0023)	-0.0011 (0.065)
Gross profit margin	0.619 (0.005)*	0.0002 (0.0001)*	0.0040 (9.264)*	0.391 (0.009)*	-0.0003 (0.0002)	0.0012 (1.980)
Return on assets	0.263 (0.016)*	-0.0003 (0.0002)	0.0008 (2.623)	0.104 (0.014)*	-0.0001 (0.0003)	-0.0012 (0.024)
Return on equity	0.312 (0.082)*	0.0000 (0.0008)	-0.0005 (0.004)	0.035 (0.104)*	0.0009 (0.0024)	-0.0010 (0.129)
Debt to assets ratio	0.632 (0.014)*	-0.0000 (0.0001)	-0.0005 (0.049)	0.627 (0.017)*	0.0002 (0.0004)	-0.0007 (0.380)

* = significant at 1% level
# = significant at 5% level

The results of the multiple regressions using size-based dummy variables are presented in Table 4. The results presented are for all firms, although the sample of incorporated firms showed a similar pattern of results. Initially these regressions compared large firms employing 200+ persons with smaller size groups.

The regressions for manufacturing firms suggest that the 200+ employees threshold is too high a threshold for large firms. The broad pattern of the results suggests that firms in the manufacturing sector employing up to 80 are different from those with higher employment levels. This was again revealed when the threshold for large firms was reduced to 100, the conventional statistical divide between small and large firms in the manufacturing sector that has been used in Australia. All of the individual employee size groups up to 80 employees, when regressed against firms employing more than 100, were significant at the 5% level, with all but the 51-60 employees range also being significant at the 1% level. The multiple regressions were then performed on a large/non-large divide of 80 employees, and the adjusted R2 and the significances of the F-values were virtually the same as where 100 employees was the boundary.

The adjusted R^2 for the regressions were generally below 0.1 for the regressions where 200 was the threshold for large firms. The adjusted R^2 tended to be higher when the threshold for large was reduced to 100.

The regressions for the wholesale sector cannot be interpreted in a meaningful way. This appears to confirm the earlier evidence in this study indicating the absence of any statistical relationship between financial ratios and firm size in the Australian wholesale sector.

Table 4 Regression Results Comparing the Financial Ratios of Different Firm Size Groups with Large Firms (200+employees)

$$\text{Size dummy} = a + b_1(\text{current ratio}) + b_2(\text{inventory turnover}) + b_3(\text{total asset turnover}) + b_4(\text{gross profit margin}) + b_5(\text{return on assets}) + b_6(\text{return on equity}) + b_7(\text{debt asset ratio})$$

Firm Size Group	Manufacturing		Wholesaling	
(employees)	Adjusted R^2	F ratio	Adjusted R^2	F ratio
1-10	0.0008	1.097	-0.0199	0.090
11-20	0.0326	3.494*	-0.0282	0.319
21-30	0.0279	2.810*	-0.0345	1.705
31-40	0.0567	4.384*	-0.0126	0.781
41-50	0.1270	8.107*	0.0844	2.475#
51-60	0.0301	2.390#	0.0761	2.118#
61-70	0.0551	3.417*	0.1933	3.876*
71-80	0.0365	2.501#	0.0940	2.216#
81-90	0.0056	1.214	0.0291	1.321
91-100	-0.0029	0.891	-0.0315	0.703
101-125	0.0235	0.0593	0.1347	2.535#
126-150	0.0362	2.428#	0.1289	2.459
151-175	0.0093	1.337	0.2271	3.602*
176-200	0.0645	3.482*	0.2137	3.524*

Conclusions

The results obtained from this Australian data are broadly consistent with those of Osteryoung *et al* (1995) for US data. They suggest that although financial ratios are not good indicators of firm size, the divide of 100 employees between large and not large that is applied to some Australian statistical collections in the manufacturing sector may not be too far from the mark. No guidance is provided for the wholesale sector statistical collections.

Despite its limited findings in terms of delineating firms of different size, this study has been important for a number of reasons. It has tested for size related financial performance relationships on Australian data and has employed a large database to avoid the possibility of any serial correlation. Moreover, it has been able to apply the methodology used to a much wider range of firm sizes than previous international research on this issue.

This study has found the relationships to be somewhat weaker that those of Osteryoung *et al* (1995) and this may be because of the much wider range of firm sizes studied.

Caution should be exercised in interpreting the findings because of the low overall explanatory power of these financial performance variables on business size differentials. Only a weak link appears to exist between firm size and firm financial performance as measured by financial ratios. This suggests that other firm characteristics might be more useful in classifying business by size.

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Marketing Practices of Chinese Small Firms:

A Comparison among State-owned, Collective and Private Enterprises

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SUMMARY

This paper reports the survey results of marketing practices of 163 Chinese small firms in China. The findings suggest that the specific marketing practices of state-owned, collective and private small firms in China are somewhat different from each other.

INTRODUCTION

It is generally agreed that small firms contribute to economic development. This assertion is also applicable to China because small firms have played, for some time, a very important role in the country's economic growth [1]. It is expected that the private sector, mostly small firms, will increase its share of the nation's gross value of industrial output from 0.8% in 1957 to 13.4% in 2000, whereas the state sector will drop from 53.8% to 27.3% over the same time period [2].

The research findings of Siu and Kirby [3] reveal that broad western marketing principles are not necessarily fully applicable to, and suitable for, some specific socio-cultural contexts. Despite the importance of small firms in China's economic growth, no major research study has been conducted to examine exactly how and to what extent these small firms have managed to survive, grow and succeed, or more specifically, how they make marketing decisions, promote their products and maintain competitiveness. To date, scholarly publications on the management

of small firms in China are few and rare. Some researchers have adopted macro, non-managerial perspectives, such as regional studies [4, 5] urban development [6], political studies [7], sociology [8, 9, 10] and economic development [11, 12, 13]. Also, some management researchers conclude that factors, such as the competitive environment [14], psychological traits [15] and the entrepreneurial spirit [16, 17], are essential to the success of small firms in China. However, management researchers have not acknowledged the effects of economic ownership and also the contribution of marketing to Chinese small firms, a factor being regarded by management scholars [18, 19] as an essential ingredient for business operations.

Siu and Kirby [20] suggest an integrative approach to advance small firm marketing theory and have a better understanding of small firm marketing implementation process. Thus, this research blends the process model and the contingency model in studying Chinese small firm marketing. The marketing process model proposed by Brooksbank [21] has been adopted for understanding the marketing activities of small firms in China. In addition, the study embraces the contingency model used by Siu and Kirby [3] to identify the marketing practices of different economic ownership.

RESEARCH QUESTIONS

The paper examines a number of questions, namely: -

(1) What is the specific approach of Chinese small firms to marketing?

(2) How do the marketing practices and principles of Chinese state-owned, collective and private enterprises, differ, if at all, from each other?

RESEARCH OBJECTIVES

Researchers [22, 23] argue that the traditional content approaches using formal planning procedures and logical flow plan models are inappropriate to the reality of planning marketing. Piercy and Morgan [24] state that marketing should be examined from the context approach which places emphasis on the behavioural process in making marketing decisions. This study will follow the context approach which has been suggested by some small business researchers [25, 26] to investigate small firm marketing in China. Specifically, the objectives of this proposed

research are to:

(1) examine the extent to which marketing has actually been adopted by different types of economic ownership of small firms in China;

(2) compare and contrast the marketing practices of state-owned, collective and private Chinese small firms.

RESEARCH DESIGN

Churchill [27] suggests using descriptive research when the research purpose is to describe the characteristics of certain objects. Nevertheless, Ferber, Blankertz and Hollander [28] advocate that a descriptive study does not mean that it is simply a fact-gathering expedition, rather it is the glue of explanation and understanding, and also the framework of theory. Thus, the descriptive research method was used for this research. The survey research method, a branch of the descriptive research used for obtaining information from respondents by asking a variety of questions, has been selected. There are three common survey administered methods -- telephone interviews, personal interviews and mail questionnaires. Though the personal survey is widely criticised (moderate response rates, a relatively high interviewer-interviewee bias and relatively expensive), it has proven to be a valuable method of collecting data in China [29, 30]. More specifically for this research, it allows the researcher to collect a great deal of data relating to the marketing process and decisions. The confidential assurance offered by the interviewer provides a favourable atmosphere for the respondents to give sensitive data, such as relative performance in profits, sales and return on investment compared with their major competitors. This helps increase the response rate. Thus, a personal interview survey method is used for this study.

Sampling Frame Design

Rosen [29] and Yau et al. [30] query the sampling frame and the appropriateness of contact in survey research in China. Given that there is no up-dated directory relating to small firms in China and the preliminary nature of this research, a quota sampling approach is adopted. Guangdong, the economic hub at South China and also the province abundant in small enterprises, is purposively selected as the sampling province at the first stage. Seven major cities, namely Guangzhou, Swatow, Shunde, Zhaoxing, Dongguan, Shenzhen and Foshan were conveniently selected as the sampling cities at the second stage. A quota sampling approach was used. 30 companies were drawn from each city and this resulted in a sample size of 210. 189 companies were successfully interviewed. Characteristics of the

respondents are shown in Figure 1.

Figure 1 : Profiles of Respondents

Cities			**Employment size**		
Guangzhou	28	14.8%	1-9	10	6.1%
Swatow	29	15.3%	10-49	42	25.2%
Shunde	30	15.9%	50-99	34	20.2%
Dongguan	30	15.9%	100-199	42	22.7%
Shenzhen	29	15.3%	200-499	44	25.8%
Foshan	21	11.1%	500 or above	16	8.5%
Zhaoxing	22	11.6%			
Company			**Turnover**		
State-owned	50	26.6%	Below 100,000	19	10.1%
Collective	63	33.5%	100,001-500,000	15	7.9%
Private	75	39.9%	500,001-1,000,000	12	6.3%
			1,000,001-3,000,000	37	19.6%
Business			3,000,001-6,000,000	24	12.7%
Manufacturing industrial products	68	36.0%	6,000,001-10,000,000	22	11.6%
Manufacturing consumer products	93	49.2%	10,000,001-30,000,000	21	11.1%
Services industries	11	5.8%	30,000,001-60,000,000	12	6.3%
Distribution & Retailing	12	6.3%	60,000,001-100,000,000	16	8.5%
Others	5	2.6%	100,000,001-300,000,000	11	5.8%

The Instrument

The questionnaire was developed from the literature [3, 21, 26, 31, and 32] to collect information on basic company details, marketing practices and the performance of small firms. To eliminate translation bias, the questionnaire was translated into Chinese and back translated into English. The questionnaires were administered with the assistance from a research team consisting of professors of universities in China. They prepared a simplified Chinese character questionnaire, arranged for questionnaire printing, travelled between cities, trained interviewers, and coordinated data collection.

Data Analysis

The 189 returned questionnaires were further screened by the criteria proposed by Brooksbank [33] for small and medium sized industries. Firms with fewer than 500 employees and an annual turnover less than or equal to Reminbi Yuan 300 million were selected. However, Siu and Martin [34] suggest that inter-sectoral business diversification of Chinese small firms is commonplace in a Chinese socio-cultural environment. Accordingly, the product strategy proposed by Brooksbank [33] was not adopted as one of the screening criteria. Also, quoted listed companies were not selected as they did not possess the characteristics of the small business, as suggested by Osteryoung and

Newman [35]. Thus, 163 firms were eventually analysed. The Chi-square test in the CROSSTABS routine of the SPSS/PC+ 4.1 computer software package was used to identify the differences between performers across various marketing practices.

FINDINGS

Business Philosophy

From Table 1 (Chi-square value = 0.94413, p value = 0.62371), it would seem that at the 95 percent confidence level, no statistically significant relationship exists in small firms, between the type of economic ownership and the role of marketing within corporate planning. The distribution appears to suggest that the sample does not give marketing a higher priority (the leading of joint leading role) than the other business functions in their overall approach to business.

