

**4Ps INNOVATIONS IN SMALL MEDIUM ENTERPRISE AND THE
IMPACT TO THE BUSINESS PERFORMANCE**

By

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ABSTRAK

Para pengkaji telah mengenalpasti inovasi sebagai kunci kepada aktiviti sesebuah organisasi, yang telah menyumbang secara langsung kepada keberterusan operasi jangka panjang sesebuah organisasi. Dengan menggunakan-pakai sampel PKS (Perniagaan Kecil Sederhana) merangkumi Daerah Alor Setar dan Kubang Pasu di Kedah, kajian ini telah mencadangkan ujian ke atas model yang menunjukkan perhubungan di antara inovasi 4P (product, price, place dan promotion) dan prestasi organisasi. Keputusan kajian secara amnya menyokong kajian-kajian sebelumnya oleh Biggs (1996), Cohen (1988), Kelleberg (1986), Palmer (1993), Perreault dan Russ (1976), yang mencadangkan inovasi mempunyai perhubungan yang positif dengan prestasi kewangan dan bukan kewangan sesebuah organisasi.

ABSTRACT

Researchers have identified innovation as a key organizational activity, contributing directly to the long-term viability of operations. Utilizing a sample of SMEs' (Small Medium Enterprise) from Alor Setar and Kubang Pasu District in Kedah, this study proposes and tests a model that assesses relationships between 4Ps (product, price, place and promotion) innovation and organization performance. Result generally support past work by Biggs (1996), Cohen (1988), Kelleberg (1986), Palmer (1993), Perreault and Russ (1976), who have proposed that innovation is positively related to financial and non-financial performance of the organization.

Chapter 1

INTRODUCTION

1.1 Introduction

The Small Medium Enterprise (SME) is built on challenges to find the necessary resources, to attract and to retain talent to find a defensible niche in the marketplace. The challenges involve rapid technological changes that significantly contributed in SMEs competitive environment that have become increasingly complex and less predictable in recent decades (Burgelman & Maidique, 1988). For instance, the development of automated or computer-controlled processes can help firms sustain cost advantages over competitors (Walker, Mullins & Larrechi, 2002). In Malaysian context, with a growing population and higher standards of living, it seems that there is a huge potential waiting to be tapped by local SMEs to be more technology driven, getting the highest yield from the smallest of acreage used, in order to be more efficient, productive and competitive.

At this stage, innovation is found as the single most critical source of competitive advantage, whereby it enables firms to respond creatively to competitive threats and opportunities, the essence of entrepreneurship (Drucker, 1986). Cost, quality, and time will be requisites for market entry, and innovation will be the key differentiator among competing businesses (Biggs, 1996). Thus, innovation may be means for market leadership, contributing directly to the long-term viability of operations.

In recent years, innovative processes have been rapidly investigated, but much of this work has not focused on 4Ps (product, price, promotion, and place) as their independent variables. The studies only focused on innovation as a whole or only on product innovations. For instance, a study done by Palmer (1993), focused on the relationship between innovation and financial performance. Despite widespread interest in innovation, practitioners have had little in the way of direct evidence to support the use

of competitors as moderating variables. Moreover, the relationship between innovation and business performance has not been established.

1.2 Research Problem

The adoption of innovations may yield benefits to the firm but it also may lead to inefficient investment decisions that will affect the firm's performance. Wasted resource allocations may not improve profitability (Abernathy & Wayne, 1982) and lack of attention given to the 4Ps strategy and competitor analysis might be the factors that will decrease firm's performance. Moreover, most of innovations studies relied on samples consisting of large business enterprises and little is known about innovation in small and medium firms, even though SMEs serve as incubators for many innovations. Thus, the direct transfer of previous findings to small and medium businesses may be misleading (Palmer, 1993). Empirical studies focusing specifically on innovation in small and medium enterprises are needed.

