

Entrepreneurial Orientation and Firm Performance: Evidence from Small and Micro-Enterprises in Kenya

Chenuos, Nehemiah Kosgei¹ Maru, Loice C.²

1. Doctor of Business Management Scholar, School of Business and Economics, Moi University, P.O. Box 3900, 30100, ELDORET, Kenya.
2. Department of Management Science, School of Business and Economics, Moi University, Nairobi Campus, P.O. Box 63056, 0200, NAIROBI, Kenya

Abstract

Entrepreneurial orientation is a significant determinant of firm performance. The multifaceted nature of EO prompted a need for a more insightful study to bring to fore the extent of effect it has on performance. Nonetheless, past research has shown that simply examining the effect of Entrepreneurial Orientation on firm performance provides an incomplete picture. To stimulate the relationship between Entrepreneurial Orientation and firm performance, there is need to control internal and external contingent factors. Using data from 333 Small and Micro-enterprises (SMEs) in Uasin-Gishu County in Kenya, the study showed that innovativeness ($\beta_1 = 0.632$, p value = 0.000) and pro-activeness ($\beta_2 = 0.246$, p value = 0.000) have positive effects on firm performance; however, risk-taking negatively effects firm performance ($\beta_3 = -0.163$, p value = 0.002). The study makes significant contributions to the understanding of the relationship between Entrepreneurial Orientation and performance of SMEs. This knowledge is invaluable to both SME owners and policy makers in designing and shaping firm and industry-level strategies that are appropriate for positive outcomes of entrepreneurship.

Keywords: Entrepreneurial orientation, Innovativeness, Pro-activeness, Risk-taking, Firm Performance

1. Introduction

Several studies have found that firms demonstrating more entrepreneurial orientation perform better (Wiklund and Shepherd, 2005). However, Smart and Conant (1994) do not report any significant entrepreneurial orientation and performance relationship. Hart (1992) argues that a firm's entrepreneurial strategy-making mode may even lead to poor performance under certain circumstances. An important message from past research is that simply examining the entrepreneurial orientation and performance relationship provides an incomplete picture of performance. A need to control internal and external contingent factors in the examination of the entrepreneurial orientation and performance relationship is apparent (Wiklund and Shepherd, 2003, 2005; Rauch *et al.*, 2004; Walter *et al.*, 2005; Covin *et al.*, 2006). Neglecting these contingent factors may lead to the 'wholesale adoption' of an entrepreneurial orientation (Wiklund and Shepherd, 2005), and forsake firms' entrepreneurial efforts. However, some studies have found that the effect of entrepreneurial orientation on performance is influenced by firm size, national culture (Rauch *et al.*, 2004), access to financial resources (Wiklund and Shepherd, 2005), network capability (Walter *et al.*, 2005), and strategic processes (Covin *et al.*, 2006).

Entrepreneurial firms constantly face complex and turbulent external environments (Lumpkin and Dess, 1996) that are fertile grounds for new information and knowledge and hence provide a context that is conducive for information acquisition and dissemination. The more entrepreneurial a firm is, the more proactively and extensively it engages in environmental scanning (Daft and Weick, 1984) and the greater the extent to which it is involved in information acquisition and dissemination (Sinkula, 1994). Furthermore, entrepreneurial firms are innovative and risk-tolerant, and therefore provide the internal environment in which learning through exploration and experimentation is most likely to take place (Slater and Narver, 1995).

1.1 Problem Formulation

Entrepreneurial orientation has been a topic of much debate in management and entrepreneurship literature for the last two decades. Furthermore, a firm should consistently take risks, innovate and be proactive in order to be labeled as "entrepreneurial" (Miller, 1983). Past studies have shown a correlation between entrepreneurial orientation and firm performance (Keh *et al.*, 2007; Lee, Lee and Pennings, 2001; Lumpkin & Dess, 1996; Zahra and Covin, 1995). However, to date, the main debate remains within the area of entrepreneurial orientation (EO) research in relation to firm performance (Covin, *et al.*, 2006).

Lumpkin and Dess (1996) draw attention to the complexity of entrepreneurial orientation and firm performance relationships and suggest that the relationship is context specific as influenced by the prevailing external environment as well as internal organizational processes. Further, entrepreneurial orientation research has been conducted mostly in the context of the United States or other developed countries and has rarely been conducted in developing countries. This study thus sought to address the gap by examining the contingent relationship between entrepreneurial orientation and performance of small SMEs in Kenya.

