

# Relationship between Organisational Culture and Entrepreneurial Orientation: Indonesian SMEs Context

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**Abstract.** The purpose of this paper is to investigate the relationship between organisational culture (OC) and entrepreneurial orientation (EO). This study was based on a questionnaire survey which was applied to the owners or managers of small and medium sized enterprises in Indonesia. Total of 463 responses were obtained. Semi-structured interviews to 8 respondents were also carried out. The results showed that there was significant relationship between OC and EO. It was found that OC is a relevant predictor to EO. Hence, EO achieves better results when it is supported by appropriate organisational culture. This paper adds to the current literature by providing empirical work correlating organisational culture to entrepreneurial orientation in SMEs.

**Keywords:** Entrepreneurial Orientation, Organisational Culture, SMEs

## 1. Introduction

The development of entrepreneurship has also long been attributed to culture. Some cultures are more conducive for entrepreneurship than others, considering the different cultural heritages and business practices<sup>1, 2</sup>. Thus, culture has been shown to influence the ability of an organisation to affect the organisational process<sup>3</sup>, to improve commitment, loyalty and reduce bureaucratic costs<sup>4</sup> and increase performance<sup>4, 5</sup>. Entrepreneurial orientation (EO) is critical for the development of companies as well as for the economic and gives a useful framework for researching entrepreneurial activity<sup>6</sup>. Meanwhile other study pointed out that certain cultures are more favorable to the development of entrepreneurial orientation<sup>2</sup>. A few studies examined the relationship between organisational cultures and performance and between entrepreneurial orientation and performance. But very few explored the relationship between Organisational Culture (OC) and EO. In addition, previous studies were carried out in larger firms. Therefore, this present study attempts to gain insights on the possible relationship between organisational culture and the entrepreneurial orientation in the context of SMEs in Indonesia. In order to reach this objective, the concepts of OC and EO are explained below.

## 2. Literature Review and Conceptual Model

### 2.1. Organisational Culture

Culture has been characterized by many authors as “something to do with the people and unique quality and style of organisation”, “the way we do things around here” or the “expressive non-rational qualities of an organisation”<sup>7</sup>. However, social scientists began to converge on an operational definition of culture as the attitudes, values, beliefs, and behaviors that are shared by a particular group of people<sup>2, 3, 8, 9, 10, 11</sup> i.e. a definition that uses identifiable, measurable, and enduring behavioral components. The major reason for the wider interest in organisational culture stems from the argument that certain organisational cultures lead to superior organisational financial performance<sup>12</sup>. Researchers found that cultural strength was significantly associated with financial performance both short term<sup>13</sup> and long term<sup>4</sup>. Culture also affects an organisation’s competitive position because of benefiting from having highly motivated employees dedicated to common goals<sup>14</sup>, influencing the organisational performance<sup>4</sup>, and developing organisational competences and obtaining competitive advantage<sup>15</sup>. Overall, organisational culture can be the factor that sends an

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organisation to greatness as its members are inspired to do their utmost to work hard to conceive and make goods and services that improve the welfare of their customers and hence develop organisational competences and obtain a competitive advantage<sup>15</sup>. This illustrates that organisational culture is a determinant of entrepreneurial orientation, which refers to all aspects related to processes, practices and decision and decision making activities, which lead to adopt or acquire the new venture creation<sup>6, 16</sup>.

There are three commonly accepted aspects of organisational culture, namely: bureaucratic; innovative; and supportive<sup>17</sup>. Bureaucracy is viewed as hierarchically structured, orderly, procedural, and highly regulated. Innovativeness is seen as creative, enterprising, risk-taking, and results-oriented. Supportiveness is characterized by equitable, sociable, trusting, and collaborative behaviors. Meanwhile, other researcher has outlined dimensions of organisational culture, which covered process-result oriented, open-closed system, tightly-loosely controlled, normative-pragmatic, and employee-job oriented<sup>18</sup>. The primary assumption underlying Hofstede's influential longitudinal research is that the cultural differences influence and restrict the ability and willingness of management to operationalize certain organisational theories and management practices<sup>19</sup>. In view of their attractive characteristics, our empirical study adopted four items of Hofstede's concept to be applied to this study. Following the foregoing studies, the present study also examines organisational culture as an independent variable.