Malaysian firms, especially in Kedah whose economy has historically been agriculture based, are still dependent on others for their sustenance. A huge sum of money flows out to buy food products. Malaysia's food import bills have surpassed RM11 billion annually for food expenses (Malaysian Enterprise, November 2000). To avoid this, product innovations by using technology and modern processes are needed to strengthen our food production sector, not just to cater the local demand, but also claim a bigger slice of the world's market. Besides that, SMEs' also needs innovations with aggressive promotions in introducing their product. For instance, Malaysia has many premium products made from local materials, the product design and manufacturing quality can be proud of with competitive pricing. But these products remain unpopular

due to unaggressive promotions with innovations. As showed in table 1, Food and beverage industry were at the fourth rank in Kedah (www.smidec.gov.my). This might include both industrial and consumer product:

Table 1
SMEs By Industrial – Northern Region

Industry	Perlis	Kedah	Pulau Pinang	Perak
1. Food Beverage & Tobacco	14%	14%	18%	19%
2. Fabricated metal products, machinery & equipment	23%	23%	23%	13%
3. Wood & wood products	16%	14%	10%	13%
4. Textile, Wearing Apparel & Leather	13%	10%	12%	13%
5. Chemical & of Chemical, Petroleum, Coal, Rubber & Plastic Product	1%	20%	14%	18%
6. Paper & paper product, printing & publishing	3%	16%	10%	7%
7. Non metallic, mineral products except products of petroleum & coal	21%	8%	3%	9%
8. Basic metal industry	5%	3%	5%	5%
9. Others	3%	2%	3%	1%

(Source: www.smidec.gov.my)

The coming AFTA 2003, tariffs will be abolished and foreign products will enter Asean markets that will lead competition among products. Therefore, this study has decided to look into the 4Ps innovations not only to the product and promotions but also price and distribution as influencing factors to the business performance, and to see whether competitors plays a role between innovations and performance. It will make an interesting study for as far as it is known since no studies have been done previously on 4Ps innovations of Malaysian SMEs.

1.3 Research Objective

The objective of the research is to establish and tests a framework of 4Ps innovation in organization. Utilizing the sample of Small and Medium Enterprise (SME) that produces end product to the customer, the following questions will be addressed: 1) What is the relationship between business performance and 4Ps innovation; 2) Does 4Ps innovation has a significant impact to the business performance?

Innovation has been studied at many different levels of analysis ranging from the effects of public policy decisions on the wide scale diffusion of innovations to characteristics of individual that contribute to organizational innovation (Palmer, 1993). Thus, factors like 4Ps innovations are likely to systematically influence firms business performance whether it has to compete with other firms or not. A model can be drawn using the following conceptual paradigm:

- The business performance will be the dependent variable; the moderator variable will be the competitor, the independent variables being the SMEs' innovation in product, price, promotions, and place/distribution.

4Ps innovation has been chosen as the independent variable since it will give the overall picture in the process of the product development from the beginning until the end. Moreover, it is assumed that firms that adopted innovations will be succeeded in their performance. Thus, business performance has been chosen as the dependent variable to see whether innovation will give a positive impact to the firm's performance.

1.4 Significance of the Study

This study of 4Ps innovations, which may contribute to the success and failure of the business, can be significant to the Small and Medium Enterprise in Kedah, since the government's goal is to encourage new ideas using new strategy, technology and modern processes to enhance the business performance among SMEs in Malaysia. This study is designed to provide SMEs owners with a tool to identify innovations that will lead to their success. Furthermore, SMEs has a comparative advantage over large-scale enterprises in terms of their flexibility, innovativeness, adaptability, and ability to survive (Asheier & Seibel, 1987).

Innovation has the potential for the greatest returns. One of the great paradoxes surrounding innovation is that, initial success can be the greatest encouragement to further innovation. As SMEs moves into this next decade, where a changing and competitive environment will be the constant and not the exception, increasing attention will have to be paid to the forward looking measurements of an organization progress. Therefore, study of the 4Ps innovation in the competitive environment is needed in order to determine the business performance of SMEs.

1.5 Defining Key Terms

It is appropriate at this juncture to define the various terms that will appear repeatedly in the text, for purposes of clarification and common understanding.

SME: The SME adopts the definition of the Small and Medium Scale Enterprise Division of the Ministry of International Trade and Industry of Malaysia, which currently classifies small-scale enterprise as those with shareholders funds not exceeding RM500,

000 with full time employees not exceeding 30. Medium scale enterprise are manufacturing entities having shareholders fund between RM500, 000 and less than RM2.5 million, with full time employees of not more than 150.