2. Literature Review

2.1 Innovativeness and SME Performance

In the World Bank report (2009), innovation has been viewed as vital in ensuring competitive advantage by organization and long term loyalty. The importance of innovation as a key factor of economic growth and development was also highlighted by Joseph Schumpeter in his Theory of Economic Development (1934) who considers the entrepreneur's task and capacity to realize new combinations of the production factors, and thus innovation, as the basis of his theory. According to Casals (2011), globalization of the markets and increasing international competition force SMEs to search for new, innovative, flexible and imaginative ways to survive. This provides a basis for a SME to innovate to survive. Moreover, innovation is an important ingredient in today's knowledge-based society for SME performance; although there is limited evidence on this in emerging economies. Yet SMEs need to continuously innovate to reduce production costs, delivery schedules, hence manufacturing skills, supplier relationship among other business practices (De Wit *et al.*, 2007).

SMEs that have adapted flexible production systems and competitive costs and prices have been able to capture increased market share (Kemp *et al.*, 2003). This signifies the importance of innovation in enhancing loyalty and long term customer value. Kemp *et al.* (2003) found that innovation output is determined by the innovative input, such as in the transformation of input into output. Consequently innovative output is related to the firm performance as it boosts competitiveness of SMEs in the market.

Rothwell and Zegveld (1982) assert that SMEs exhibit behavioural features that give them an innovative advantage over larger firms; for example, SMEs are thought to be more able to respond rapidly to external threats or opportunities; they have more efficient internal communications, and exhibit interactive management styles. Conversely, SMEs are thought to lack the material and technological resources that enable large firms to spread risk over a portfolio of new products' and fund longer-term R&D (Rothwell & Zegveld (1982). Thus, it is perhaps not surprising that innovatory advantage is unequivocally associated with neither large nor small firms (Rothwell and Zegveld (1982). This study thus hypothesized that *Innovativeness has no significant effect on the performance of Small and Micro-enterprises.*

2.2 Pro-activeness and SME Performance

Wisner (2004) argues that the dimensions of SME proactive orientation include, creating a greater level of trust throughout the customers, identifying and participating in additional innovative products, establishing more frequent contact with a firm's members, creating a compatible communication and involving all supply chain members in firm's product/service marketing plans which if properly implemented will lead to high organization performance. Mentzer *et al.* (2008) note that SME proactive orientation strategies depend on a close interaction with in-company marketing and sales resources, processes and skills. Supplier management and customer relationship strategy, which are consistent with proactive orientation, were found to have a positive impact on organizational performance.

Green *et al.* (2006) found that market orientation relates positively and significantly with SME pro-activeness strategies which in turn lead to higher organizational performance. This brings about a lot of marketing strategies that ensure continuous sale of product hence high firm performance. Mentzer (2007) argues that proactive orientation plays a fundamental role in implementing SME management and overall organizational performance. Tukamuhabwa *et al.* (2011) further identified a positive relationship between proactive market orientation and SME management strategy together with organizational performance. Mentzer (2007) further asserts that market orientation improves SME management through its proactive orientation.

Salvador *et al.* (2001) argue that when firms are proactively oriented through interaction with suppliers and customers regarding materials flow and quality issues, they achieve better time-related organizational performances in terms of speed and delivery punctuality. Green *et al.* (2006) suggest that suboptimal organization performance could be due to a weak marketing and proactive orientations. Mason (as cited in Green *et al.*, 2006) argues that effective SME management involves a marketing orientation and cost reduction, which improves the firm's financial performance. Cervera *et al.* (2011) found that proactive orientation, especially in supply chain, is significantly and positively correlated with global performance.

According to Juttner *et al.* (2010), management and customer relationships, which are components of proactive orientation, influence organization performance in terms of shorter end-to-end pipeline time, total costs and shorter lead-time. Therefore, higher levels of customer-oriented supply chain practices will have a positive impact on customer-oriented organizational performance outcomes.

Success of an SME depends heavily upon the success of the pro-activeness of the innovation line in which it participates as a partner (Zelbst *et al.*, 2009). Cai *et al.* (2008) also state that one of the issues that have become critical for gaining competitive advantages for companies is improving innovation and its orientation. As contemporary firms recognize that they can no longer effectively compete in isolation of other entities, they have shifted their attention from competition between firms to competition between the entire innovation chains (Hult *et al.*, 2007; Ntayi *et al.*, 2009).