Table 1: Company Nature by Role of Marketing in Corporate Planning

	% State-owned (N=34)	% Collective (N=58)	% Private (N=71)
Marketing has the leading and joint leading role	32.4	29.3	23.9
Marketing has a subordinate or no role	67.6	70.7	76.1

Chi-square = 0.94413, D.F. = 2, P = 0.62371

As Table 2 (Chi-square value = 5.89624, p value = 0.05244) reveals, the results of the survey indicate at the 90 percent confidence level a statistical relationship exists between the type of economic ownership and an approach to marketing based on the prior analysis of market needs. 70.4% of the private firms reported that they made what they could sell to whoever would buy, or placed major emphasis on advertising and selling. These findings lend support to the notion that state-owned and collective Chinese small firms are more likely to define their marketing activities as customer-driven, compared with their private counterparts.

Table 2: Company Nature by Company Approach to Marketing

	% State-owned (N=31)	% Collective (N=56)	% Private (N=71)
Make what we can and sell to whoever will buy / place major emphasis on advertising and selling	54.8	50.0	70.4
Place major emphasis on prior analysis of market needs	45.2	50.0	29.6

Chi-square = 5.89624, D.F. = 2, P = 0.05244

Strategic Analysis

According to the findings presented in Table 3 (Chi-square value = 10.39723, p value = 0.00552) a statistically

significant relationship exists between the type of economic ownership and the extent of strategic marketing planning. 74.1% of the collective enterprises restricted their marketing planning to annual budgeting or did little or no planning, whereas about half of the state-owned enterprises (47.1%) and the private enterprises (53.5%) used strategic marketing planning. The present evidence shows that private and state-owned Chinese small firms are more strategic-oriented in marketing planning than collective Chinese small firms are.

Table 3: Company Nature by Extent of Strategic Marketing Planning

	% State-owned (N=34)	% Collective (N=58)	% Private (N=71)
Strategic or annual marketing plan	47.1	25.9	53.5
Annual Budgeting or no planning	52.9	74.1	46.5

Chi-square = 10.39723, D.F. = 2, P = 0.00552

Table 4 (Chi-square value = 2.27644, p value = 0.32039) summarises the responses across the five types of situation analysis: (1) internal (company); (2) competitor; (3) market; (4) customer; and (5) wider business environment. It would seem that there is no statistically significant relationship between the type of economic ownership and the degree of importance to comprehensive situation analysis.

Table 4: Company Nature by Importance Attached to a Comprehensive Situation Analysis

	% State-owned (N=34)	% Collective (N=56)	% Private (N=70)
High Importance	32.4	48.2	40.0
Average or Low importance	67.6	51.8	60.0

Chi-square = 2.27644, D.F. = 2, P = 0.32039

Tables 5 and 6 summarise the responses to the awareness and usage of six marketing planning tools: the SWOT (Strengths, Weaknesses, Opportunities, and Threats) analysis; the Experience Curve; the PLC (Product Life Cycle) analysis; Portfolio Planning Matrices; the PIMS (Profit Impact on Sales) study; and the Marketing Audit, respectively. The results show that there are no statistically significant relationships between the type of economic ownership and the awareness (Chi-square value = 3.82874, p value = 0.14743) and usage of (Chi-square value = 3.59973, p value = 0.16532) the six marketing planning tools.

Table 5: Company Nature by Awareness Levels of Six Marketing Planning Tools

	% State-owned (N=31)	% Collective (N=58)	% Private (N=68)
High	19.4	37.9	26.5
Average or Low	80.6	62.1	73.5

Chi-square = 3.82874, D.F. = 2, P = 0.14743

Table 6: Company Nature by Usage Levels of Six Marketing Planning Tools

	% State-owned (N=31)	% Collective (N=56)	% Private (N=70)
High Importance	16.1	28.6	15.7
Average or Low importance	83.9	71.4	84.3

Chi-square = 3.59973, D.F = 2 P = 0.16532

As shown in Table 7 (Chi-square value = 9.43279, p value = 0.05115), the survey revealed a statistically significant relationship between the three types of economic ownership and their approaches to planning. Half of the state-owned enterprises (50.0%) adopted a more proactive approach to planning - forecasting and planning accordingly. Nevertheless, 44.1% of the private enterprises appear to monitor the environments and adapt accordingly. Three approaches to planning were adopted over evenly by collective enterprises. Thus the results suggest that state-owned and collective Chinese small firms adopt a more proactive rather than reactive approach to the future.

Table 7: Company Nature by Approach to Planning for the Future

	% State-owned (N=34)	% Collective (N=57)	% Private (N=68)
Monitor and then adapt	29.4	29.8	44.1
Forecast and plan accordingly	50.0	33.3	39.7
Plan and make it happen	20.6	36.8	16.2

Chi-square = 9.43279, D.F. = 4, P = 0.05115

Table 8 (Chi-square value = 3.45834, p value = 0.17743) summarises the responses concerning the frequency of using self-generated market research. On the basis of this evidence, it would seem that at the 95 percent confidence level no statistically significant relationship exists between the type of economic ownership and the frequency of using self-generated market research. Notably, however, 65.4% of the sample reported that usage of self-generated market research was low. The results do not lend support to the notion that there is a difference in usage marketing research in marketing planning activities among three types of small firms. In Table 9 there are some extremely low or no frequency scores which make the application of the Chi-square test dubious. On closer inspection, it appears that there is no relationship between the type of economic ownership and usage of commissioned-in market research.

A majority of firms (98.1% of the sample) reported that the use of commissioned-in market research was also low. The results suggest that no significant differences are found between the three types of company. Thus, the results suggest that Chinese small firms neither use formal or informal marketing research methods.

Table 8: Company Nature by Use of Research Carried Out by Company

	% State-owned (N=34)	% Collective (N=58)	% Private (N=70)
At least a quarter	47.1	34.5	28.6
Half a year or above	52.9	65.5	71.4

Chi-square = 3.45834, D.F. = 2, P = 0.17743

Table 9: Company Nature by Use of Commissioned-in Market Research

	% State-owned (N=29)	% Collective (N=56)	% Private (N=69)
At least a quarter	0	1.8	2.9
Half a year or above	100.0	98.2	97.1

As there is an empty cell, Chi-square test is not used here.

Marketing Objectives

As Table 10 (Chi-square value = 12.56661, p value = 0.01360) reveals, there is a significant relationship at the 5 percent level of significance between the type of economic ownership and the time horizon in setting objectives. 50% of the state-owned enterprises and 47.4% of the collective enterprises adopt medium term time horizons in setting profit objectives, whilst 48.5% of the private enterprises have shorter term or no objectives. There appears to be strong support that state-owned and collective Chinese small firms tend to set longer-term profit objectives, compared with private firms. In Table 11 there are some extremely low frequency scores which make the application of the Chi-square test rather dubious. It appears that there is no relationship between the type of economic ownership and nature of marketing objectives. The distribution shows that Chinese small firms adopt defensive (No Objective, Defend or Maintain) and conservative (Steady Growth) marketing objectives.

Table 10: Company Nature by Profit Objectives

	% State-owned (N=34)	% Collective (N=57)	% Private (N=66)
Longer Term	17.6	31.6	13.6
Medium Term	50.0	47.4	37.9
Shorter Term or No Objective	32.4	21.1	48.5

Chi-square = 12.56661, D.F. = 4, P = 0.01360

Table 11: Company Nature by Nature of Marketing Objectives

	% State-owned (N=34)	% Collective (N=58)	% Private (N=70)
Defensive: No objective, Defend or Maintain	52.9	48.3	42.9
Conservative: Steady Growth	38.2	46.6	48.6
Offensive: Aggressive Growth or Market Domination	8.8	5.2	8.6

As there are some extremely low frequency scores, Chi-square test is not used here.

Marketing Strategy

From Table 12 (Chi-square value = 1.39183, p value = 0.49862), it would seem that there is no statistically significant relationship between the type of economic ownership and strategic focus. The findings suggest that Chinese small firms adopt both raising volume and productivity improvement to achieve their marketing goals.

Table 12: Company Nature by Achievement of Marketing Objectives

	% State-owned (N=34)	% Collective (N=58)	% Private (N=70)
Expanding total market/Entering newly emerging market segments/Winning share from competitors	58.8	46.6	48.6
Focusing on cost reduction and productivity improvement	41.2	53.4	51.4

Chi-square = 1.39183, D.F. = 2, P = 0.49862

Tables 13 to 23 reveal statistically significant relationships, at 10 percent level of significance, between the type of economic ownership and superiority in four areas of the marketing mix - product design (Chi-square = 6.37419, p value = 0.04129), after sale service (Chi-square value = 4.77242, p value = 0.09198), credit and finance (Chi-square = 12.46607, p value = 0.00196), and price (Chi-square = 5.65320, p value = 0.05921).

The results show that private enterprises tend to enjoy a superior position over major competitors in product design (47.6%). State-owned and collective enterprises perform better in after sales service (52.9% and 52.6% respectively). Collective enterprises (52.6%) also perform better in credit and finance. Private enterprises (81.0%) tend to set the same or higher price level than other small firm counterparts.

There are no statistically significant relationships among the type of economic ownership and other variables, including product performance (Chi-square = 3.61723, p value = 0.16388), product quality (Chi-square = 2.04854, p value = 0.35906), personal selling (Chi-square = 1.02725, p value = 0.59832), advertising (Chi-square = 2.71611, p

value = 0.25716), company/brand reputation (Chi-square = 1.15517, p value = 0.56125), distribution outlet (Chi-square = 1.35519, p value = 0.50784), and agency support (Chi-square = 1.20708, p value = 0.54687). The findings suggest that Chinese small firms exhibit different strategies in competing with each other.

Table 13: Company Nature by Product Performance

	% State-owned (N=30)	% Collective (N=58)	% Private (N=65)
Superior	16.7	36.2	30.8
Same/Inferior	83.3	63.8	69.2

Chi-square = 3.61723, D.F. = 2, P = 0.16388

Table 14: Company Nature by Product Quality

	% State-owned (N=34)	% Collective (N=58)	% Private (N=65)
Superior	55.9	62.1	49.2
Same/Inferior	44.1	37.9	50.8

Chi-square = 2.04854, D.F. = 2, P = 0.35906

Table 15: Company Nature by Product Design

	% State-owned (N=33)	% Collective (N=57)	% Private (N=63)
Superior	21.2	38.6	47.6
Same/Inferior	78.8	61.4	52.4

Chi-square = 6.37419, D.F. = 2, P = 0.04129

Table 16: Company Nature by After Sales Service

	% State-owned (N=34)	% Collective (N=57)	% Private (N=63)
Superior	52.9	52.6	34.9
Same/Inferior	47.1	47.4	65.1

Chi-square = 4.77242, D.F. = 2, P = 0.09198

Table 17: Company Nature by Credit and Finance

	% State-owned (N=30)	% Collective (N=57)	% Private (N=61)
Superior	23.3	52.6	24.6
Same/Inferior	76.7	47.4	75.4

Chi-square = 12.46607, D.F. = 2, P = 0.00196

Table 18: Company Nature by Personal Selling

	% State-owned (N=33)	% Collective (N=56)	% Private (N=66)
Superior	36.4	44.6	36.4
Same/Inferior	63.6	55.4	63.6

Chi-square = 1.02725, D.F. = 2, P = 0.59832

Table 19: Company Nature by Advertising

	% State-owned (N=32)	% Collective (N=58)	% Private (N=62)
Superior	15.6	24.1	12.9
Same/Inferior	84.4	75.9	87.1

Chi-square = 2.71611, D.F. = 2, P = 0.25716

Table 20: Company Nature by Company/Brand Reputation

	% State-owned (N=34)	% Collective (N=58)	% Private (N=62)
Superior	47.1	44.8	37.1
Same/Inferior	52.9	55.2	62.9

Chi-square = 1.15517, D.F. = 2, P = 0.56125

Table 21: Company Nature by Distribution Outlet

	% State-owned (N=33)	% Collective (N=56)	% Private (N=63)
Superior	24.2	25.0	33.3
Same/Inferior	75.8	75.0	66.7

Chi-square = 1.35519, D.F. = 2, P = 0.50784

Table 22: Company Nature by Agency Support

	% State-owned (N=33)	% Collective (N=53)	% Private (N=62)
Superior	21.2	30.2	22.6
Same/Inferior	78.8	69.8	77.4

Chi-square = 1.20708, D.F. = 2, P = 0.54687

Table 23: Company Nature by Price

	% State-owned (N=33)	% Collective (N=54)	% Private (N=63)
Lower	30.3	38.9	19.0
Same/Higher	69.7	61.1	81.0

Chi-square = 5.65320, D.F. = 2, P = 0.05921

The results of Table 24 (Chi-square value = 4.11557, p value = 0.12774) show that there is no statistically significant relationship at the 95 percent level of confidence between the type of economic ownership and the approach to developing and marketing new products. The results indicate that Chinese small firms do not actively innovate in product development. Table 25 (Chi-square value = 7.43763, p value = 0.02426) shows that there is a statistically significant relationship between the type of economic ownership and the extent of innovation in introducing new ways of doing business. 73.5% of state-owned enterprises and 76.1% of private enterprises stick to the methods they have always used or watch their competitors and imitate their ideas, whereas about 45.6% of the collective enterprises lead the market in introducing new ways of doing business. Collective Chinese small firms tend to innovate more frequently in business practices. Thus the results suggest that collective enterprises tend to be more innovative than their state-owned and private competitors.