Innovation: Innovations are organizational adoptions of ideas that are new to the firm or an industry (e.g, Rogers & Shoemaker, 1971; Sayles, 1974). Innovation results from processes involving assents of relationship between availability of technologies, entrepreneurial capabilities of firm, and market characteristics (Burgelman & Maidique, 1988). Typically, these processes are initiated by firms in response to the identification of programs of action that no longer satisfy performance criteria (March & Simon, 1958). This situation gives rise to a search of alternative that meet performance objectives followed by an evaluation of alternatives in light of product or process needs (Utterback, 1973)

4Ps: As defined by Evans and Berman (1994), 4Ps relates to the marketing decision to product, place/distribution, promotion, and price factors as. "Products" in this study are focusing on consumer products that are goods destined for the final consumer for personal, family, or household use. Consumer products were first classified by Copeland (1986). His three category system of convenience, shopping, and specialty products is still widely employed today. "Place" or distribution is regarding to the movement of goods from producer to consumer as well as the related transfer of ownership of them in a channel of distribution, which consist a channel members. "Promotion" is focuses on a total promotion effort-informing, persuading, and reminding. Finally, "prices", where it places a value on a goods. Additionally, pricing must interrelated with product, distribution and promotion decision.

Competition: As defined by Cohen (1991), competition relates to organizations competencies with the firm for business or the acceptance of ideas. In addition, competition includes all the actual and potential rival offerings and substitutes that a buyer might consider (Kotler, 2000).

Business performance: It is defined as how consistently and well a product functions and the service is performed in presence of the customer (Berry & Parasurman, 1991). In addition, as defined by Churchill, Ford and Walker (1997), business performance is the business contributions to the goals of the organization. It has a normative element reflecting whether the business operation is “good” or “bad” in light of the organization goals and objectives.

1.6 Organization of the Thesis

The following chapter begins with a discussion of the 4Ps innovation and how it has been operationalized in the past studies. In Chapter Three, the methodology used in the study is described. Sample selection techniques, research hypothesis, operationalization of major constructs, and the basic research design are presented. Identification of moderating variable and a discussion of data analysis procedures will then follow.

In Chapter Four, results of the study are presented. This is followed by Chapter Five, in which conclusions based on these findings are discussed. Implications for practitioners and researches are also discussed along with recommendation for future research.

Chapter 2

LITERATURE REVIEW

2.1 Innovation Defined

There is a popular perception that small firms are the engines of innovation. Daft (1978) categorized innovations into those that directly influence the basic work of organizations (technical innovations) and those that indirectly influence basic organizational work (administrative innovations). Thom (1990) proposed a typology consisting of product and process innovations. Product innovations are ideas leading to adaptations to goods or services such as the introduction of new products, marketing techniques, or mode of customer service. Cosh, Hughes and Wood (1996) found that the most innovative manufacturing sectors in United Kingdom (UK) are the engineering sectors, including electrical engineering, chemicals, mechanical engineering and metals. Process innovations involve adaptations to processes within organization made in an effort to increase productivity or enhance scale of economies. As mentioned by Biggs (1996), innovation may be one of the most difficult key performances to measure, but it has the potential for the greatest returns. He also mentioned that customer surveys are of limited use in measuring innovation since they measure what customer expects today; they cannot measure future expectations.

Innovations vary along multiple dimensions such as their relative cost, the impact that they potentially have on functional elements of organizations, and their complexity (Downs & Mohr, 1976). Birkett (1996) found that SMEs' do not need cost management expertise, but they are likely to have cost management needs if one or more of the following forms of complexity applies:

- There is ambiguity in their products markets, such that pricing, volume, or pricing/volume mixes are problematic
- They have a product range or differentiated products, so that there is a need to make product mix decision.
- There is competition in product or resource markets so that pricing, volume and product mix problems are worsened.
- There is a need to appraise, at least occasionally, new investment requirement or opportunities.
- There is a decision or a need to manage using modern management technologies, such as just-in-time production, quality management, and continuous improvement philosophies.
- There is a need to established performance indicators that have a bearing on cost reduction or management, or on drivers that provide value for customers or owners.

However, Schumpeter (1934), in Chell (2001), could take a number of different forms of innovations:

- The creation of a new product or alteration in some of its attributes,
- The development of a new method of production,
- The opening of a new market,
- The capture of a new source of supply, and
- A new organization of industry.

Kanter (1983) largely follows the Schumpeterian line of reasoning. She points out that, although most people would think of innovation as being scientific in character,

there are many other kinds of changes that count as innovations. For example new tax laws, the creation of enterprise zones, quality circles and problem solving task forces.

