

THE MODERATING EFFECT OF EXTERNAL ENVIRONMENT ON THE RELATIONSHIP BETWEEN MARKET ORIENTATION AND BUSINESS PERFORMANCE: A QUANTITATIVE APPROACH

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ABSTRACT

The purpose of this study is to examine the moderating role of external environment on the relationship between market orientation (MO) and business performance of small and medium enterprises (SMEs) in Punjab, Pakistan. This study seeks to resolve the inconsistencies found in the contemporary literature regarding the relationship between MO and business performance. Questionnaire using a 5-point Likert scale was adopted from previous researcher's work to ascertain the responses of the respondents. Survey research design was adopted and self administered questionnaires were used to collect the data from SMEs. The analysis was conducted using SPSS 20. The major findings of the study indicated that market orientation has a significant relationship with business performance while external environment plays a moderating role between market orientation and business performance.

Keywords: market orientation, external environment, business performance, SMEs

1.0 INTRODUCTION

The current business environment has become increasingly competitive and challenging. In this cutthroat business environment, researchers and marketers must identify the methods and routes for improving business performance to stay longer in the market. Several researchers have studied market orientation and contributed in the extant literature (i.e. Kohli & Jaworski, 1990; Narver & Slater, 1990; Rueket, 1992; Jaworski & Kohli, 1993; Greenley, 1995; Mahmoud *et al.*, 2010). Researchers argued that market orientation plays an indispensable role in achieving superior performance both in developing and developing economies of the world (Kuada & Buatsi, 2005; Osuagwu, 2006; Dwairi *et al.*, 2007; Hinson *et al.*, 2008; Mahmoud *et al.*, 2010).

The study of market orientation and business performance relationship has extensively been researched over the past two decades showing mixed findings. Researchers i.e. Slater and Narver (2000); Pelham and Wilson (2001); Agarwal and Dev (2003); Wei and Morgan (2004); Tajeddeni, Trueman and Larsen (2006) and Snoj *et al.*, (2007) showed a positive and significant relationship between the two constructs. On the other hand, Au and Tse (1995) reported a negative relationship between MO and business performance. While Mokhtar, Yusoff and Ahmad (2014) and Oztoran, Ozsomer and Pieters (2014) in their study found mixed findings between MO and business performance relationships. Therefore, the study between market orientation and business performance relationship is inconclusive. Suliyanto and Rahab (2012) recommended the inclusion of external environment as a moderator on the relationship between market orientation and firm performance.

Researchers also questioned the universal application of MO in different context, because there exist differences in environments, industries and their structures as well as the size of firms (Pelham & Wilson, 1996). Most of the attention in MO implementation is focused on larger organizations, while the research of MO within small and medium enterprises (SMEs) sector has been scanty (McLartey, 1998; Lee *et al.*, 1999; Becherer *et al.*, 2003). SMEs are vital in almost all the economies of the world. In Pakistan most of the enterprises are SMEs, which contribute 40 percent to GDP and have been identified as the catalyst in employment generation and poverty reduction (Khawaja, 2006). However, there is paucity of enough studies of market orientation and business performance among SMEs in Pakistan. Evidence shows that owners or managers of SMEs may not appreciate the role of market orientation as a strategic tool for quality decision-making in the SME sector and instead use intuition to gather the market information.

This study however address as this gap and contribute to the literature by incorporating external environment as a moderator on the relationship between market orientation and business performance of SMEs in Pakistan. Following section reviews the literature leading to research hypotheses. Thereafter the detail of the research methodology is presented. This is immediately followed by the description of empirical results. Finally conclusions on the basis of the research findings are enumerated and limitations and directions for future research are provided.

2.0 LITERATURE REVIEW

2.1 Market orientation and business performance

Market orientation is organization culture that produces necessary behavior to create superior value to customers and enhanced performance (Slater & Narver, 2000). According to Narver and Slater (1990) behavioral theory of market orientation consists of three behavioral components: customer orientation, competitor orientation and interfunctional coordination. Deshpande *et al.*, (1993) stated that market orientation is to implement the market culture which focuses on the market's competitiveness which in turn increase customer satisfaction and performance. On the other hand Kohli and Jaworski (1990) proposed that market orientation construct is composed of three elements which are (1) intelligence generation, (2) intelligence dissemination, and (3) responsiveness. The main objective of any organization is to involve in working towards meeting the customers' requirements and to create satisfied customers. According to Kohli and Jaworski

(1990) organizations need to constantly innovate their products, services and their business operations in order to be competitive and survive in the market place.