Table 24: Company Nature by New Product Development

	% State-owned (N=34)	% Collective (N=56)	% Private (N=71)
Do not do any/Imitate the Competitor	35.3	39.3	53.5
Actively develop and market new products ahead of competition	64.7	60.7	46.5

Chi-square = 4.11557, D.F. = 2, P = 0.12774

Table 25: Company Nature by New Business Practice

	% State-owned (N=34)	% Collective (N=57)	% Private (N=71)
We stick to the methods we have always used/Watch the competitors and if their new ideas work well then we imitate	73.5	54.4	76.1
We lead the market in introducing new ways of doing business	26.5	45.6	23.9

Chi-square = 7.43763, D.F. = 2, P = 0.02426

Marketing Organisation

Table 26 (Chi-square value = 16.77612, p value = 0.00023) reveals that there is a statistically significant relationship between the type of economic ownership and marketing organisational structure. 58.8% of the state-owned enterprises and 51.7% of collective enterprises adopted a pyramid organization structure, whereas 77.1% of the private enterprises replied that they adopted a flat organisation structure, that there was no middle management and all marketing staff reported directly to the senior marketing executive. Private Chinese small firms tend to have a

simpler marketing organisational structure.

Table 26: Company Nature by Marketing Organization Structure

	% State-owned (N=34)	% Collective (N=58)	% Private (N=70)
Pyramid	58.8	51.7	22.9
Flat	41.2	48.3	77.1

Chi-square = 16.77612, D.F. = 2, P = 0.00023

Tables 27 to 31 reveal statistically significant relationships between the type of economic ownership and marketing communication style in two types of the marketing communication flow methods -- opinion vented freely (Chi-square value = 7.38952, p value = 0.02485), and participative decision (Chi-square = 9.32859, p value = 0.00943). Most collective (79.3%) and private (84.3%) enterprises reported that they agreed with opinion vented freely, while state-owned enterprises (39.4%) did not agree. Chinese small state-owned (76.5%) and collective (82.8%) enterprises showed that they agreed with participative decision, whereas 41.2% of private firms did not agree with this. No differences emerged with encourage ideas, overlapping jobs, and temporary task force. The results appear to suggest that the Chinese small collective enterprises tend to use “flexible” and “open” marketing communication, instead of “fragmented” and “closed” communications.

Table27: Company Nature by Opinion Vented Freely

	% State-owned (N=33)	% Collective (N=58)	% Private (N=70)
Agree	60.6	79.3	84.3
Neutral/Disagree	39.4	20.7	15.7

Chi-square = 7.38952, D.F. = 2, P = 0.02485

Table28: Company Nature by Encouraging Ideas

	% State-owned (N=34)	% Collective (N=57)	% Private (N=68)
Agree	91.2	91.2	80.9
Neutral/Disagree	8.8	8.8	19.1

Chi-square = 3.62040, D.F. = 2, P = 0.16362

Table29: Company Nature by Participative Decision

	% State-owned (N=34)	% Collective (N=58)	% Private (N=68)
Agree	76.5	82.8	58.8
Neutral/Disagree	23.5	17.2	41.2

Chi-square = 9.32859, D.F. = 2, P = 0.00943

Table30: Company Nature by Overlapping Job

	% State-owned (N=34)	% Collective (N=57)	% Private (N=68)
Agree	23.5	35.1	38.2
Neutral/Disagree	76.5	64.9	61.8

Chi-square = 2.23583, D.F. = 2, P = 0.32696

Table31: Company Nature by Temporarily Task Force

	% State-owned (N=33)	% Collective (N=57)	% Private (N=68)
Agree	33.3	52.6	42.6
Neutral/Disagree	66.7	47.4	57.4

Chi-square = 3.28718, D.F. = 2, P = 0.19328

Marketing Control

Tables 32 to 35 reveal that there are no statistically significant relationships between the type of economic ownership and marketing control in four controlling devices -- customer satisfaction surveys (Chi-square value = 1.02850, p value = 0.59795); claims investigation (Chi-square value = 1.63148, p value = 0.44231); lost order analysis (Chi-square value = 3.09100, p value = 0.21321) and research into market share movement (Chi-square value = 4.43924, p value = 0.10865). Table 36 and 37 also reveal that no statistical relationship exists at the 95 percent confidence level between the type of economic ownership and the use of on-going marketing intelligence-gathering systems (Chi-square value = 6.43670, p value = 0.16882), and special marketing software packages (Chi-square value = 3.31921 p value = 0.19021). The collective picture drawn in Tables 32 to 37 shows that Chinese small firms neither make good use of marketing information systems, nor marketing control devices.

Table32: Company Nature by Customer Satisfaction Survey

	% State-owned (N=34)	% Collective (N=57)	% Private (N=71)
At least a quarter	35.3	45.6	39.4
Half a year or above	64.7	54.4	60.6

Chi-square = 1.02850, D.F. = 2, P = 0.59795

Table33: Company Nature by Claims Investigation

	% State-owned (N=33)	% Collective (N=57)	% Private (N=69)
At least a quarter	48.5	47.4	37.7
Half a year or above	51.5	52.6	62.3

Chi-square = 1.63148, D.F. = 2, P = 0.44231

Table34: Company Nature by Lost Order Analysis

	% State-owned (N=33)	% Collective (N=57)	% Private (N=69)
At least a quarter	57.6	59.6	44.9
Half a year or above	42.4	40.4	55.1

Chi-square = 3.09100, D.F. = 2, P = 0.21321

Table35: Company Nature by Research Market Share Movement

	% State-owned (N=34)	% Collective (N=58)	% Private (N=69)
At least a quarter	41.2	44.8	27.5
Half a year or above	58.8	55.2	72.5

Chi-square = 4.43924, D.F. = 2, P = 0.10865

Table 36: Company Nature by Usage of Marketing Intelligence Gathering Systems

	% State-owned (N=32)	% Collective (N=56)	% Private (N=70)
High	28.1	32.1	32.9
Average	46.9	57.1	40.0
Low or No Use	25.0	10.7	27.1

Chi-square = 6.43670, D.F. = 4, P = 0.16882

Table37: Company Nature by Use of Special Marketing Software

	% State-owned (N=34)	% Collective (N=58)	% Private (N=70)
Yes	11.8	15.5	5.7
No	88.2	84.5	94.3

Chi-square = 3.31921, D.F. = 2, P = 0.19021

Company Performance

Companies were classified according to a self-assessed measure, using information supplied on the questionnaire. Respondents were asked to report how, in their last financial year, their companies had performed (Better="1", The Same="2", Worse="3" or Don't Know="4") relative to major competitors on the following criteria:- profit, sales volume, market share, and return on investment. Those with a rating of 1 for all criteria were classified as "Higher Performers". "Average Performers" performed variously on the four indicators, whilst "Lower Performers" were companies with a rating of 3 or 4 on all four indicators. On this basis, 21 (12.9%) of the respondent firms were classified as "Higher Performers", 104 (63.8%) as "Average Performers" and 38 (23.3%) as "Lower Performers". Table 38 reveals that no statistical relationship exists at the 95 percent confidence level between company

performance and the type of economic ownership (Chi-square value = 5.26458, p value = 0.26121). Thus, it would suggest that economic ownership is not an essential factor contributing to success for the sample Chinese small firms.

Table 38: Company Performance by Company Nature

	% Higher (N=32)	% Average (N=56)	% Lower (N=70)
State-owned	23.8	22.1	15.8
Collective	28.6	40.4	26.3
Private	47.6	37.5	57.9

Chi-square = 5.26458, D.F. = 4, P = 0.26121

DISCUSSION

The research results suggest that state-owned and collective Chinese small firms are more likely to define their marketing activities as customer-driven, compared with their private counterparts. Private and State-owned Chinese small firms are more strategic oriented in marketing planning than collective Chinese small firms are. State-owned Chinese small firms adopt a more proactive rather than reactive approach to the future, compared with the private and collective enterprises. State-owned and collective Chinese small firms tend to set longer-term profit objectives. Also, the three types of firms exhibit different marketing practices in product design, after sales service, credit and finance and also price. State-owned and collective enterprises tend to compete more on after sales service and credit and finance, whereas private enterprises more on product design and higher price. Collective companies tend to be more innovative than their state-owned and private competitors. Private Chinese small firms tend to have a simpler marketing organisational structure, compared with that of the state-owned and collective enterprises. Chinese small collective firms use “flexible” and “open” marketing communication, instead of “fragmented” and “closed” communications. However, there is no difference among the three groups in company performance, marketing strategy formulation and implementation, and the use of strategic marketing planning tools. The results suggest that marketing in three types of economic ownership of Chinese small firms in China are somewhat different from each other. Figure 2 provides a detailed comparison among the marketing practices of three types of Chinese small firms.

Figure 2 : Marketing Practices of State-owned, Collective and Private Chinese Small Enterprises.

Marketing Practices	State-owned Enterprises	Collective Enterprises	Private Enterprises
Business Philosophies	Customer-driven	Customer-driven	Sales-driven
Marketing Planning	Strategic-oriented	Functional-oriented	Strategic-oriented

Approach to the Future	Proactive	Reactive	Proactive
Profit Objectives	Medium Term	Medium Term	Short-term
Marketing Strategies	Superiority in After Sale Service	Superiority in Credit and Finance	High Price; Superiority in Product Design
Innovation in Business Practices	Stick to Old Methods	Introduce New Ways Of Doing Business	Stick To Old Methods
Marketing Organisation	A Pyramid Structure	A Pyramid Structure	A Flat Structure

Much of the existing literature has emphasised Chinese ethnicity and culture as powerful determinants of the success of Chinese entrepreneurship. Researchers have identified family, dialect, and the Confucian value systems as peculiarly suited for business [36]. Though the cultural influences are acknowledged, what is frequently ignored is the relationship between culture and environment, and how the institutions themselves are embedded not only in culture but also in history and economics. Thus, Brown [37] argues that a culturally induced propensity for business may be a necessary but not a sufficient condition of business success; ethnic resources could provide a competitive edge but structural and institutional factors are equally important. Thus, a simple economic or a cultural interpretation of Chinese small firm marketing is inadequate. The success or failure of Chinese small firms can only be understood and explained by knowledge of Chinese cultural and economic institutions, as well as marco-economic structures and environments within which they operated. The analysis of Child [38], support this assertion as the institutional factors do influence the performance of Chinese enterprises. Thus, this research will progress to conduct follow-up interviews with respondents to understand how institutional and cultural factors influence small firm marketing practices.

CONCLUSION

The findings of this research provide a comprehensive evaluation of marketing practices in Chinese small firms in China. The Chi-square test results provide a detailed description of exactly how, and to what extent, these Chinese small firms make marketing decisions, market their products and maintain competitiveness, and also whether the marketing practices of three types of economic ownership differ from one another. However, the findings of this study tend to suggest that the readily broad small firm marketing principles, specifically generated from the Western countries, may not be fully suitable for some specific socio-cultural contexts, for example Chinese small firms in China. Specifically, the institutional factors have to be taken into consideration. Thus, care should be taken before making generalizations about marketing in Western situations and in assuming that marketing tools and techniques

are equally applicable across all places. Socio-cultural and institutional influences should be considered when attempting to understand the marketing practices of Chinese small firms in China.