2.1.1 Product Innovation

a) New Product Development

According to the marketing concept, the focus of marketing should be on the customer and customer need satisfaction. Therefore, the customer is a major source for new product ideas that revealed through market research. One survey indicated that of 267 mentions of major external sources for new product ideas, customers represented 28% (Sachs & Benson, 1981). For business companies, the percentage was even greater. In another study, 77% of the sample of 111 scientific instrument innovations and 67% of a sample of 49 process machinery innovations came from the customer (Hipple, 1978).

The competition is also an excellent source of new product development ideas for many companies. Many companies study every new product introduced by the competition for its potential. If it does appear to have potential, they decide whether to introduce a similar product that does the same thing. If they do, they must do it without violating patent or other protected rights of the company that introduced the product (Cohen, 1988). A study of 107 firms found that almost 30% used an analysis of competitive products as a source of new product ideas (Lawton & Parasuraman, 1980).

Marketing experts have sought ways of increasing the success rate for developing new products for many years. A study by Cooper (1975), in Palmer (1993), looked at 114 business products in 101 firms found four general reasons for failure as shown below:

- Sales fell below expectations,
- Profit margins fell below expectations,
- Development costs exceeded expectations, and
- Investment exceeded expectations.

Another reasons for new product failure is consumer resistance to new product failure. Booz, Allen and Hamilton (1982) the management-consulting firm, completed a major study of 13,000 new products from more than 700 U.S manufacturers, and found that factors such as marketability, durability, productive ability, and growth potential contributed to success of new product development. Additionally, factors that had little impact on whether the product was successful included: 1) being first into the market, 2) the mere existence of a strong competitor, 3) production capability by itself, and 4) product technical complexity

b) New Product Branding

Higher profit margins, image and identification are the reasons why firms brand their product (Cohen, 1988). In fact, the brand name itself can help to position a product. Studies have shown that when certain products are branded in such a way that they seem to imitate other already established and successful products, the consumer assumes that this newer product has similar or the same attributes (Miaolis & D'Anarto, 1978). When a company introduces a new product, there are four possibilities regarding branding (Tauber, 1981):

1. The company can employ a new brand name with a new product or a new service in a category completely new to the company.

2. The company can introduce a new brand, but in a category the firm is already marketing
3. The company uses the brand name in the firm's present product category
4. The company applied a brand name that is familiar to the consumer for products in a category the firm is not presently marketing.

The benefits of brand extension include the fact that the extension capitalizes on one of the company's most valuable assets. Thus, with the goodwill brand name, awareness and all other aspects and impressions that have been previously communicated by the brand, the company moves in with its new product. Also, further promotion of the brand name with the new product can lead to increase sales for the parent brand (Cohen, 1988).

c) New Product Packaging

Packaging can be a major element of new product planning. Some of the products successfully modified and presented, as new as a result of packaging innovations are deodorants, hair spray, containers for milk, toothpaste, medicine bottles etc (Evans & Berman, 1994). Packaging can also be a major key to product success (Cohen, 1988). Confirming the importance of packaging as a communication vehicle, a study conducted by Deighton (1989) found that the reason behind repackaging existing products among marketing respondents were as follows:

- Modernizing designs/graphics, 22%
- Product positioning, 22%
- Improving shelf impact, 19%
- Cost savings, 11%

Package redesign frequently occurs when a firm's current packaging receives a poor response from channel members and customers or becomes too expensive, the firm seeks a new market segment, reformulates a product, or changes or updates product positioning; or new technology becomes available (Evans & Berman, 1994). One study performed by McDaniel and Baker (1977) revealed that a significant proportion of consumers perceive that potato chips in polyvinyl packages are crisper and tastier than are exactly the same potato chips in wax packages. However, product packaging is not free. It costs money and uses up other critical company resources to design, manufacture, and produce packages for products (Cohen, 1988).

2.1.2 Place/Distribution Innovation

a) Quality Suppliers

Availability, timeliness, and the quality of physical distribution are benefits that customers value as much as product quality and a competitive price (Mentzer, Gomes & Krapfel, 1989). One study showed that distribution service was second only to product quality in importance to the channel member. It was more important than price (Perreault & Russ, 1976) The main problem for SMEs is achieving widespread distribution. The limited resources of a small firm may prohibit the use of a direct channel when it is selling to a large number of customers that are widely distributed. As a result, of the major channels for selling consumer goods direct from manufacturer to consumer is the least used.