Zelbst *et al.* (2010) argue that innovation orientation performance focuses on the ability of the SME to satisfy the needs of the ultimate customers which leads to high organization performance. Supply chain inefficiency has been identified as one of the most prevalent issues facing the SMEs (Lewis, 2005). Miguel *et al.* (2010) argue that a firm's need for proactive oriented employees who also possess the ability to self-manage is due to the challenging nature of the job itself. This quality leads to high performance within the organization itself. Proactive security investments are associated with longer intervals before subsequent breaches than reactive investments. Further, external regulatory pressure can stimulate organizational learning and change. It is thus evident that the interaction between external pressure and proactive investment increases the positive effects of the investment.

The implication of this line of thinking is that proactive investments, voluntarily made, have the greatest impact on security performance where managers and policy-makers should pay attention to the strategic and regulatory factors influencing security investment decisions. The implications for proactive and reactive learning with external regulatory pressure can be generalized to other industries. In many areas of organizational performance, learning has been found to be an important element of improvement. Organizational learning, which explains how organizations acquire the knowledge and skills necessary to achieve better performance, has traditionally been used to examine decisions surrounding investments for quality and volume improvement in manufacturing (Ittner, Nagar and Rajan, 2001). This paper, therefore, attempts to test the hypothesis that *Pro-activeness has no significant effect on the performance of Small and Micro-enterprises.*

2.3 Risk-taking and SME Performance

The concept of risk-taking has long associated with good SME performance (Bearse, 1982).. Early definition of risk-taking centred on the willingness of entrepreneurs to engage in calculated business risk which in the end leads to high SME performance (Brockhaus, 1980). Lumpkin and Dess (2006) identify venturing into the unknown as a definition for risk taking which leads to great firm performance. This is because it provides SMEs with foundation to grow and venture into new products without worrying about the outcomes (Lumpkin and Dess, 2006).

Studies have revealed that SMEs that take risks perform better in terms of profitability than those who do not (Bearse, 1982). Such firms are also expected to have better performance and a higher level of risk propensity (Leko-Simi & Horvat, 2006). According to Leko-Simi and Horvat (*ibid.*), risk-taking propensity is defined as a tendency to take or avoid risks and it is viewed as an individual characteristic. The positive relationship between risk-taking propensity and risk decision-making by individuals is expected to translate to organizations through top management teams' hence high performance of the SMEs (Panzano and Billings, 2005).

Risk-taking is necessary to support both innovativeness and pro-activeness in SMEs (Miller & Friesen, 1984). In addition, risk-taking fosters organizational creativity (Gilson and Shalley, 2004). Under unpredictable conditions, an organization's risk-taking propensity is positively related to new product development. It is also evident that risk-taking propensity in SME promotes and exhibits behaviours that lead to process enhancements, new products or services, and innovative practices leading to high performing SMEs.

Gupta and Govindarajan (2004) found that risk-taking has a positive influence on effective implementation of an SME's strategies which are aimed at high performance. Effective implementation means that a firm would face fewer functional barriers in formulating its strategy based on its resources and capabilities. Thus, risk-taking can play a key role in reducing functional impediments by helping to develop and implement an effective strategy. A managers' propensity to take risks (by making large resource commitments) should enhance a SME's capacity to adapt to the needs of the markets and thereby face fewer functional impediments.

Establishing a governing innovative council is a risk-taking trait that will contribute to the overall performance of an SME. A governing council's purpose is to give direction and help align innovation strategy with the company's overall strategy. Engaging in collaborative strategic sourcing is another risk-taking trait that will lead to noticeable productivity and profitability of a firm. Strategic sourcing in the risk-taking process is the cornerstone of successful SME performance.