## 2.2. Entrepreneurial Orientation

Empirical studies suggest that EO is a multi-dimensional construct and can be evaluated from different perspectives<sup>20</sup>. Miller's (1983) work, which views the EO construct as innovation, risk-taking, and proactiveness, is the basis for several studies<sup>20, 21, 22</sup>. Later, a number of studies have established innovation, risk-taking, and proactiveness as EO dimensions<sup>20, 23, 24</sup>. Following Lumpkin and Dess, we define each EO construct as follows:

*Autonomy* is one of the most important stimuli for the entrepreneurs in running ventures. Autonomy is described as an independency of an individual or a team to develop business vision and carry it through completion. The autonomy will be strong whenever the entrepreneurs supported with cultures that endorse them to be independently, and opportunities seekers. *Innovativeness* refers to willingness to support new ideas, creativity, novelty, technological leadership, experimentation, and R&D in the development of new processes. It also gives large contribution to the presence of entrepreneurship. Under supporting cultures—supporting creation of new ideas, experimentation, original solutions to problem, and creative process—innovativeness will produce positive results. *Risk taking* is defined as willingness to accept uncertainty, seizing opportunity in the marketplace by making large resource commitment with expectation to achieve high returns. Only entrepreneurs with the risk take behavior and in cultural foundation of ambiguity, uncertainty and commit resource will harvest the benefits. *Competitive aggressiveness* refers to firm's tendency to compete with its rivals/competitors directly and intensely. It also refers to entrepreneurs who live in culture of achievement oriented. This dimension is becoming an important component of EO because without competitive aggressiveness, firm would not be able to survive and success in starting up a new venture. Since proactiveness dimension is identical to competitive aggressiveness<sup>21</sup> and therefore is excluded in this present paper.

Our conceptual model comprises of two substantive theoretical constructs: organisational culture as independent variable and entrepreneurial orientation as dependent variable. In this research, organisational culture as proposed by<sup>18</sup> is applied. Meanwhile, dimensions of entrepreneurial orientation are adopted from<sup>16</sup> i.e., autonomy, innovativeness, risk taking, proactiveness, and competitive aggressiveness. Following<sup>21</sup>, we exclude proactiveness dimension in this paper.

## 3. Approach, Discussion and Findings

In this study, items were adapted from previous studies and modified. All constructs were measured multiple items in a five-point Likert-type scale (1 – disagree strongly, 5 – agree strongly). Content validity was made and the questionnaire was refined through rigorous pre-testing for wordings. Final questionnaires were distributed to SMEs in SMEs trade centres and in exhibitions in Jakarta. The questionnaire is composed of background of the SMEs and 5 dimensions of OC and four dimensions of EO. The questionnaire has forty two items in total. The key informants in the survey were owners or managers of SMEs. Data were collected through personal face to face interview. Data were collected from various types of industries such as handicraft, leather, furniture, and pharmaceutical. The total useable questionnaires were 250 from 463 respondents.

Two stages of statistical analysis were performed. First, factor analysis was performed to investigate the dimensions of OC and EO. Next, regression model was applied to examine the effects of the OC on EO. The basic assumptions with respect to the constant variance, and normality were thoroughly verified and did not affect the results. Bartlett's Test of Sphericity and Kaiser–Meyer–Olkin measure of sampling adequacy (KMO-MSA) were considered important in determining the appropriateness of the data for factor analysis. KMO has to be more than 0.60 and Bartlett's Test of Sphericity has to be significant. For factor analyses, principle components analysis and Varimax rotation were performed. The items that had factor loadings lower than 0.50 were eliminated. The Cronbach's alpha reliability analysis was also conducted. The Cronbach's alpha reliability values have to be above the threshold level of 0.60. The results in Table 1 show that measure of sampling adequacy is above 0.60 and Bartlett's Test of Sphericity is large and significant.