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The Tribal Organization: Implications for SMEs in Emerging Economies

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Summary

The more significant, pervasive, and transcendent of the workplace the system of interpersonal relationships is, the more impactful it will be on organization design and functioning. If placed on a continuum, the priority accorded these relationships may range from totally unimportant to absolutely critical. Weber's bureaucracy, since it embraces the notion of a highly rational, impersonal system, provides a good example of the one extreme, but what constitutes the other?

Opposing the pure *Corporate* form, is the *Tribal* system where developing and maintaining strong interpersonal relationships takes precedence over all other considerations. Recruitment, promotion, retention, and sourcing decisions are based on association. Nepotism is often regarded over merit. Venture analyses might begin with an assessment the potential impact on individuals or groups. Strategic choice is dominated by issues of social harmony, respect for sovereignty, and personal preferences. Conflict is approached through *attitudinal bargaining* where maintaining the social atmosphere is more important than resolving issues. The ultimate form is the family business where the line between family and business is indistinguishable.

Long the mainstay of some regulated industries, the family firm, and tradition-steeped enterprises (e.g. the wholesale diamond trade), the *Tribal* form of organization also appears to be the design of choice for Western *energy-driven entrepreneurs* and emerging SMEs in The Peoples' Republic of China. Among its advantages are: 1) workforce stability and harmony, 2) clear separation of task and administrative work, 3) centralized control, 4) flexibility, and 5) resource conservation and leveraging. On the distaff side, such organizations can: 1) limit organization growth, 2) impede employee development, 3) obstruct effective succession, 4) eclipse rational decision making, and 5) be extremely vulnerable to the vicissitudes of interpersonal, group, and social dynamics. Where favorable cultural traditions exist, however, the *Tribal* organization design exhibits several advantages for enterprise formation in emerging economies.

Introduction: Interpersonal Relationships and Organization Forms

The degree to which satisfying interpersonal relationships is important to top management and other organizational members will often influence the ultimate organization form adopted. One might view this

concern as a continuum that ranges from totally unimportant to absolutely critical. Weber's bureaucracy[1], since it embraces the notion of a highly rational, impersonal operation provides a good example of the one side. But what lies at the other? What occupies the middle-ground? In a generic sense, the continuum might look a bit like Exhibit 1. In the following discussion, we will examine how organization form reflects the perceived importance of social processes.

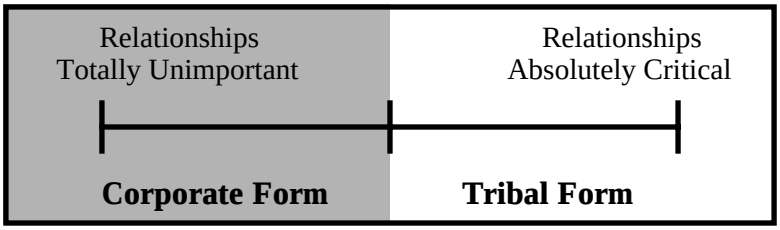

Exhibit 1. Relationship Significance and Organization Design

Corporate Forms

Modern organizational life is punctuated with mobility, career tracking, and job hopping. In times past, individuals were likely to be more job- than career-oriented and working life-long tenure with a single employer was not unusual. Co-workers were equally likely to be neighbors and life-long friends. The contemporary workforce portrays a significantly different profile. Since World War II, the U.S. labor pool has become progressively more mobile, individuals have become more concerned with career paths than jobs, and employment patterns and the interpersonal relationships that derive from work associations have become more transient. This shift has also brought with it a change in role played by the social processes (a.k.a. informal organization and emergent network) in organizations.

Employees may not only be shareholders in the companies that employ them, they may also own stock in the companies with which they compete. Professional managers acquire and deploy equity assets provided by thousands or perhaps millions of anonymous owners and look to their personal career advancement by providing short-term profitability. Fast-tracking executives keep in regular contact with well-connected recruiters and are quite willing to jump, not only to the employ of former competitors, but also, to entirely different industries. Simultaneously, employing organizations reflect the trend by emphasizing the "bottom line," offering "golden handcuffs" to the chosen few, staffing-up to peak demand or upscaling and then initiating wholesale layoffs and forced retirements during slow periods or when downscaling. Leveraged buyouts, spinoffs, acquisitions, and

divestitures are undertaken solely on the basis of financial and strategic analyses. The focus of corporate life is more on organization success than on the individual players' satisfaction.

This is not to say that many firms have not "gone the extra mile" to provide a secure and satisfying workplace for their employees or that there is no loyalty among todays workers, but the general theme is that the firm is a business before anything else. Keeping the board of directors satisfied and providing shareholders with an attractive return on their investments takes precedence over building strong interpersonal relationships. In fact, close ties with co-workers might even be a liability because of the potential for clouding rational judgment when making sound business decisions, placing oneself in a compromising position or jeopardizing a competitive edge when the next promotion opportunity comes available, or by creating feelings of loss when the inevitable relocation, job change, or layoff occurs.

At the extreme, the corporate form of enterprise is characteristically fast-paced; operating in a rapidly-changing, high-risk environment where there is potential for big gains and big losses from transactions. Success is facilitated by super-star performers who operate semi-independently. Winners become overnight heroes and receive handsome rewards; individuals who go too long without a win or who incur a significant loss are history. *Market imperfections* [2]— knowledge or information not readily available to others — provide a clear competitive advantage, therefore, key players spend much of their time working networks and developing sources. The organization's social processes are used to collect information, cultivate support, and isolate potential contenders. Mead [3] noted that among the benefits of such collaborative practices are mutual defense from enemies and exploitation of adversaries. A lot of the "work" gets done by harnessing political alliances.

Internal competition reigns supreme and the dominant rule is "win." Conflict resolution is *distributive* — there can only be winners and losers, compromise is unacceptable. The informal organization is structured much like ancient Roman society: there are citizens — insiders who enjoy the privileges associated with being part of "the network" and who have access to executive management and scarce resources — and there are barbarians — outsiders who are potential rivals. Citizens regularly compete among themselves, but they will close-ranks when a barbarian threatens to break into the circle. Should a barbarian succeed, he or she will be granted "citizenship" because citizens *use* other citizens to accomplish their ends. The basis for these relationships is parasitic or symbiotic at best . . . citizens are not friends, they are coconspirators, collaborators, co-opters, and allies. Resources, both inside and outside the organization are jealously guarded.

Typical of the extreme corporate form are political parties, investment banking firms, and advertising agencies. The organization *character* is suspicious, guarded, work-hard-play-hard, intense, often brutal, and

frenetic[4]. The high-stress climate shortens many careers by "burnout" and various stress-related health problems.

Tribal Forms

At the opposite end of the continuum is the extreme tribal system where developing and maintaining interpersonal relationships takes precedence over all other considerations. Recruitment, promotion and retention decisions are based on association. Nepotism is often regarded over merit. Venture analyses begin with an assessment the potential impact on individuals or groups. Strategic choice is dominated by issues of social harmony, respect for sovereignty, and personal preferences. Conflict is approached through *attitudinal bargaining* — maintaining the social atmosphere is more important than resolving the issue. Relationships are the driving forces in decision making and business conduct.

The extreme case of the tribal form is the family business where the line between family and business is indistinguishable. Family members may be placed in positions for which they are unqualified, may displace non-family members in currently occupied positions, new positions may be created on their behalf "just to make room for them," their jobs may be permitted to outlive any positive contribution to the organization, and their advancement may "leapfrog" more deserving non-family members. Delegation, compensation, succession, and perquisites will follow bloodlines more closely than they do lines of authority or accomplishments. Individuals who are neither shareholders nor employees may have greater influence on how decisions are made and executed than do active organization members. Actions that favor family members might be undertaken even if they engender great risk to the survival of the organization as a whole. The creation of a legacy overshadows short-term profits. In the extreme tribal form, not only is "blood thicker than water," often it is also more substantial than than sound judgment.

For an organization to assume a tribal form, it is not mandatory that relationships be fostered by lineage or long-term affiliation, e*nvironmental forgiveness* may also be a contributing factor. The more *slack* there is in the external and internal operating environments, the more likely it is that the organization's character will be relaxed, informal, and, perhaps, even nurturing. Where resources are plentiful, timing is flexible, the magnitude of potential losses from errors is small, opportunities for distinguished performance are numerous, rewards are evenly distributed, and individual accountability is difficult to assess, relationships may become the standard against which the quality of work life and success are measured. This is particularly true if the work itself is tedious or boring. Nowhere was this more evident than in the leisure travel industry before deregulation.

Operating level airline employees, travel agents, resort personnel, tour conductors, and cruise line personnel changed their employ with some frequency and even worked for the same employer on several occasions throughout a career. Relationships with current and former co-workers and bosses endured and few individuals ever considered employment outside the industry. Supervision was so informal it was almost transparent, there was a high degree of cooperation among industry member firms, and social gatherings were numerous and frequent. Quite typically, service providers offered their excess capacity to other industry members, including employees of competing firms, for no charge or at deep discounts. Work severance was more likely to occur as a result of some interpersonal conflict than issues of wages, hours, or working conditions. As the industry became less regulated, competition increased, and the dominance of interpersonal relationships as a primary industry norm subsided correspondingly. With few exceptions, the entire industry slipped to the left along the continuum and has taken on a more corporate appearance.

An additional factor facilitating the tribal form is tradition: that is, the industry has operated with and depended upon the tribal form for so long that any management or organization deviating from the pattern is looked upon with suspicion. Agricultural cooperatives, religious organizations, and the wholesale diamond trade are, customarily, tribal in nature. The diamond trade is rather unique in that the failure of parties to perform on agreements could result in millions of dollars in losses. Still, all deals are closed with only a handshake. Interpersonal relationships and blind faith in the sanctity of those relationships are the mainstays of the industry and it has operated in this manner for hundreds of years.

Why Tribal?

Although numerous family enterprises employ a tribal form of organization, not all tribal organizations are family dominated and not all family firms operate in tribal fashion. The nuclear, or conjugal, family is comprised of parents and their children. It may be *extended* through polygamy, the sharing of a common residence by two or more nuclear families, or the connection of several generations through the male or female line. From a sociological perspective, relationship-based organizations represent neither conjugal nor extended families. The terms *clan*, if matrilineal, or *GENS*, if patrilineal, do not apply because each can trace a connection to a common ancestor. Tribes are distinguished by their occupancy of an identifiable domain; a shared pattern of ideas, behaviors, and beliefs; a shared sense of mutual duties and obligations; and, autonomous governance. Memebers are generally interdependent and are linked together by economic, religious, or blood ties. Tribes may operate with individual, shared, formal, or informal leadership and can include families, clans, and others

who share no ancestral connection. Further, unlike families and clans, tribal membership can be revoked or abdicated. Tribes represent considerably more than *collections* where a single common trait is sufficient to constitute membership. And, they are more complex than *collaborations* where relationships are fostered by some external event or shared goal. Relationship-based organizations, therefore, are virtual, if not actual, tribes.

The Significance of Context

Metaphorically, the organization is a pressure cooker. As the heat is turned down, the pressure subsides. This is precisely what happens as one moves to the right on the continuum depicted in Exhibit 1. As the line between winning and losing becomes wider and more diffuse, corporate warfare and internal competition become more benign. As the emphasis on super-star performance abates, interpersonal relationships based on mutual attraction, shared goals and interests, perceived status, favorable evaluation by outsiders, and simple proximity become more prevalent. The social processes become less political and more a vehicle for sharing information and fulfilling affiliation needs. Teamwork displaces "winning at any cost," and conflict resolution becomes more *integrative* — that is, oriented more toward mutual problem-solving and accommodation. The more significant, pervasive, and transcendent of the workplace the system of interpersonal relationships is, the more impactful it will be on organization functioning. The organization's *character* becomes more humane. As organizational members become less dependent on specific others to forge substantial and fulfilling relationships, the greater the tendency will be for the organization to fall somewhat to the left of the extreme position on the continuum in Exhibit 1.

In the corporate form, interpersonal relationships are simply subordinated to other factors. As noted in the extreme case, one such factor might be the nature of the industry and its impact on internal operations. External forces such as the level of competitive rivalry involved in selling outputs, regulatory activity, scarcity of resources, the velocity of change (economic, political/legal, social), cultural pressure, and stakeholder involvement will influence the nature of sanctioned internal behavior. Another factor might be the core technology adopted by the organization itself.