According to Plourd (2009), the importance of risk-taking is now escalated above issues such as long-term and short-term financing constrains. Proclaiming the existence of a risk management strategy is insufficient; enterprises need to actively engage in risk management practices to address the convergence of major impediments that are facing SMEs today. The use of enterprise risk-taking can be viewed as a business competency enabling managers to optimize opportunities (Hofmann, 2009). SMEs should apply basic risk activities, embedding the risk champion's knowledge of exposures, across the entire scope of an enterprise's risks such as strategic risks, operational risks, financial risks and regulatory compliance risks. Bradford (2009) argues that a structured risk approach enables an enterprise to pursue its strategies aggressively and efficiently as management can anticipate the risk exposure of each activity engaged in, thus achieving more acceptable results at a reduced cost. This paper, therefore hypothesizes that *Risk taking has no significant effect on the performance of Small and Micro-enterprises.*

3. Materials and Methods

The study used an explanatory survey with a sample of 333 Small and Micro-enterprises in Uasin-Gishu County, Kenya. It used Yamane's (1967, p. 886) simplified formula, where Neyman allocation formula was used to distribute sample size among the strata and employing simple random sampling technique. Primary data was collected using questionnaires. Respondents were requested to indicate their degree of agreement or disagreement for each item in the questionnaire using five-Point Likert-type scale as follows: 1=Strongly Agree, 2=Agree, 3=Not Sure, 4=Disagree and 5=Strongly Disagree. The respondents were asked to indicate their level of agreement by choosing a value that corresponds to what they felt on job characteristics and their performance. Reliability of items was tested using Cronbach Alpha and the results obtained indicated acceptable values as shown in table 1.

Table 1. Reliability Analysis Results

Variables	Alpha Value	Items
Performance of SMEs.	0.738	5
Entrepreneurial orientation	0.770	18

Source: Survey Data, 2013

The data was analysed using descriptive and inferential statistics that include measures of central tendency such as mean and measures of dispersion standard deviation, and Pearson Product Moment correlation and Multiple

Regression. Inferences were drawn from the findings to answer the key hypotheses of the study. The Regression equation was stated as follows:

$$y = \beta_0 + \beta_1x_1 + \beta_2x_2 + \beta_3x_3 + \varepsilon$$

y is Performance of small and micro-enterprises, β_0 Is the constant of the equation, x_1 is Pro-activeness, x_2 is Risk-taking, x_3 is Innovativeness, β_1 . β_3 are the coefficient regression or change induced in y by each x and ε = error term

4. Results

4.1 Innovation and SMEs Performance

The study revealed that SMEs reported to lay a strong emphasis on marketing of tried and true products or services (mean of 1.93 and a standard deviation of 1.216). Further, SMEs laid a strong emphasis on research and development, which indicates that they carried out research and development but at a low level (mean = 2.06 and standard deviation = 0.97). Nevertheless, SME entrepreneurs indicated that they did not have a new line of products or services which was indicative of continuous innovation although this was applicable to just a handful of the small and micro-enterprises (mean = 3.53 and standard deviation = 1.309). This implies that though some of the SMEs practiced innovation through exploitation of new lines of products and services, many of them actually did not despite recognizing the importance of the innovation. This was also confirmed by majority of the respondents who agreed that there were very many lines of new products and services. The low levels of innovation can also be traced to the nature of the changes in product or service lines which in most cases, as agreed to by majority of the respondents, showed that the changes in product or service lines have been mostly of minor nature and that the changes in products or services have usually been quite dramatic. This points to the fact that although the SMEs pursued innovation through product and services changes, the effect of their perceived innovation does not significantly affect performance of their firms.

Table 2. Descriptive Statistics for Innovativeness with Normality Test
 (1-1.5 = Strongly Agree, 2 = Agree, 3 = Neutral, 4 = Disagree, 5 = Strongly Disagree)

	Mean	Std. Deviation	Skewness	Kurtosis
A strong emphasis on the marketing of tried and true products or services	1.93	1.216	1.594	1.657
A strong emphasis on research and development	2.06	0.97	0.824	0.415
No new line of products or services	3.53	1.309	-0.686	-0.806
Very many new lines of products or services	2.45	1.108	0.861	0.123
Changes in product or service lines have been mostly of minor nature	2.5	1.337	0.836	-0.481
Changes in products or services have usually been quite dramatic	2.51	1.138	0.43	-0.611
Average Mean for Innovativeness	2.4974	0.69619	0.797	0.538
Reliability (Cronbach's Alpha)	0.734			

Source: Survey Data, 2013

4.2 Pro-activeness and SMEs Performance

As shown in Table 3, SMEs typically respond to actions which competitors initiate (mean = 1.93 and standard deviation = 1.076). This was also indicated by the way the competitors behave in the face of competition, that is,

they respond to actions which the respondents initiate in their businesses (mean = 2.37 and standard deviation = 1.066). This generally signifies a push and pull between the competitors in their quest to conquer the market. From the study, majority of the respondents also agreed that very often, they were the first business to introduce new products/services, administrative techniques, operating technology (mean = 2.49 and standard deviation = 1.099). The SMEs also exhibited a combative way of handling and relating to their competitors since majority of them agreed that they typically adopted a very competitive behaviour to outdo competitor posture (mean = 2.42 and standard deviation = 1.135).