The use of indirect channels includes employing retailers, wholesalers and business supply houses; including manufacturers representatives and other agents are more popular to distribute customer products. Manufacturers representatives and agents

who represent the manufacturer; but are independent and do not take title to the goods sold, are very beneficial when the producer is small and has a narrow product line. One major advantage for all indirect channels is increased marketing opportunities and wider distribution potentials under varying conditions (Cohen, 1988).

b) Speedy Deliveries

For speedy deliveries, firms always use more than one channel simultaneously because it tends to provide additional outlets for sales and more chances for selling. However, multiple channels may not be desirable for SMEs since the economics of the situation has to be considered, including costs, profits, and available resources. Because resources are always limited, and this is especially true with a smaller firm whereby resources may only be available for a single channel (Cohen, 1988).

The channels tend to be shorter in the following situations: 1) manufacturer is strong financially, 2) the product line is large and complete, 3) the average order size is high, 4) the customers tend to be concentrated geographically, 5) there is little seasonality, 6) the distance from producer to market is short, or 7) the product is perishable. Retailers are one of the shortest channels, and the quickest way of knowing what is going on in the marketplace (Michman, 1983).

c) Warehouse Facilities

Ackerman and Lalonde (1980) from Ohio State University recommended that improvement should be done to one specialty area of physical distribution that is warehousing. Their recommendations might usefully be considered in all physical distribution areas to improve efficiency. The areas noted by these experts for emphasis

were increasing the size of units shipped, seeking round trip opportunities where the transportation conveyance didn't travel empty, increasing the use of cubes and other efficient packaging methods for shipment, reducing the distance traveled, reducing the items handled, improving forecasting accuracy, freeing labor bottleneck, smoothing the flow variation, and installing specific improvements targets. A study by Lalonde (1980), in Tyndall (1989) for the industry on logistics improvements received the following results to improve efficiency of physical distribution:

- A 25% reduction in time from order placement to merchandise receipt at the distribution center,
- A doubling of merchandise turnover at the distribution center,
- More than 60% of vendor transactions accomplished through electronic means,
- A dramatic increase in the use of bar code technology, and
- 98% of sales transactions recorded by point-of- sale data.

2.1.3 Promotion Innovation

The objectives of promotion can be divided into two general categories, stimulating demand and enhancing company image (Evans & Berman, 1994). The following are five broad alternatives for reaching the advertising objectives (Boyd, Ray & Strong, 1972):

- 1) Stimulate primary demand for the product or service,
- 2) Introduce previously unknown or new advantages or attributes,
- 3) Alter the assessed importance of an existing product or services attributes,
- 4) Alter the perception of a product or service, and

5) Change the perception of competing products.

A firm also develops advertising themes, the overall appeal for its campaign. The basic advertising themes are product, consumer, and/or institutional appeals. A good or service appeal centers on the item and its attributes, a consumer appeal describes the good or service in terms of consumer benefits rather than product characteristics and, an institutional appeal deals with corporate image (Weilbacher, 1984). When selecting media, several factors should be considered and one of them is media innovation which include regional editions and special one-sponsor issues (advertorials) to revive magazines, newspapers improving their computer skills in placing ads; advertising in cable television; televised commercials in supermarkets, movie theaters, and airplanes, specialized yellow pages, more radio stations handling ads in stereo, better quality in outdoor signs; full length advertising programs (infomercials) on television; and direct mail ads featuring computer diskettes (Schlossberg, 1993). One survey of American public found that people are generally rather skeptical with regard to the content of the following promotion messages (Donaton, 1993):

- 60% believe ads with money back guarantee,
- 57% believe ads with products approved by medical or health groups,
- 38% believe ads where comparisons to competitors are made,
- 29% believe ads using hidden-camera interviews, and
- 25% believe ads featuring celebrity endorsements.

2.1.4 Price Innovation

One important survey done some time ago indicated that only 50% of marketing practitioners rated pricing as an important marketing decision (Udell, 1964). But, a recent study conducted by Fleming Associates of Columbus, India shows pricing was the critical pressure point for today's marketing arena (Marketing News, Nov, 1983). As indicated by Cohen (1988), Pricing decision is required when the change comes due to the introduction of a new product, or an environmental change such as an action by a competitor or the government, or even a technological breakthrough occurs, or the firm takes a change in strategy, or there is a change in the product line.