One of the earliest studies into sociotechnical systems, and the impact of technology on relationships, was conducted by the Tavistock Institute in Great Britain [5]. For centuries, British coal miners worked shoulder-to-shoulder in teams picking away at long veins of coal in underground caverns. Shifts and teams worked together over long periods of time and members depended upon each other for group productivity, social exchange, and personal safety. After World War II, the introduction of newer, more-automated equipment

eliminated some jobs, demanded greater specialization in others, and greatly increased the physical distance between workers. Although the new technology made the work easier and safer, its impact produced results quite different from those intended. Productivity declined and labor disputes increased. The technology ignored the importance of the interpersonal relationships the miners had developed over years of working together and the influence those relationships exerted over work performance and state-of-mind.

The adoption of more efficient technologies may place employees in workstations, "cubes," home offices, and "doing business out of briefcases." Face-to-face encounters may be replaced by telephone calls, FAXs, and e-mail. To the extent that organizations may be compelled to assign low priority to interpersonal relationships in work-flow designs, it is likely that they will have to tolerate, or create mechanisms for dealing with, the backlash elsewhere in the total system. Conversely, where the preservation of specific relationships dominates all other considerations, non-competitiveness, insider-outsider discord, erratic or arrested growth patterns, and operating-inefficiency are likely to follow.

Human beings are basically gregarious creatures and social separation can introduce social pathology. Feeling depersonalized and disconnected, individual responses may range anywhere from cynicism and apathy to brutality and violence, from aimlessness to nihilism to predatory behavior. The more important authentic interpersonal relationships are to the individual or the group, the more likely the deprivation of those relationships will yield more extreme responses. This phenomenon was noted in the dog-eat-dog behavior found in "win big, lose big" industries in contrast to the more subtle social disquiet found where existing relationships were disrupted by change.

Human beings are also highly subject to seduction by over-indulgence. Self-image is enhanced by unconditional acceptance and access: self-criticism vanishes in its wake. The development of personal competency is arrested when well-meaning others assuage all difficulties. Extreme interdependence deprives the individual of an effective set of broader social skills, objective experiential learning, and a sense of authentic personal accomplishment. The resulting combination of high self-esteem and mediocre personal competency can create myriad complications for both the individual and the organization. Such occurrences are not-at-all rare in successive generations of family businesses when the "wealth takers" succeed a generation of "wealth makers." In truth, too little or too great a relationship-orientation, irrespective of its origin, has its downside.

The Tribal Organization in an Emerging Economy: The Chinese SME

Operationally, the concept of "family" in China is more broad than the Western view. The Chinese *jia* may be a nuclear, three-generation, or five-generation household. The *jia-zu* or "family of families" includes all who share a common ancestry, but is not limited to kinship relationships. "The family" may encompass transgenerational relationships, close friends, and even school mates[6]. Confucian values stress the importance of family ties and group loyalty. "The individual exists for the benefit of the group" and the "group," in turn, ministers to the social, psychological, and physical needs of its members[7]. The "group," in the case at hand, refers to the *jia* or the *jia-zu*. The same sense of loyalty, however, does not extend to those outside the "family." It has been further observed that the individual's sense of loyalty and obligation diminishes as the distance between the individual and the "inner family circle" increases [8].

The practical wisdom of Chinese reliance on family ties has been severely tested over the course of history and has prevailed. "Family" loyalties have preserved the well-being of "family members" in the face of natural disaster, arbitrary governance, foreign incursion, dictatorship, social upheaval, and even the normal aging process. In the latter instance, it is the family that maintains the status and provides care for its elderly members when they are no longer able to be productive. The *jia-zu*, appears to parallel the tribal organization in several dimensions.

A Little History

Within the past hundred years, China has undergone more than its fair share of change. Beginning with multi-country expeditionary force occupation, the Boxer Rebellion, and a monarchy at the beginning of the century, it has since endured Japanese military occupation, traded monarchy for Marxism, isolated Taiwan, supported North Korea's military adventures, and invaded Tibet. As the twentieth century comes to a close, China has crushed human rights activists and encouraged private enterprise; fostered isolationism and a "cultural revolution." Simultaneously, it granted Hong Kong administrative autonomy for fifty years, and applied to the World Trade Organization for membership. It has seen one hundred years of turmoil and contrasts . . . politically. Socially, China has changed very little: Confucian values[9][10] endure, Chinese culture remains steadfast [11][12], agrarianism prevails [13] . . . ancient warlords were simply replaced by contemporary politicians.

It is within this context that a renaissance of capitalism is taking place. Beginning in the late 1970s, legal reforms in China have progressively moved in the direction of creating a market economy to "supplement

the socialist economy of private ownership" (Exhibit 2)[14] . Interestingly, the overall thrust of these new policies has been to "permit," rather than proactively "stimulate," private commercial activity.

Date	Event	Impact
October 1, 1949	Founding: Communist Party of China (CPC) People's Republic of China (PRC)	Shop owners compelled to join State Cooperatives — Private sector abolished
1978	Third Constitution adopted	Small business legalized Fixed income tax introduced
1982	Fourth Constitution adopted	Modernization program adopted. Stipulation that private enterprises should supplement socialist economy.
March 1993	Socialist market economy amendment adopted by National People's Congress	Private enterprise forms are defined: • *siying quiyejia* = privately owned enterprise employing 8 or more people • *geteibu* = privately owned enterprise employing fewer than 8 people (literally - "one man business") • *xiangzhen qiye* = extended family enterprise (generally rural)
October 1995	"Opening" policy adopted	339 jurisdictions (totaling 300 million people) are declared open economic areas
1997	consolidation	Mergers and acquisitions encouraged among light industrial enterprises (objective is to reflect Korean *Chaebol* model)

Exhibit 2. A Brief History of Business-Oriented Public Policy Reform in the PRC [15]

Despite the benign legal impetus for creating a market economy, those who perceived the potential opportunity were quick to respond. It could be argued that all the public policy shift accomplished was to legalize what had, for eons, been common practice. Blackmarketeering and barter trade have fueled a domestic market economy for ages. High ranking party officials with an entrepreneurial bent, and a dependable relative to run the business, have been using Hong Kong as a "back door" for international trade since the revolution. Nevertheless, the reported consequences of legal reform are quite dramatic (Exhibit 3). Since legalization, some 16 million private enterprise licenses have been granted. Approximately seventy per cent of of these are in rural areas. Because of the problems associated with excessive urbanization, rural entrepreneurial activity has been encouraged by creating special development districts, land reclamation programs, and tax incentives for private sector farmers.

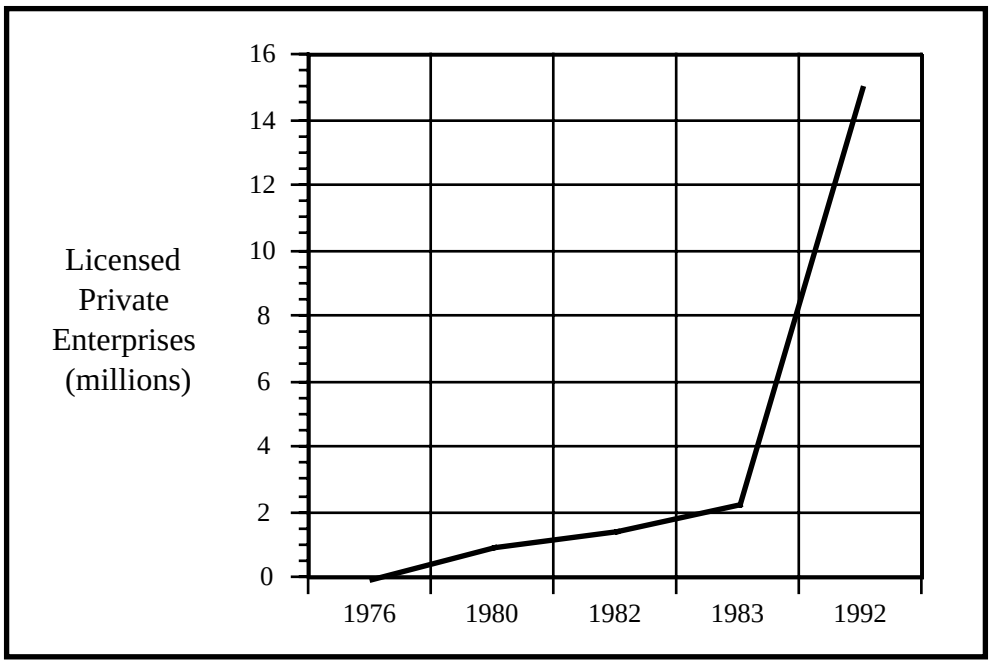

Exhibit 3. Private Enterprise Population Growth in the PRC [16]

Although individual and group-of-families forms of licensing are quite popular, the most successful form of SME has been the family enterprise or "specialized household," . Most enterprises are, also, quite small with respect to scale of operations and number of employees. Were this the end of the story, it would represent little more than an interesting aside. Small, principally-rural, relatively-isolated, family businesses operating within a country that provides little government assistance and few if any venture capitalists would be expected to be *tribal* in nature. So what? It is the operational definition of "family" and the methods of operation that attend the Chinese SME, however, that provide some "top spin" to the *tribal organization* construct.

Internal Business Operations

Chinese enterprise management relies heavily on family ties and traditional values (respect for age and hierarchy, sanctity of relationships, shame-avoidance, etc.) in the regular conduct of business operations[17]. Conflicts are more likely to be resloved by family councils than adjudicated in public courts [18]. High centralization and low bureaucratization, typical of most Chinese SMEs, depend on employee loyalty and respect, as opposed to supervision and procedures, for their success. Formal controls and standardization are eschewed in favor of personal control by principals[19]. Venture capital comes from family coffers and consulting advice comes from experienced family elders. Even the scale of business operations is avered to

derive from a conscious decision to keep personal accountability high by limiting the physical size of the enterprise (recall, proximity reinforces loyalty and obligation) even though it may equally inhibit potential economic advancement[20]. Creativity and innovation are prized as vehicles for improvement. The SMEs stand in stark contrast to state-owned enterprises that manifest high degrees of bureaucracy, low accountability, and innovative malaise[21]. Suggesting that these operating patterns are more cultural than national in their origin, several studies have noted similar practices in expatriot Chinese SMEs [22][23][24].

Strategic Business Operations

If the *jin-zu* facilitates efficient internal operations, it is the "life's blood" of effective strategic operations in the PRC. Chinese SMEs do not up- and downscale relative to business conditions as do many of their Western counterparts. Instead, they maintain a consistent, but small, cadre of core employees (not unlike a skeleton crew on a ship) . . . employee loyalty and obligation are repaid in kind by business owners. As production demands increase, additional capacity is provided by other SMEs in "the family." On such occasions, no particular provision is made for interfirm coordination and control, it is simply expected that each enterprise will execute its performance in a manner that will *save face* (avoid shame) for all participating family members. The enterprises involved in these arrangements are determined by the *jin-zu* relationships of the principals and the circle of family extends to employees, suppliers, and customers alike[25]. It bears noting that these relationships are purely voluntary and cooperative as opposed to the more mandated and collective participation found in the Japanese *Sogo Soshas*. Also disparate from the Japanese models, performance is more a matter of family loyalty and obligation than public spiritedness and team play [26].

In addition to providing capacity flexibility, *jin-zu* relationships have been shown to provide a basis for resource exchanges (even when costs are higher than market prices) [27], vendor and customer relationships [28], intelligence gathering and sharing[29], geo-expansion, and even new enterprise formation. Emigrant Chinese SME principals are significant investors in PRC SMEs [30]. The PRC is the single largest investor in Hong Kong SMEs. "Spin-offs" and new business startups are as likely to be the product of scale minimization decisions and nepotism practices as they are the result of opportunity analyses. When enterprise size approaches a scale difficult to manage by traditional practices, a new venture may be launched to preserve the organizational integrity of the pressured firm. Equally prevalent, when a family member is ready for greater responsibility, a new enterprise may be spawned to provide upward mobility[31]. *Jin-zu* members borrow and loan, buy and sell, invest and harvest, and teach and learn within the *jin-zu*. Contracts are not written, disputes are not litigated, and

breaches, even in the absence of formal performance specifications and stipulated penalties, are uncommon. So interdependent are the relationships among *jin-zu* members, they have been described as "enterprise cities [32]," centrifugal business systems [33]," and "web-based management" systems [34].