The study on market orientation and business performance relationship has extensively been researched over the past two decades with researchers generally agreeing on its positive outcome. However, most of the previous studies have focused on its applications in large scale organizations. Blankson *et al.*, (2006) and Keskin (2006) observed that only recently researchers have begun to study the effect of MO in small and medium enterprises (SMEs). SMEs need to be more customer focused, monitor the competitive trends and strategies of competitor and respond effectively and appropriately to the market intelligence in order to survive successfully (Mahmoud, 2011). Raju *et al.*, (2011) evaluated that SMEs generally have a better understanding of MO and they compete effectively with the larger organizations. Extant literature has revealed mixed findings on the impact of market orientation on firm performance. Therefore, market orientation orientation to performance relationship studies is inconclusive. Some studies discovered positive association between the MO and performance (i.e. Jaworski & Kohli, 1993; Pelham, 1997; Pitt *et al.*, 1996; Pulendran *et al.*, 2000; Ruckert, 1992; Kara *et al.*, 2005; Kirca *et al.*, 2005). Whereas, Au and Tse (1995) reported a negative relationship amid MO and business performance. On the other hand, Mokhtar *et al.*, (2014) and Oztoran *et al.*, (2014) in their study mixed findings amid the relationship between market orientation and business performance.

Moreover, several other researchers i.e. Shehu and Mahmood (2014a) and Kelson (2014) studied MO to business performance relationship with both positive and negative outcomes.

H1: Market orientation has a significant effect on business performance

2.2 External environment as a moderator

External environment has been described as those factors and situations that are capable of dictating and influencing the performance of firms (Mohd, 2005). The various factors and forces and that make up the external determinant could be problems or opportunities especially in the current competitive business environment to the firm and consequently can effectively determine their competence and performance (Arowomole, 2000). Kuratko and Hodgetts (2004) noted that external environmental factors could directly or indirectly influence the entrepreneurial decisions, thereby also affect the firm's performance. Wood *et al.*, (2000) highlighted that the external environment in which firms function is uncertain, complex and constantly changing and competition is one of the significant characteristic of the external environment.

Slater and Narver (1994) explored that the firms that identify the existence and intensity of competition have a greater tendency to recognize and evaluate the information to be competitive and produce higher performance. In a similar context, Wood and Bhuian (1993) the ability of a firm to recognize the threat from the competitors drives the firm to formulate customer focused strategies to fulfill their requirements and enhance the performance. Thereby, there is a greater tendency to adopt market orientation when competition is perceived as a threat by the firm (Wood *et al.*, 2000).

Several researchers suggested that the inconsistent findings between MO and performance may be moderated by external environmental factors (Greenley, 1995; Han *et al.*, 1998; Homburg &

Pflesser, 2000; Jaworski & Kohli, 1993). Ellis (2006) studied on a Meta analysis of market orientation and performance strongly supported that moderators influence the market orientation-performance relationship. Moreover, several studies have investigated the influence of different environmental factors on the effectiveness of organizational performance (i.e. Slater & Narver, 1994; Jaworski & Kohli, 1993; Greenley, 1995; Han *et al.*, 1998). Kohli and Jaworski (1990) argued that in transition economies firms should monitor and determine the influence of external environment on market orientation to develop a strong market-oriented culture.

The above mentioned arguments, however, are in consistent with the assumptions of contingency theory that focuses on the fit concept. That is there should be a fit between intended strategy and external environmental factors to improve the firm's performance. This study adopted external environmental factors i.e. market turbulence and competitive intensity to determine the moderating effect amid market orientation and business performance relationship. On the basis of above discussion following hypothesis is formulated,

H2: External environment moderates the relationship between MO and business performance.

3.0 RESEARCH METHODOLOGY

3.1 Research design

The study adopted a quantitative approach using a questionnaire protocol to collect data from respondents SMEs. In this study, 364 SMEs were extensively surveyed, to ascertain the moderating effect of external environment on the MO and business performance relationship. The hypothesized relationship have been evaluated and validated by employing SPSS 20. This study was a survey field study and was conducted in real-life situation that systemically investigated relationships amid variables.

Survey research was employed as it has more scope and coverage; moreover it is less expensive and commonly used method. According to Neuman (1997) survey mode facilitates the researcher to collect data from many respondents to measure many variables in the study and to test the hypotheses. In addition, to achieve the research objectives, cross-sectional research was used. Cross section approach involves gathering the data at one point in time from the firm (Cavana, Dalahaye & Sekaran, 2001).

Items of the questionnaire were adopted from previous researcher's instruments. Face and content validity was ensured. Five-point Likert scale was used to measure all the items of questionnaire. Three measurements were used in the study. Sixteen items of Market Orientations were adapted from (Narver & Slater, 1990), External environment eight items were borrowed from (Jaworski & Kohli, 1993) and six items of Business Performance were adopted from (Valmohammadi, 2011; Yusuf *et al.*, 2007; Jaworski & Kohli, 1993).

The population included the small and medium enterprises (SMEs) in Pakistan. Data were collected from Owner/manager of SMEs. The sample size was 380. Email and drop and pick approach were used to collect the data. A total of 500 questionnaires were distributed and 367 completely filled questionnaires were collected. Response rate was 73 percent. SPSS 20 was used for analysis. Factor analysis was conducted to check the reliability and validity of the

instrument. Multiple regression and hierarchical regression were employed to test the research hypotheses.

3.2 Sampling Technique

The sampling technique used was simple random sampling. It allows the sample to be selected randomly and there is less biasness (Sekaran, 2003).