Table 1. Exploratory Factor Analysis and Reliability Statistics for Measures

Construct	Dimension	Item	Factor	Cronbach $\alpha$	KMO-MSA	
OC	Process-Result cultures	People put in maximal effort	.537	.697	KMO .773 Bartlett 1015.437 Significance .000	
		Manager help good people to advance	.734			
		Organisation and people are open	.675			
	Communication and Flexibility	Management stingy with small things	.579			.654
		Little attention to physical work environment	.513			
		Organisation contributes little to society	.574			
		Results more important than procedures	.654			
		Never talk about the history	.650			
	Tightly-Loosely Cultures	Meeting times kept punctually	.650			.708
		Typical member well-groomed	.806			
EO	Opportunity, Risk and Innovativeness	Always speak seriously of organisation and job	.752			
		Willingness to identify opportunity	.643	.832		
		Capacity to identify opportunity	.508			
		Evaluate downside risk	.603			
		We actively introduce improvements and innovations in our business	.810			
		Our business is creative in its methods of operation	.650			
		The product covers more customer needs	.776			
	The product is of higher quality	.539				
	Work that requires original thinking	.548				
	Competitive Aggressiveness	Our business is intensively competitive	.812	.747		
In general, our business takes a bold or aggressive approach when competing		.812				

The original OC scale had 23 items and 5 dimensions (orientation, communication, control, flexibility and employee oriented vs. job oriented). The factor rotation produced five dimensions from a total of 23 variables. Five items with a factor loading lower than 0.50 was eliminated. Based on the results of factor analysis, two items from process-oriented versus results-oriented culture, one item from pragmatic versus normative culture, and one from job-oriented versus employee-oriented culture came out as one factor. The same result was also found for two items from process-oriented versus results-oriented culture. However, the reliability of these factors was below 0.60. Therefore, these factors were excluded from the analysis. Factor analysis for OC reduced 23 variables to 11 variables and resulted in three factors, process-oriented versus results-oriented culture, tightly versus loosely controlled culture, and a new factor emerged, and it was labeled as communication and flexibility culture.

The EO construct initially had 19 items and 4 dimensions (autonomy, competitive aggressiveness, risk taking and innovativeness). One item with a factor loading lower than 0.50 was eliminated. Autonomy and risk taking were eliminated since the reliability of those factors was below 0.60. Two items from competitive aggressiveness, one item from risk taking and five items from innovativeness appeared as one factor and it was labeled as opportunity risk and innovativeness. Other two items from competitive aggressiveness came

out as one factor, and it was kept as competitive aggressiveness. Hence, using factor analysis, it was found that the original items were reduced to 10 items in 2 factors. Such different result which is unexpected may happen in many studies. Not all research work has managed to confirm that the variables in previous research may emerge the same in later research<sup>25, 26</sup>. A research by<sup>27</sup>, for example, was reported to face similar condition, when their later work could not replicate their previous own work. Using their own five dimensions of service quality measurement, factor analysis generated six factors rather than five.

In our present study, such unexpected result for the measures may be explained by various reasons such as different scales of business operation from the sample taken. The original concepts were built using samples from large firms in developed countries.

The organisational culture (OC) is treated as an independent variable, while the entrepreneurial orientation (EO) is treated as a dependent variable. Prior to performing regression analysis, a product moment analysis correlation of those variables was verified. Inter-correlation between variables factors in OC and EO construct did not show any multicollinearity. The analysis, reveals that there is significant relationship between OC and EO ( $R^2 = 13.7\%$ ,  $\beta = 0.370$ ,  $t$  value = 6.268 and  $p \leq 0.001$ ). The result does not only support the notion that certain cultures affect the entrepreneurial orientation<sup>2</sup>, but it also specifies to the culture that is responsible to the development of entrepreneurial orientation, i.e., organisational culture. Hence, OC is a relevant predictor to EO. In addition, the result confirms that the concepts are also applicable to smaller to medium size of firms. Based on the interviews with the owners, it was found that the organisational culture of the SMEs emphasizing on the openness e.g. the employees are encouraged to express their ideas, opinions related to their work, no communication barriers, and putting their extra effort to achieve target drives employees to identify business opportunities and to innovate in many ways such as in developing sales strategy to win the competition.

#### 4. Conclusion

The purpose of this paper is to propose a culture-based framework of entrepreneurship that may contribute to the theoretical development of entrepreneurship research by examining corporate culture and entrepreneurial orientation. Although both concepts were developed based on business practice of larger firms, this study tried to investigate the relationship between organisational culture and entrepreneurial orientation of their smaller counterparts, particularly SMEs in Indonesia. The results demonstrate that OC affects EO, which supports previous studies that organisational culture affects the entrepreneurial orientation<sup>2</sup> and influences the members of organisation to achieve their goals and develop its competitiveness<sup>15</sup>. The results suggest that this relationship could be expanded to include the performance indicator, to gain a better understanding of the relationship of both constructs on company performance.

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#### 6. References

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