Conclusions

As noted earlier, tribal organizations tend to flourish when external pressures are weak to moderate and internal relationship bonds are strong (but not necessarily reciprocal). The more robust and dependable the relationships are, the more likely the organization will be able to withstand considerable environmental turbulence before having to adopt a more formalized and systematized configuration and become more *corporate* in form. In fact, some external forces may actually strengthen internal bonds and enable the tribal organization to endure beyond what might be expected. Resource scarcity may engender strong resource sharing systems such as those found in agricultural cooperatives and communes. Powerful common competitors may induce a high degree of cooperation and cohesion among groups of smaller competitors. Even prevailing ideologies can strengthen the bonds among those who harbor alternative views: such is the stuff of revolutions. Consequently, tribal SMEs are found to be powerful economic engines in emerging economies where barriers to entry are low, resources are scarce, and infrastructure is limited. By leaning heavily on solid interpersonal ties, such organizations can minimize administrative energy expenditures and devote their time and scarce resources to task accomplishment. By paying particular attention to to the nuances of cultivating and maintaining strong relationships, such organizations also provide for the satisfaction of significant social and psychological needs of their members.

Whereas many societies and industries have fostered the tribal organization as a consequence of contextual pressure or the lack thereof ("a common enemy" or environmental *slack*), Chinese society has adopted it as a logical extension of extant cultural machinery. As a result, *jia-zu* systems are larger and more complex than most typical tribal organizations, yet their members are not particularly conscious of the adhesive that holds them together. Cultural compliance is not a conscious act it is "simply they way things are done around here." There is one proviso. Because duty and responsibility erode as the distance between the individual and the inner family circle increases, a conscious effort is made to keep the SMEs small. The absolute dependence on cultural values as a substitute for supervision, formal sourcing, coordination, and contractual agreements is relatively unique to the Chinese SME. Another distinctive feature is the presumption of reciprocity. In other tribal organizations, maintaining relationships supersedes other considerations and, thus,

inequities are tolerated, but they do not go unnoticed. The one-sidedness of parent/child exchanges in many family businesses attests to this. In the *jia-zu*, it is simply assumed that all parties will perform to their utmost and not jeopardize or take advantage of another "family" member for personal gain.

When a tribal organization precipitates from a conscious relationship-orientation, system failures can be anticipated and contingency plans adopted to compensate for them where possible. In the typical tribal organization this is generally viewed as a cost of doing business in such a manner. Further, complications are limited to the affairs within a single enterprise. In the Chinese SME, the adoption of a tribal form is more natural than contrived. Consequently, system failure is likely to come as a total, and debilitating, surprise. Not only do the networks of interdependent SMEs create more opportunity for failure, but the impact will likely be more far-ranging. On the positive side, reliance on cultural values has enabled the Chinese SMEs to minimize overhead, maximize flexibility, accumulate dependable supplies of scarce inputs, and operate with considerable efficiency. Further, by relying on its cultural heritage, the PRC has managed to "jump start" a groundswell of controlled-capitalism in a socialist society in a very brierf amount of time (a feat that Russia was unable to accomplish).

The ultimate success of the Chinese SMEs may also reveal their greatest weaknesses. By limiting the size of their organizations, *jia-zu* members preclude the possibility of penetrating economy of scale industries. By keeping everything within the "family," talented outsiders with valuable skills will be excluded, capital markets will go untapped, and operating employees will not be developed to assume a wider range of tasks or greater responsibility. Excessive reliance on traditional suppliers may drive up costs or disrupt production schedules. As business owners and employees become more prosperous, they will also be presented with more options and this, in itself, may disrupt the integrity of a cultural system that has endured for over a thousand years. One needs only to look at the impact of the current generation in Japan's labor pool to see how choice can mitigate one's sense of duty and obligation. With prosperity has come a steady erosion of the work ethic and company loyalty that enabled Japan to build its post-war economy.

As a seminal building-block for economic development, the PRC has clearly demonstrated the merits of the tribal form of organization. So long as the Chinese SMEs remain SMEs and limit their sphere of operations to culturally homogeneous territory, they are likely to continue writing new chapters in their already-impressive success story. What remains to be seen, however, is how the *jia-zus* will fare when economic development and extra-national competition demand movement to larger scale operations.

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FACTORS UNDERLYING BUSINESS GROWTH IN SWEDEN

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FACTORS UNDERLYING BUSINESS GROWTH IN SWEDEN

Summary

As capitalism becomes more widely recognized for its contributions to increases in and distribution of wealth, a great deal of interest has become focused upon what factors in an economy contribute to the growth of private sector business activities. This issue has been of special importance among European policy makers since the U.S. has demonstrated a greater economic growth rate over the last ten years and has a comparatively greater contribution to overall economic activity by private sector businesses than by government economic activities.

To explore this issue, we have examined the factors contributing to business firm growth in Sweden. We use a special database prepared for Jonkoping International Business School by Statistics Sweden that is a census of all businesses in Sweden. Given the complexity of business organizations, our definition focuses on business activities rather than ownership or size under the assumption that activity type is a major contributing factor to growth. Because of this focus, our "business" definition is neither the traditional enterprise nor establishment definition and differs from other research in this way.

Analysis of this data is done with multiple regression where growth rate is the dependent variable. The results show that business age (younger is better), independent ownership, several types of business activity, beginning size (smaller is better), and legal form and are the most important factors related to growth. This suggests that young, small, independent businesses (entrepreneurial businesses) in certain types of activities are important contributors to overall growth in Sweden's private sector.

Introduction

Since the worldwide economic recession of 1989-90, the national economies of the European Union have experienced below average rates of growth. This is especially obvious when compared to the U.S. where there has been economic growth at an above average rate. This has led to a growing interest in determining what factors in these economies underlie the differences in growth rates. This interest focuses upon private sector business growth since the private sector makes up a greater part of the U.S. economy than in the EU nations.

While there is an extensive body of theory of the firm in economics, linkages between this theory and reality of business formation, growth and decline are crude and contradictory. For example, Gibrat's law theorizes that both small and large firms will on average have the same rates of growth. But empirical evidence has refuted this theory although no alternative theory has been developed. And, the empirically derived and widely acknowledged life cycle theory of the firm is not an economic theory at all since there is no justification for such a cycle in neo-classical economics. Nonetheless, an economic based typology of economic development based upon new firm formation and growth is available in Wennekers and Thurik [17]. Therefore, we begin our study of factors underlying growth by examining previous empirical research on factors underlying growth of business firms.

David Storey [14] provides an overview of the many factors considered by researchers prior to 1993 and concludes that among small firms, there are six factors of significance. These are firm age, size,

sector/markets, legal form, location, and ownership. Storey notes that empirical research shows that age is inversely related to growth, i.e., older firms grow more slowly than younger firms. Size of firm is another factor but one that is the source of some debate in economic theory (Gibrat's Law). As noted above empirical research has demonstrated that smaller firms grow at a greater rate than larger firms. However, Storey notes that Evans [6] and Hall [8] were the first to demonstrate that Gibrat's Law did not hold for U.S. firms. Subsequent empirical research confirmed Evans' findings.

Storey finds that growth rates vary by industrial sector and/or markets. Different sectors, e.g., services, retail trade, and manufacturing, have been found to grow differently and there is evidence for different growth rates of firms in different sectors. Legal form also is related to growth as firms that choose limited liability legal forms grow more rapidly. Storey notes that this is likely to be due to the fact that limited liability forms are chosen by those who wish to grow as such forms provide greater opportunity to acquire and accumulate equity capital needed for growth. Location is also noted by Storey as important since firms that locate in places where there are scarce resources or slim markets will not grow as rapidly as those in better locations.

Storey's [14] last factor is firm ownership since small, closely held firms would be expected to reflect the interests of their owners. Storey [14] says that fear of getting to much administration and creating problems of control are important reasons for a firm to discontinue growth after reaching the minimum efficient size. Almus and Nerlinger [1] also site Audretsch [2] and Scherer and Ross [13] in noting that in economic theory, a firm needs to grow to a certain point, referred to as "minimum efficient size" or "optimal size" in order to achieve profitability and survive. But, optimal size varies by industry sector and is not a function of legal form. Thus, Storey's concerns about owners' fears may also exist among professional managers within larger publicly traded firms as well as owner/managers of small firms. Equally important, however, is whether the firm is independently owned or a division or subsidiary of another firm.

In the following paragraphs, we use Storey's [14] summary as a base for reviewing more recent empirical research that has addressed this issue and to formulate our own model of growth for testing in Sweden.

Age of Firm

Age of firm is a widely used independent variable. Almus and Nerlinger [1] used multiple regression to examine high technology firms in Germany over a ten-year period and found that older firms have lesser growth rates. Joachim Wagner [16] also found the inverse relationship between age and growth rate in his multivariate analysis of a census of Lower Saxony (Germany) manufacturing firms. Glancey [7] in his analysis of 117 small manufacturing firms from the Tayside Region of Scotland found that growth was positively related to firm age. And Wijewade and Tibbits [19] used data from Australia in a multivariate analysis and found that older firms grow less rapidly than younger firms. Age, then, is an important factor in determining business growth.

Business Size

Without a doubt, business size is the most widely studied factor for its contributions to growth. This is because of the widespread interest and debate on the issue of job creation and size of firm. Empirical research has addressed this issue in two ways. First, several researchers have examined a cross section of firms to determine if there is a relationship between growth rate and size. Evans [6] used U.S. data from the Compustat data files comparing firm size and growth rate and found a significant negative relationship between size and

growth rate, i.e., larger firms have lower growth rates. Hall [8] used a modification of Evans' model and came to the same conclusion. Almus and Nerlinger's [1] bivariate Tobit-Model analysis of 580,000 high tech firms in Germany showed size of firm at the beginning of the period of study was a negative factor in determining growth. Wagner [16] used data from a census of manufacturing firms in Lower Saxony to find a negative relationship between firm size and growth rate.

Second, two studies focused on start-up size of new businesses. Phillips and Kirchhoff [11] provided empirical research that showed start-up firms with five or more employees had a much greater six year survival rate than those that started with fewer than five employees. They used a census of all 814,000 firms that started-up in the U.S. during 1977-78. Later research using the same database showed that firm survival is correlated with firm growth, so this was an early indication the start-up size is correlated with growth in the U.S. (Popkin and Company [10]). Confirmation was found in Wagner's 1992 [15] research that found start-up size is positively correlated with growth among new manufacturing firms of Lower Saxony.

It is not surprising to find that newly formed firms have greater growth rates since new firms start small and they are very young. Almus and Nerlinger [1] argue that this newness growth phenomenon is due to the need for the firm to rapidly achieve the minimum efficient size. Beginning size and age are clearly important factors in growth.

Business Sector/Market

Almus and Nerlinger [1] found industry sector, defined as either high tech or medium tech, to be a significant factor in their analysis of German high-tech firms. Joachim Wagner [16] found industry sector was an important factor in his multivariate modeling of a census of manufacturing firms in Lower Saxony, Germany. Phillips and Kirchhoff [11] reported descriptive statistics that show survival rates of newly formed firms vary by industrial sector. This was confirmed by Popkin and Company [10] multiple regression analysis of this same data using survival rate as the dependent variable. Obviously, business sector/market is an important factor for consideration.

However, there are two apparent problems with examining this factor, blurring of business activities and variations in market definitions. First, business activities are blurred because larger firms are inadequately represented by a single business sector classification since their many, often widely different, divisions and subsidiaries are frequently in different sectors. For example, IBM is classified as a manufacturing firm but it has many divisions that deliver services to customers. Thus sector differences among firms may be blurred by grouping many different activities within a single business sector identity. As will be noted later, we use an definition of "business" that adjusts for this.

Second, business sector/market size may differ significantly among firms in similar business sectors because of international operations among some but not all businesses. This will be most evident among firms with wholly owned foreign subsidiaries as their growth may be increased by exports of goods and services from domestic locations or may be decreased by moving operations from domestic locations to foreign locations.

Furthermore, growth may also be affected by changes in industry sector/market. Such changes may be a natural outcome of growth or a cause thereof, especially in technology intensive industries where rates of product/service changes are known to be relatively high. Popkin and Company [10] found in its multivariate analysis that changes in industry sector were positively related to survival. Therefore, it is appropriate to

examine both industry/market sector and change in industry/market sector as factors contributing to growth. We will include a variable for this factor.