Table 3. Descriptive Statistics for Pro-activeness with Normality Test

	Mean	Std. Deviation	Skewness	Kurtosis
Typically responds to actions which competitors initiates	1.93	1.076	1.345	1.464
Typically initiates actions which competitors then response to	2.37	1.066	0.875	0.058
Is very seldom the first business to introduce new products/services, administrative techniques, operating technology, etc	2.99	1.134	0.181	-0.813
Is very often the first business to introduce new products/services, operating technology etc	2.49	1.099	0.618	-0.123
Typically seeks to avoid competitive clashes, preferring a live and let live posture	2.64	1.392	0.406	-1.117
Typically adopts a very competitive, undo the competitive posture	2.42	1.135	0.342	-1.209
Pro-activeness	2.47	0.604	0.424	-0.385

Source: Survey Data, 2013

4.3 Risk-taking and SMEs Performance

As indicated in Table 4, majority of the respondents agreed that they had a strong tendency for lower risk projects (mean = 2.42 and standard deviation = 0.909, with skewness = 0.103). This can be best explained by majority of the respondents who agreed that owing to the nature of the environment, it was best to explore it gradually via timid, incremental behaviour, mean = 2.93 and standard deviation = 1.287, with skewness = 0.176), despite the fact that majority of them agreed that owing to the nature of the environment, bold, wide-ranging acts are necessary to achieve the firm's objectives mean = 2.28 and standard deviation = 1.202, with skewness = 1.014). Although this is the case with majority of the small and micro-enterprises, many of them were undecided on whether or not to typically adopt a cautious, 'wait and see' posture in order to minimize the probability of making costly decisions (mean = 2.67 and standard deviation = 1.044, with skewness = -0.235) which implies that majority of the small and micro-enterprises do not have a clear-cut strategy for dealing with risks which puts their businesses at risk of low performance. Despite the inefficiencies in relation to risk-taking, a significant number of the respondents (mean = 2.32 and standard deviation = 1.156, with skewness = 0.734) agreed that they typically adopted a bold aggressive posture in order to maximize the probability of exploiting potential opportunities. These results indicate that many of the small and micro-enterprises do not have clear strategies for dealing with risks and how to act when taking risks, although they recognize the fact that risk-taking is an important aspect in the performance of the small and micro-enterprises.

Table 4. Descriptive Statistics for risk taking with Normality Test

	Mean	Std. Deviation	Skewness	Kurtosis
A strong tendency for lower risk projects (with normal and certain rates of return	2.42	0.909	0.103	-0.639
Owing to the nature of the environment, it is best to explore it gradually via timid, incremental behaviour	2.93	1.287	0.176	-0.999
Owing to the nature of the environment, bold, wide-ranging acts are necessary to achieve the firms objectives	2.28	1.202	1.014	0.268
Owing to the nature of the environment, bold, wide-ranging acts are necessary to achieve the firms objectives	1.93	0.808	0.927	0.83
Typically adopts a cautious, 'wait and see" posture in order to minimize the probability of making costly decisions.	2.67	1.044	-0.235	-0.968
Typically adopts a bold aggressive posture in order to maximize the probability of exploiting potential opportunities	2.32	1.156	0.734	-0.163
Risk-taking	2.4997	0.68113	1.326	2.578

Source: Survey Data, 2013

4.4 Performance of Small and Micro-enterprises

As shown in Table 5 revealed small and micro-enterprises agreed there has been increased sales turnover (mean = 1.97 and standard deviation = 0.901). Small and micro-enterprises had achieved increase in their profit margins (mean = 1.87 and standard deviation = 0.689). However, the table shows that the firms had not achieved increased number of employees despite having increased sales and profit margins (mean = 2.66 and standard deviation = 1.02). Further, results show that the firms had achieved improved overall performance (mean = 1.89 and standard deviation = 0.781).