Cohen (1988) also mentioned that, there are three basic alternative pricing tactics which can be followed in introducing a new product into the marketplace: (1) penetration pricing, (2) a meet-the-competition pricing, and (3) price skimming. With penetration pricing, the marketing manager seeks to enter a market with a low price to capture as large a share as possible. Price skimming implies entering the market with a relatively high price for a new product. Meet-the-competition pricing means that the marketer will enter the market with the new product priced the same or approximately the same as those currently offered by competitions. One researcher looked at 356 business items sold to the government and priced under both sole-source conditions-where there was a single supplier without competition and under competitive conditions with two or more suppliers. The mere facts of the presence of competition resulted in a price reduction of between 10.8% and 17.5% (Burt & Boyett, 1979).

The following elements of a successful pricing system, which can be adopted in the marketplace, has been indicated by (Ross, 1984): 1) have as much information available

as possible about market and customer characteristics, competitor capabilities, likely competitor actions and internal capabilities, competitor cost, and pricing, 2) collect and analyze price data for each product introduced by competitors early in the development process and throughout the product's life, 3) take advantage of the latest data to support effective and optimal pricing, 4) maintain flexible and responsible organizations and systems for collecting and data, and 5) ensure the competent people are assigned the task of collecting, analyzing, and dispensing price information.

2.2 Competition

As indicated by Lusvarghi (1996), "No analysis seems to be made of current and potential competition, its marketing strategy, or its cost. What the small business owner knows is the price offered by competitors, and sometimes not even that – more often, he or she knows the name of customers lost to competitors". So, a differentiation strategy is required to create a product to be unique in the market. This strategy is implemented through unique product design, modes of customer service, dealer networks, and marketing (Porter, 1980: 35).

Biggs (1996) found that, innovation would be the key differentiator among competing businesses. As found by Cosh, Hughes and Wood (1996), firm size and industry are important determinants of a firms innovative activity, and innovation should be seen as a part of a dynamic competitive process within sectors. They also found that the spur to innovate arises directly from a firm's assent of its competitive environment. In other words, one may not observe poor performance to be prompt to innovation, because firms always threatened by their competitors' development of a new product. At the heart of the conventional wisdom regarding technological change has been the belief that a

large enterprise is able to exploit at least some market power are the engine of technological change (Zoltan 1999, in Walker, Mullins, & Larrechi 2002). This view dates back at least to Schumpeter (1934), in Chell (2001), who argued, "The monopolistic firm will generate a larger supply of innovation because there are advantages which though not strictly unattainable on the competitive level of enterprise, are as a matter of fact secured only at the monopoly level".

Additionally, as Prahalad and Lean (1994) have indicated, "quality won't be a competitive differentiator in the year 2000, it will be the price of entry... instead, and the capacity to create fundamentally new products will be the key competitive advantage". According to Dess and Davis (1984), in Cohen (1988), business units adopting differentiation strategies emphasized brand identification, advertising, new product development, and innovations in marketing. Furthermore, findings by Figenbaum and Karnani (1991) illustrated that the ability of smaller firms to gain or maintain a differential advantage was associated with innovations in output variability since it enabling smaller firms to compete against larger, low cost competitors. Abernathy and Clark (1988) discuss the nature of competitive advantage arising from innovative activity. On the technology/production side they suggest is the resources, skills and knowledge that affect design and production, which ultimately create competitive advantage.

Overall, the above studies indicate that: 1) firms exhibit innovation adoption that are consistent with the content of competitive strategies, 2) firms that compete on the basis of efficiency emphasize innovation in an effort to gain or maintain differential advantage, and 3) competitors seeking to compete through differentiation strategies emphasize innovations enhancing product offerings. Therefore, competition has been

chosen as the moderating variable that will moderate the relationship between 4Ps innovation and business performance.

2.3 Business Performance

Being successful today means that the decision made yesterday has added value to both the SME and its customers. Knowing how to make the decision today that will continue to add value tomorrow for both the SMEs and its customers is the basic challenge. Being knowledgeable about customers, their needs and choice, and about competitors, their strategies and strength, is as important as being efficient and cost-effective in building and marketing of products and services of the SMEs.

In a pioneering analysis, Downie (1958) proposed a model of the competitive process based upon the interaction between firm performance and innovation. He suggested that a relatively slow growth or decline follows a decline in relative efficiency, which in turn reflects a relative failure to innovate. However, he found that slow growing firms did not necessarily have a lower chance of success in innovation in the future. While acknowledging that slow growing firms are likely to have less financial resource to devote to innovative activity than more faster growing firms, Downie (1958) also found that fast growing firms would be less motivated to innovate because of the pain of rethinking established habits and process and the risk that innovation investment will be wasted. While a slow growing firms may suffer from less intimate knowledge but free from distorting influence of the pride of creation. Another reason why slow growing firms may be next to innovate is that technological advance may be faster than the replacement cycle, and they will be far more highly motivated to re-examine their existing methods and experiment with new ones.