Location

Storey [14] argues that some locations are more conducive to firm growth. Davidsson [3] agrees and models "growth opportunity" as an important variable. Further Davidsson says that characteristics of the geographical area are important for industries where firms are bound to the local market. However, the geographical area variables do not emerge as strong factors in his empirical test results.

Likewise, Almus and Nerlinger [1] used regional population density as a location variable and found only minor indications that location affected growth rates. The effect appeared to be "U" shaped with size of firm, i.e., the smallest firms and largest firms had the least location effects. It is possible that location effects are closely linked to industry/market factors that are associated with size. Or location effects may be associated with industries. Almus and Nerlinger looked only at technology based firms. And it is know that firms in high tech growth industries tend to cluster in the same location. Popkin and Company [10] found that location effects were removed from their regressions when industries definition variables were allowed to enter their equations. They conclude that location is closely associated with industry clustering and probably of secondary importance.

However, Storey's and Davidsson's theoretical arguments are intuitively appealing and therefore location should be tested as an additional factor contributing to business growth. Furthermore, changes in location may also be relevant to growth rate so we will include a measure of change in location.

Legal Form

Almus and Nerlinger [1] included legal form in their multivariate analysis of high tech German firms. Their results showed that firms with limited liability realize higher growth rates than firms where founders' private capital investments are liable. They suggest that firms with limited liability are more willing to take risks since the founders' personal wealth is protected from excess losses of the firm. Legal form therefore is a factor underlying firm growth rates.

Almus and Nerlinger [1] also found that partnerships with other firms correlated with greater growth rates. However, Rosa and Scott [12] describe that although high rates of inter-company links are connected with higher growth the common practice of multiple directorships among small entrepreneurial firms may be an adequate substitute for formal partnerships. They suggest further research on multiple directorships as a proxy for business ownership or portfolio entrepreneurship. This raises an interesting issue regarding business firm relationships. Many businesses are wholly or partially owned by other businesses. Many have joint stock ownership with several other businesses. Some of these relationships extend across national boundaries and/or give access to international markets. Thus, it is important to examine the effects of such business relationships and changes in these business relationships such as spin-offs, acquisitions and mergers

Since legal form is obviously an important factor, it is likely that change in legal form will also be a factor in firm growth. Either the firm will change its legal form as it grows larger, or the managers will choose to change the legal form as their attitudes shift towards growth. Acquisitions and mergers may affect growth rates by changing resource availability that then promotes or inhibits growth. Clearly, there are many changes in legal form that can affect growth and each has to be recognized as a potential factor.

Owner/Manager Resistance to Growth

Almus and Nerlinger [1] are alone in examining manager attitudes as a contributing factor to firm growth. They found that use of a management team improved growth and manager/team technical skills also improved growth rates. Almus and Nerlinger conducted a major survey of German high tech firms in order to gather data about management of these firms. Obviously, managers who desire growth can influence business behaviors so as to achieve or not achieve growth.

Overview

Many factors have been identified by these various authors. However, Almus and Nerlinger [1] and Wagner [15] appear to have used broad-based databases that are similar to our Swedish database. Therefore, we have prepared a table comparing these two research studies to Storey's conceptualization and our own model, which will be described next. This is shown as Table 1 below.

Designing the Swedish Model

Based upon the above review of research we developed the following model for testing:

> Growth Rate = f (age, business size, overall enterprise size, industry sector, change in industry sector, legal form, change in legal form, ownership governance, change in governance, international activities, location, change in location)

The following paragraphs describe our database and its contents followed by a description of how we operationalized our variables from the data available.

Structure of the Database

The data set was developed in close cooperation with register experts from *Statistics Sweden* (i.e., the official 'Bureau of Census'). Their registers are complete in the sense that all legal commercial activity is represented, whether run as sole proprietorship, partnership, limited liability company or some other legal form. Data originate from different sources such as tax authorities and mandatory surveys. Updating is frequent and generally speaking the registers are of a very high standard by international comparison. Data from three different registers, and ten annual versions of each, have been utilized in developing the data set. For a more elaborate description of the data set, see Davidsson [4].

Table 1

Comparison of Storey's Conceptual Scheme with Three Empirical Research Studies

Storey [14] Conceptual scheme	Almus and Nerlinger [1] (Western Germany)	Wagner [15] (Lower Saxony, Germany)	Kirchhoff et.al. (2000) (Sweden)
Age:	Years	Years	Years
Size:	Number of employees	Number of employees	Number of employees Enterprise overall number of employees
Sectors/markets:	New technology based firms High tech Industries Medium-tech industries Other manufacturing Diversification	Manufacturing Industry Concentration, (Herfindahl index) Industry effect Innovations	Industry sector (16 sectors) Change in industry sector
Legal form:	Status of limited liability Team foundation	Production unit	Change in legal form Ownership governance Change in governance
Location:	Inhabitants/km^2	NA	Region type Change in region type
Ownership:	Independent firms Subsidiary/affiliated firm Skills	NA	International subsidiaries, joint ventures etc. Foreign ownership Change in ownership

Our unit of analysis is the *business*, which is the legal entity. This legal entity may run one or several establishments (plants, outlets). Further, the business may be either independent or majority owned by a parent company. We choose this unit of analysis because an analysis of establishment level growth is for multi-establishment businesses not informative about what in theory is conceived of as 'the firm'. Accepting as one unit the entire hierarchy of parent and daughter companies (when applicable) was considered but rejected for several reasons. First, such large, multi-business units are not ideal for assessing the influence of industry on growth since they are typically active in multiple industries. Using this level of business definition would blur the effect of industry sector in our analysis. Second, such large corporate structures typically go through mergers, divestments and ownership changes of such magnitude and frequency that meaningfully following them and assessing their growth over long periods of time is almost impossible. Third, such large corporations typically have some business units that grow rapidly while others shrink thereby hiding the growth businesses within the overall corporate behavior. On the other hand, the size of the overall ownership organization may influence the growth of its separate businesses. This size measurement has been retained in the database for all businesses that have a parent corporate ownership.

Codes for companies may be changed because of ownership changes, industry re-classifications, or spatial relocations. This may make what in reality is an on-going business appear in the registers as a discontinuance and a start-up. Identification codes for establishments are relatively more insensitive to changes of the mentioned kind. We have therefore not accepted business codes as the criterion for tracking businesses over time. Rather, a constellations of establishments (and their employment) associated with a certain company code is regarded as 'the same' company if they appear together in the next annual version of the register under a different company code.

The data set comprises *all commercially active businesses in the private (non-government) sector in Sweden that in November 1996 had at least 20 employees.* With respect to that category, we are dealing with a census study. Annual data for all businesses have been compiled for the 1987-1996 period. There are 11,748 such enterprises, 8,562 of which were already in operation in 1987. Previous government-sector businesses are included if by the final year they have transferred to the private sector, as are start-ups during the period if they fulfill the size criterion for the final year. However, in order to have a sound basis for computing growth rates we have demanded that businesses be active in the register at least for the final three years. This decreases the number of cases to 11,196. Businesses that dissolve during the period are excluded regardless of their previous size and growth, as are surviving businesses that previously may have had more than 20 employees but do not reach that number in 1996. No upper size limit has been employed, but in numbers the data set is dominated by small and medium-sized businesses.

From this description it should be clear that our data set is *not* a panel of businesses that is being followed from 1987 to 1996. Rather, the data set should be compared to a cross-sectional survey in which businesses with 20 or more employees were contacted in November 1996 and asked about their development history. Compared with such a study, our data set has the distinct advantages that: (a) it is a census rather than a sample, and (b) data from previous years were collected at the time and not subject to memory error or hindsight bias. Importantly, however, the design of the data set makes it likely that positive effects of smallness and low age on growth are exaggerated.

Operationalizing the Variables

A range of variables is available for each business each year. Size data are available for total employment, organic employment (excluding merger or acquisition activity), and sales. Sales data were not used because such were available only for a biased half of the cases. Both total and organic employment growth were tested but as the results were very similar we only present analyses concerning total employment growth. Business growth rate can be operationalized in many different ways (see: Delmar, Davidsson and Gartner [5]). We began with the simple calculation of 1996 employment minus initial employment divided by initial employment (percent change). However, this variable has a highly skewed distribution that makes it unsatisfactory as a dependent variable in multiple regression analysis. Therefore, we chose to use a growth index calculated as 1996 employment minus initial employment divided by the average of 1996 and initial employment. This index variable is asymptotically normally distributed. so it is statistically appropriate. The independent variables are described in Table 2 below.

Table 2

Independent Variables and Their Measurement Method

Business Age - AGE	Age of business in 1996. The data file only contains 25 years of data so age is truncated at 25 years.
Business Size – BEGSIZE	Number of business employees at the time of first observation.
Overall ownership organization size – CORPSIZE	Number of overall employees at the time of first observation
Industry Sector – BEGINDUSnn	Industry codes are condensed into 16 industry sectors, each a dummy variable. The sector defined as "metal working and manufacturing" is the omitted dummy.
Change in industry sector – CHINDUST	Defined at one if industry sector code changes one or more times during the period observed.
Legal form – BEGLEG	Dummy variable. Limited liability = 1.0; all others are zero.
Change in legal form – CHGLEGAL	Dummy defined as 1.0 if one or more changes occur.
Ownership governance – BEGPAREN, BEGDAU, BEGINDEP	Dummy variable. Defined as one or zero depending on whether: parent, daughter, or independent.
Change in governance – six dummy variables	Defined as six dummy variables – a change is indicated by 1.0 (otherwise zero) for: Parent to daughter: PARDAU Parent to independent: PARIND Daughter to independent: DAUIND Daughter to parent : DAUPAR Independent to daughter: INDDAU Independent to parent: INDPAR
International subsidiaries, joint ventures, etc. – Three dummy variables.	Dummy variables: BEGINTER is 1.0 if foreign subsidiary exists in beginning. LOSINTER is 1.0 if foreign subsidiary is lost. GETINTER is 1.0 if foreign subsidiary is added.
Foreign Owned – three dummy variables	BEGFOROW is 1.0 if foreign owned at beginning LOSFOROW is 1.0 if foreign ownership is lost. GETFOROW is 1.0 if foreign ownership is gained.
Geographical location – REGTYPnn	111 labor market areas combined into 9 regions based upon structural similarities. Stockholm region is the omitted dummy variable.
Change in geographical location CHLOCATI	One or more changes in labor market area during the period of observation.

Methodology

Since we have the population of businesses in Sweden for our database, we can conduct regression analysis and interpret the results for relative affect upon the dependent variable, i.e., business growth rate. To facilitate ease of interpretation, we will use a straightforward linear model without any transformations of the

variables. The error term is assumed to be normally and independently distributed with constant variance. The assumption of normal distribution seems in our case to be valid asymptotically based on the fact that the number of our observations exceeds eleven thousand. However, the assumption of constant variance was not valid based on the results obtained by the White [18] test. This was remedied by using White's heteroscedasticity-consistent covariance matrix.

Another important issue is the underlying statistical assumptions regarding the residual in the regression. When the data generating process is characterised by cross sectional observations, as the case is in the present study, one might suspect that the assumption of homoscedasticity is not fulfilled. By homoscedasticity is meant that the disturbance variance should be constant at each observation point and that the disturbance covariances at all possible pairs of observation points are zero. A failure of this condition to hold leads to invalid inferences whenever the traditional formula for the ordinary least squares (OLS) variance is utilised in the construction of, for example, t-statistics. It is therefore important to test for the presence of heteroscedasticity. The commonly applied White [18] test for heteroscedasticity is a very general test in that it covers a wide range of heteroscedastic situations.

We applied the White test and the results, not presented but available on request, showed that the null hypothesis of homoskedasticity could be rejected strongly. This means that the variance of the residuals is not constant and any reference based on this variance is likely to be misleading. As is well known the unbiasedness of least squares is unaffected by violation of the assumption of homoscedasticity. However, the effectiveness of least squares is affected if the variance is not constant. To remedy this issue White suggests a correction for heteroscedasticity. He has derived a heteroscedasticity-consistent covariance matrix for calculating standard errors and t-statistics. In the presented study we have used that matrix for that purpose.