4.0 DATA ANALYSIS AND RESEARCH FINDINGS

4.1 Reliability

Cronbach alpha was calculated for each construct to assess the internal consistency and reliability. Nunnally (1978) stated that internal consistency is one of the methods to determine the reliability. Whereas reliability refers that the research instrument is error free and yield same results on repeated trials. Generally, alpha value of 0.70 or more are considered good and satisfactory (Nunnally, 1978). The results in Table 1 show that the Cronbach's alpha values of all the constructs, Market Orientation, External Environment and Business Performance ranged between 0.705 and 0.802, indicating a high reliability of the scales.

Table 1

Reliability Analysis

Variable	No of items	Cronbach's alpha
Market Orientation	16	.802
External Environment	8	.708
Business Performance	6	.705

4.2 Regression Analysis

To answer the research hypotheses, the questionnaires collected from 364 respondent SMEs were analyzed using multiple regression technique. SPSS software 20 was used for analysis to get the value of R, R^2 , the Beta value and the value of significance. Multiple regression analysis was conducted to examine the relationship between dependent variable (BP) and the predicting variable (MO). Table 2 model summary exhibits the result of independent variable (predictor) against business performance. R (0.843) is the correlation between independent variable (MO) and dependent variable (BP). Whereas R square value (0.710) explains that 71% variance in business performance is explained by predicting variable market orientation. These suggest that 71% of business performance is explainable using variable of Market Orientation. Hierarchical regression analysis was employed to test the moderating effect of external environment (EE) on the relationship between MO and business performance. The findings of the analysis show that EE moderates the relationship between MO and BP.

Table 2

Model summary

Model	R	R Square	Adjusted R Square	Durbin-Watson
1	.843	.710	.709	1.669

According to the results reported in Table 3, MO ($\beta = 0.843$, $t=29.898$, $p=0.000$) has a significant positive relationship with business performance. This shows that with effective implementation of MO the firm can improve its performance by increasing its sales and profitability. Moreover, EE ($\beta = 0.128$, $t=4.124$, $p=0.000$) plays a moderating role between MO and business performance. Hence H1 and H2 are accepted.

Table 3

Results of Multiple Regressions

Hypothesis	B	t	P value	Conclusion
H1	.843	29.898	.000	Accepted
H2	.128	4.124	.000	Accepted

5.0 CONCLUSION

SME sector plays a very vital role in the economic prosperity and industrial progress of a country, such as efficient domestic resources usage, equitable income distribution, employment generation, exports, social stability and regional development (Dasanayaka, 2011; Malik *et al.*, 2010; Bhutta *et al.*, 2009). According to The Economic Survey of Pakistan (2005) in reality SME sector portrays the growth and progress of Pakistani business environment, therefore better the performance of SME sector; the superior and better quality of products and services will be produced in Pakistan. SME sector contributes approximately 40 percent in the annual GDP (SMEDA policy, 2007). Sherazi *et al.*, (2013) observed that despite of vital contribution of SMEs in economy of the country, Pakistani researchers and practitioners have not given adequate attention to enhance the productivity of SME sector. SMEs are less productive and show suboptimal performance due to lack of managerial skills, insufficient capital, inconsistent govt policies, unavailability of appropriate and timely information etc.

The finding is in consonance with the findings of the previous studies conducted by Aziz & Yasin (2010), Kirca, Jayachandran & Bearden (2005), Narver & Slater (1990), and Kohli & Jaworski (1990). The facts indicated that, if Pakistani SMEs want to become the top contributor of the country's economy, the owners and managers need to be more market oriented and innovative. The study recommended that SMEs must implement market orientation aligning with external environment to enhance the business performance. The SME sector is the backbone of the Pakistani economy, so the proper implementation of MO could give some tremendous results by boosting the performance of SMEs and contributing in the economy of the country.

Managers of SMEs would be able to reap the various benefits of implemented strategy by aligning different management strategies i.e. Market Orientation with external environment factors to deliver better products and services to customers. The findings indicated that external environment moderates the relationship between market orientation (MO) and business performance of SMEs. The study found support for aligning Market Orientation with external environment to contribute towards higher SMEs business performance. The findings suggests that firms should take strategic decisions to serve better in the marketplace and are able to satisfy existing and future demands and needs of customers. Moreover the results also contributed to the literature and strengthen the contingency theory, which states that strategies must be aligned with external environmental factors to achieve higher performance.

The positive relationship between MO and Business performance measures shows the significance of market orientation to improve firm's sustainability and performance. The implementation of MO may guide managers on how to coordinate with customers, motivate employees and ascertain the competitor's strategies in order to improve firm's performance. Through frequent communication with and feedback from the customers, a firm can fulfill the needs and requirements of the customers accurately and by timely delivering high quality and reliable products or services will enhance the performance. Moreover, by systematic measurement of customer feedback and using it in the improvement of product/service can increase customer satisfaction. When a firm anticipates the current and future needs and expectations of customers' and addresses their complaints accurately and on time, the firm can improve its sales, market share, and profitability by investing in profitable areas.

The sample of the study consists of the SMEs in Punjab region only, so the response cannot be generalized to other regions, therefore there is a need to conduct the study on other parts of the country for in depth understanding. The study can be extended by considering other variables such as organization culture or organizational structure as a moderator.

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