Table 5. Descriptive Statistics for performance of small and micro-enterprises with Normality Test

	Mean	Std. Deviation	Skewness	Std. Error	Kurtosis	Std. Error
Increased sales turn over	1.97	0.901	0.901	0.147	0.242	0.294
Increase profit margins	1.87	0.689	0.178	0.147	-0.89	0.294
Increased in the number of employees	2.66	1.02	0.023	0.147	-0.553	0.294
Improved image and reputation	1.81	0.69	0.263	0.147	-0.894	0.294
Improved overall performance	1.89	0.781	1.308	0.147	2.433	0.294
Performance	2.0452	0.66964	0.963	0.147	1.963	0.294

Source: Survey Data, 2013

4.5 Correlation Results

As shown in Table 6, there is a clear indication of positive and significant association between the various independent factors and performance of small and micro-enterprises at 0.01 level of significance. The table shows that innovativeness and performance of SMEs have 69.9% association, 59.8% with pro-activeness and 33.3% with risk-taking.

Table 6. Correlation results

	Performance	Innovativeness	Pro-activeness	Risk Taking	Learning Orientation
Performance	1				
Innovativeness	0.699**	1			
Pro-activeness	0.598**	0.676**	1		
Risk-Taking	0.333**	0.607**	0.457**	1	

** Correlation is significant at 0.01 levels (2-tailed)

Source: Survey Data, 2013

4.6 Hypothesis Testing

The study used multiple regression model to test the study hypotheses Ho₁, Ho₂ and Ho₃. The results in Table 7 show that innovativeness (beta = 0.632) significantly ($p = 0.000$) performance of SMEs and hence hypothesis Ho₁ (that there is no significant effect of innovativeness on performance of SMEs) is rejected.

Further the results show that pro-activeness (beta =0.246) has significant ($p = 0.05$) effects on performance of SMEs and hence hypothesis Ho₂ (there is no significant effect of pro-activeness on performance of small and micro-enterprises) was also rejected..

Additionally, the study revealed that risk-taking had significant inverse effect on SMEs performance (beta = -0.194 with p value 0.002) . Consequently, the hypothesis Ho₃ (that there is no significant effect of risk taking on performance of small and micro-enterprises) was rejected. These results show that the more risks an entrepreneur takes the less the performance of small and micro-enterprise.

Table 7. Model Summary

	Unstandardized Coefficients		Standardized Coefficients		Collinearity Statistics		
	B	Std. Error	Beta	t	Sig.	Tolerance	VIF
(Constant)	0.253	0.13		1.942	0.053		
Innovativeness	0.608	0.061	0.632	9.98	0	0.431	2.321
Pro-activeness	0.272	0.063	0.246	4.341	0	0.54	1.852
Risk taking	-0.16	0.052	-0.163	-3.1	0.002	0.627	1.593
R Square	0.535						
Adjusted R Square	0.53						
F	103.105						
Sig.	.000						
Durbin Watson	1.816						

Source: Survey Data, 2013

5. Conclusions and Implications

The purpose of the study was to investigate the effect of entrepreneurial orientation on the performance of small and micro-enterprises. To achieve this purpose, the study investigated the impact of innovativeness, pro-activeness and risk-taking on the performance of small and micro enterprises by collecting and analyzing the data from the owners of small and micro-enterprises.

The managerial implications are three-fold: First, for entrepreneurs to be innovative and improve performance enormously, they must be committed to learning. Second, entrepreneurs should shun away from taking risks

before learning the environment and establishing the likely drawbacks of such risks. Entrepreneurs should learn which risks improve performance of their firms. Moreover, championing an entrepreneurial learning of risk that favours change may help the firm to be proactive in streamlining business processes, promoting autonomous decision-making, and tapping into individuals' creative power – these will engender a higher-order generative learning that requires the desertion of old traditions. Third, firms must endeavour to pro-actively generate learning in line with their chosen firm strategy, allowing for exploration and experimentation as well as fully developing existing ideas so as to outdo their competitors.

6. Implications for Further Research

This study has revealed an inverse relationship between risk-taking and SMEs performance. This finding is rather surprising because risk taking is normally assumed to lead to improved performance. Future research should therefore refocus on risk taking and performance in SMEs from varied sectors and carry out a comparison to determine if these findings are generalizable to all SMEs irrespective of their sectoral context. Furthermore, an in depth study on the nature and prevalence of risk taking in SMEs in relation to performance is much needed to adequately inform policy and practise

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