When building an econometric model, the assumption of parameter stability is widely used because of the resulting simplicity in estimation and ease of interpretation. We checked for parameter stability by using the recursive coefficients. By studying the behaviour of the recursive coefficients, not presented but available by request, the parameters appear to be stable.

Results and Interpretation

Table 3 below shows the results of the regression. We used stepwise regression with each variable entering the equation if the value of B was statistically significant when the variable was added to the equation. Significance was defined at a probability of 0.05 or less. Table 3 shows the variables that entered the equation given this criterion for entry. All other variables failed to enter the equation, i.e., would not be statistically significant if they entered the equation.

Table 3 shows the normalized regression coefficients. These coefficients represent each independent variable's comparable affect upon the dependent variable. Thus, the larger the coefficient, the greater the relative affect upon the dependent variable. Thus, to facilitate interpretation, we have rank ordered the list of variables in Table 3 by size of normalized regression coefficients.[1]

Table 3

REGRESSION RESULTS RANK ORDERED BY NORMALIZED BETA COEFFICIENTS

Variable	Coefficient Sign	Standardized coefficient	Statistical Significance
1. AGE-4	Negative	0,319	0,000
2. BEGINDEP	Positive	0,180	0,000
3. BEGINDU7	Positive	0,101	0,000
4. BEGINDU6	Positive	0,090	0,000
5. BEGINDU13	Positive	0,073	0,000
6. BEGLEG	Positive	0,073	0,000
7. BEGSIZE	Negative	0,071	0,000
8. DAUIND	Negative	0,067	0,000
9. CORPSIZE	Negative	0,065	0,000
10. PARIND	Negative	0,056	0,000
11. BEGINDU8	Positive	0,053	0,000
12. INDDAU	Positive	0,050	0,000
13. PARDAU	Negative	0,042	0,000
14. BEGINDU10	Positive	0,039	0,000
15. BEGINDU12	Positive	0,036	0,000
16. BEGINDU2	Negative	0,029	0,004
17. BEGINTER	Negative	0,028	0,004
18. BEGINDU4	Negative	0,027	0,005
19. REGTYP6	Negative	0,026	0,015
20. BEGPAREN	Positive	0,024	0,029
21. CHLOCATI	Positive	0,020	0,015

R-squared = 0.2318	Mean dep. Var = 5.9436	Log likelihood = -43657.25
Adjusted R-squared = 0.2292	Prob(F-statistics):0.000	F-statistics = 98.932
S:E of regression = 1,196,450	S:D: dep var. = 13.590	Durbin-Watson stat = 1,897,961
Sum squared resid. = 1,597,832	Akaike info criterion = 4.967	Schwarz criterion = 4.984

[1] Since the data are a census of all businesses, statistical significance is not a test of sample value as a population estimate. However, a census statistical relationship may occur due to measurement error that is always a problem with empirical data. Such error is stochastically distributed so the tests of significance listed here are a safeguard against including variables in our results that may appear due to chance alone because of measurement error. It should be noted that with over 11,000 cases, coefficients tht are not significant at the .05 probability level represent very small effects.

Given the large number of observations in the database, the regression is able to handle the large number of independent variables we have designated in Table 2 and sort out 21 as significant in determining the business growth rate index.

Age and Independence

As others have found, age of business is significant and negative, i.e., older businesses grow more slowly. And age has the most influence on the growth rate index. Second in influence is beginning as an independent business firm, i.e., no corporate ownership. Interestingly, these two variables describe Schumpeterian entrepreneurship, i.e., young or new, independently owned firms. Interestingly, variable number 20 in the rank order is "beginning as a parent." It impacts positively, although weakly, upon the business growth rate. This means that the firm is independent and has more than one establishment at its first appearance in the database. Independence remains a major factor, but beginning with more than one establishment adds to the growth rate.

Three Industries

The next three variables in the ranking are specific industry sector dummy variables. The positive sign on these dummies indicates that these industry sectors show greater impact on growth than the omitted industry "metal working and manufacturing." We chose this industry for omission because it is very large in Sweden, a a stable but cyclical industry, and it has a relatively moderate growth rate. The positive sign indicates that these three industries contribute more to business growth rates than the omitted industry. "Other knowledge intensive services" (including computer services), "technical consultants," and "education and health care" are widely acknowledged as above average growth industries. The high rank order of these industry variables and the appearance of eight of the industry variables in the regression equation suggest that industry effects upon growth rates are very important. This conclusion can be made with great certainty here because of our use of "business" as the defining entity thereby eliminating the blurring of industry influence on growth. The lower levels of industry impact reported by others may be due to their use of either establishment or enterprise definitions.

Legal Form

The sixth variable in the ranking is beginning legal form. The positive coefficient here means that the limited liability form improves the growth rate ratio of firms. This confirms what others have found.

Business Size

Variable number seven is beginning size and it has a negative coefficient. This means that smaller businesses have greater growth rate ratios thereby agreeing with other researchers' findings. The position of this variable in the ranking may be lower than expected by proponents of entrepreneurship because the growth ratio we used tends to reduce the size of the variable's influence on growth by using average size, rather than beginning size, in the denominator. As noted by Kirchhoff and Greene [9] use of this ratio is a comparative static approach to measuring the very dynamic phenomenon of entrepreneurship and therefore distorts the full effect of new firm formation and growth. Thus, our use of a statistically appropriate dependent variable has yielded a less dynamic measure of growth which in turn probably depresses the influence of business size. Nonetheless, business size remains an important factor.

Business size is closely followed by the owner overall organization size variable. The relationship is negative indicating the smaller owner organization, the greater the growth rate. This agrees with other research findings where enterprise (or firm size) has been the unit of analysis and small enterprises have greater growth rates. It also suggests that the greater resources that might be available from a large corporate owner are not adequate to overcome some other aspects of corporate ownership that depress growth rate.

It is important to note that the database contains firms with 20 or more employees in 1996. This probably leads to exaggeration of the negative effect of business size. However, this should not have any effect on the impact of overall enterprise size. Our choice of growth rate ratio as the dependent variable also disfavors small businesses relative to a rate based upon beginning size alone. As many other studies have found a negative size and growth relationship, we should be safe in interpreting the sign of our estimated effect as real although its magnitude may have been incorrectly estimated.

Change in Governance

The eighth variable in rank order is change from daughter to independent. This means that the business was "spun-off" from the parent into an independent business. The negative coefficient indicates that the effect of this action was a reduction in the growth rate. Undoubtedly, the two events -- spin-off and decline in employment -- are linked but neither is clearly the cause of the other. The reason for this negative relationship probably resides in an exogenous factor – the economic recession of 1990-93. It is likely than many businesses suffered declines in business activity and used mechanisms such as spin-offs and closures to reduce their operating costs. And, this was done along with layoffs of employees.

Additional governance change variables also appear in the equation at similar normalized beta coefficient values. The tenth variable is change in governance from a parent to an independent. This means the parent has spun-off or closed its daughter businesses and experienced declining growth in employment. This is also consistent with the above discussion of the recession's impact on business firms but yields no clear information about cause and effect.

Number 12 is change from independent to daughter. This means the independent business was acquired by a larger firm with a positive impact upon growth. This suggests that the greater resources of the large firm are used to facilitate greater growth in the business. Such resources may be more than capital and could be specialized personnel, established distribution systems, greater marketing knowledge and skills, etc. Number 13 is change from parent to daughter with a negative impact on growth. This represents an acquisition of a parent business by another firm. This acquisition, in contrast with the acquisition of an independent business, has a negative impact upon growth. This may be due to the parent business becoming distressed and laying off employees before being taken over by another firm while in distress.

More Industry Sectors

Close to these governance variables in beta coefficient value are beginning industries 8, 10, 12, 2, and 4. Variables 8, 10 and 12 have positive coefficients indicating that these industries have above average growth impact on businesses within them. These industries are "banking, insurance and finance," "retail and wholesale," and "transportation and communication." Variables 2 and 4 have negative coefficients showing that these industries have below referred industry impact on businesses within them. Industry 2 is "wood, paper and

pulp" and industry 4 is "mining and steelworks." No surprises here but this does reinforce our findings that industry sectors have significant impacts on business growth rates.

Foreign Operations

Business with foreign subsidiaries had lower growth rates than those without such subsidiaries. Cause and effect is difficult to decipher here. The recession could be an exogenous cause, i.e.; the decline in overall economic activity may have hurt business with foreign subsidiaries more than others. Or, the foreign subsidiaries may have been widely used to "export jobs" to lower labor cost areas thereby reducing Swedish employment. Or, the growth of the subsidiaries may have shifted delivery of goods and services from export of value added by Swedish employees to foreign domestic production. This may have been necessary to preserve market position in the foreign nations in the face of increasing restrictions on imports. Whatever the cause, the effect of foreign subsidiaries was to reduce the growth rates of businesses that have them.

Location

Only one region type, Region 6 is significant and negative in its direction. Region type 1, "Stockholm," is the omitted dummy variable because it is the fastest growing area in Sweden. Since Region type 6 is negative, this means that its impact upon business growth rates is negative compared to Stockholm. Region type 6 is a grouping of many smaller communities in Sweden that share the characteristics of a mixed economic structure that is average for Sweden as a whole. These communities have no characteristics that make them different that "average." They have not special industries, business activities or population growth that make them special. Apparently, the affect of the declining economic conditions during the recession depressed the growth of businesses therein. Given that the affects of industry specific factors have already entered the equation, the growth affects of this region is broader than any single industry sector can explain.

Change in location, however, has a positive affect on business growth rate. Cause and effect is not apparent here. It is possible that fast growing businesses move more often than slower growing businesses. For example, faster growing manufacturing and service businesses will outgrow the physical facility and must necessarily move to larger quarters. Or alternatively, moving a business may increase its growth rate. This is definitely possible for retail businesses and other location sensitive businesses such as banking.

However, the location variables are weak, among the weakest in rank order. Thus, region affects are minor compared to other factors.

Missing Variables

Many of the variables we included in our regression analysis do not appear as significant in our equation. Their absence provides insight into their influence on growth rates. First, change in industry sector is absence from the equation indicating that such changes have little influence on growth. This is also true for change in legal form. Apparently, growth oriented firms are or enter in the limited liability legal form and no additional change is necessary to achieve growth. Foreign ownership is also not significant and not in the equation. Thus, foreign ownership is neutral in its affect on growth suggesting that foreign ownership does not bias business growth performance in any specific direction.

Perhaps most significant is the absence of most of the geographical region variables and the very small affect of the two that do appear. This suggests business growth rates are not significantly affected by the location of the business. This is contrary to all the views of economic development directors who prefer to believe that their city or region is the best location for businesses.

Summary and Conclusions

We began this research as a quest for understanding what factors contributed to business growth rates in Sweden. We identified numerous categories of variables from previous research. We then used our own knowledge of business activity along with the wide assortment of measures available in the Swedish database to create a model of the factors underlying business growth rates. The results of the regression analysis show us no surprises compared to research by others. Business age (the younger the better), business independence, business size (smaller is better), and limited liability legal form are all confirmations of previous research. Importantly, we demonstrate that Swedish businesses are largely influenced by the same factors as reported for other nations, the U.S., Germany and Scotland. There seems to be a universality of these factors in all western capitalist nations.

The addition we make to the literature is the appearance of strong influence of industry sectors upon business growth rates and the clear indications of which sectors contribute to above or below average growth. Another unique contribution is identification of the impact of mergers, acquisitions and spin-offs upon business growth rates. Although one of the variable's impact is not in the direction expected, this results may be conditioned by the occurrence of a recession in the fourth through seventh year of the data.

From the entrepreneur's perspective, these results are quite positive because they suggest that the factors that underlie growth are largely in the command of the business owner/manager. Age, of course, simply takes time and survival. But beginning size, industry sector, legal form, independence of ownership are all choices made by the owner/manager. Location is unimportant so the entrepreneur is free to locate where ever s/he lives. In addition, the fact that many of the effects are weak and offer limited explanatory is actually good news for entrepreneurs. Weak effects mean that entrepreneurial determination and creativity can overcome most of these effects and find opportunities to achieve growth. But, then it may be that ambitious entrepreneurs have always known this intuitively as indicated by a variety to anecdotes on successful growth business start-ups.

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