The Nickell and Nicolitsas (1995) results are consistent with the Downie hypothesis of an innovation mechanism since they observed a significant negative relationship between past change in profits per employee and their subsequent introduction of new technology. There is also some evidence which implies the opposite, i.e., that current innovation performance is a positive function of past overall firm performance, which implies that there is persistence in both innovativeness and overall performance. However, Geroski (1995) found that there is no evidence of a significant relationship between innovation and either growth or profitability.

Rates of innovation adoption may have differential impacts on the financial performance of firms (e.g., Abernathy & Wayne, 1982). Authors have indicated that, while innovation may enable firms to capitalize fully on market opportunities, enhancing financial performance, it may also lead to inefficient investment decisions (Hayes & Abernathy, 1982; March & Sprowell, 1990). Only a limited number of empirical analyses have directly examined relationships between innovation and financial performance. However, findings from these studies have consistently reported positive associations.

For example, in 411 small computer firms, health care clinics, and eating and drinking establishments, Kalleberg (1986) found that innovation are positively related to market share gains and profits margins. Innovations by firms enabled them to assume proactive positions in product and service markets, allowing them to gain first mover advantages that enhanced market share and profitability. Miller and Toulouse (1986) reported that the ability of SMEs to differentiate product offerings through innovation was positively related to sales growth, ROI, and growth in net income. As mentioned by Covin and Slevin (1989) in their studies on 141 small manufacturers, product innovation

increased the ability of firms to respond to changing consumer demand in a timely manner and to fully capitalize on market opportunities. In addition, Shumpeter (1934), and Kanter (1983), in Chell (2001) mentioned that, innovation leads to better performance, it gives a business a competitive edge that enabling it to outperform its competitors and the innovation is better than its predecessors. It also suggests that technical or technological innovations do lead to better economic performance of companies.

Besides using financial information as a guide for business performance, Biggs (1996) suggested SMEs' to develop performance indicators that are output based rather than input based. Since historical financial information will not provide sufficient information on output, he mentioned that, many of the performance indicators would be non-financial. Essentially, the non-financial measurements can be grouped into two categories: quality and time (as shown in figure 1).

FINANCIAL

- Revenue growth
- Profitability- by customer, by market, by product
- Gross margin return on investment
- Return on sales
- Return on gross assets employed
- Return on equity
- Inventory turnover
- Accounts receivable turnover
- Cash flows

NON-FINANCIAL

Quality

- Market share
- Number of new customers
- Number of repeat customers
- Number of satisfied customers
- Number of dissatisfied customers
- Safety performance

Time

- Number of on-time deliveries
- Time taken to respond to customer inquiries
- New product development cycle time
- Manufacturing cycle time

Figure 1: Examples Of Key Performance Indicators

(Source: Biggs, 1996)

Time has been recognized as a source of competitive advantage. Jones (1993) writes that high-speed management competing on the basis of time will be essential for corporate survival in the coming decade. In the coming decade, proportionately less time will be spent on making decisions and more time will be spent on implementation. As Pfeffer (1992) puts it, "rather than spending inordinate amount of time and effort in the

decision making process, it would be seem at least as useful to spend time implementing decision and dealing with their ramifications”.

2.4 Summary

This research establishes and tests a framework for the study of 4Ps innovation that incorporates the influence to the business performance. The model is comprised of the following four-predictor variables: 1) Product innovation, 2) Place innovation, 3) Price innovation, and 4) Promotion innovation.

While past studies have assessed influences on product and process innovation on the business performance, none have specifically studied on another 3P's innovation (Place, price and promotion). They focused on innovation in general or only on product innovation. Moreover, only a limited number of studies have been directly examined relationships between innovation and performance. This study seeks to provide more comprehensive examination of innovation by simultaneously examining the influences of 4Ps innovation on firm's business performance, as studied by Palmer (1993), Reuber (1996) etc. The following chapter outline the methodology employed in the study. Sampling procedures, research hypothesis, operationalizations of dependent and independent variables, moderating variables, and statistical procedures are described in detail.