

**THE IMPACT OF THE ENTREPRENEURIAL ORIENTATION ON  
PERFORMANCE IN AUSTRALIAN FRANCHISE FIRMS**

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**Abstract**

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## **Abstract**

The Australian franchise industry represents a significant employer group and is responsible for a large portion of the Australian retail and services expenditure. This paper examines the impact Lumpkin and Dess's (1996) Entrepreneurial Orientation (EO) dimensions: autonomy; innovation; risk taking; proactiveness; and competitive aggression, had on franchise firms performance.

The EO dimensions were found to be dominant at the inception of each franchise firm reviewed. Over time all components diminished in importance whilst performance of the franchise continued to improve. It was found that autonomy became restricted by boards of management, innovation reduced through the introduction of proven systems, and that risk taking became "calculated" risk taking. It was also found that over time proactiveness no longer meant having to establish new markets or trends, and there was a diminished importance in the firm's propensity to competitive aggression.

A paradox was present in the surveyed franchise businesses. The entrepreneurial owners strived to create independent and flexible organisations through the formation of franchise businesses, however by creating the buying, marketing and support systems necessary to run a franchise, the owners inadvertently developed bureaucratic constraints often seen in other corporate organisations.

# THE IMPACT OF THE ENTREPRENEURIAL ORIENTATION ON PERFORMANCE IN AUSTRALIAN FRANCHISE FIRMS

## INTRODUCTION

Covin and Slevin (1991) believed that companies achieve success through their entrepreneurial activities. This paper will examine if the successes in the franchise industry have been due to an entrepreneurial environment. Lumpkin and Dess (1996) provided the Entrepreneurial Orientation (EO) framework to establish a relationship between EO and a firm's performance. Research has been conducted to examine the effects of EO in many areas, however, there does not appear to have been any significant studies conducted showing the effects of EO in the franchise industry.

The franchise industry has seen prolific growth during the 1980 s and 1990 s and there is no evidence that this will slow in the 2000s. The Australian franchise industry has lead the world with it's Code of Conduct in 1997, ensuring that the industry is a recognised professional industry, contributing to substantial employment opportunities and in controlling a large proportion of the dollars spent within Australia. The industry represents the benefits of both the small business (franchisees), with its ability to utilise innovation and flexibility to broaden markets and gain competitive advantages, plus have the corporate base (franchisor) from which training, research and development, and marketing support can be accessed. Zahra and Covin (1995) suggest that firms with EO can take advantage of emerging markets and trends, but as Porter (1985) argues, the difficulties in small businesses can be in resource constraints that prevent a firm from "pursuing cost leadership" or "differentiation strategies". Franchising has been found to help reduce these constraints.

Recent statistics show that the franchise industry in Australia employs 651,900 employees and has a turnover in 1998/1999 of \$76.5billion (AUD), therefore representing a significant component of the Australian economy, Frazer and Mc Cosker (1998). It also had a compound growth rate of nearly 17% pa during the 1990 s, making it an important component of the Australian retail sector.

This research assessed whether the Lumpkin and Dess (1996) Entrepreneurial Orientation (EO), dimensions might be the catalyst for a successful firm in the Australian franchise industry. Three well - known Australian franchises were involved in the study.

Three segments of each organisation were considered – where the franchisor is the owner of the franchise business, is an entrepreneur, and as such acts in an entrepreneurial manner. The staff referred to is the staff that report to the franchisor in the franchise firm, and the franchisee who is the independent owner of the franchise store operating within the framework of the franchise organisation it represents.

The franchise industry, the franchisor and the franchisee, and the entrepreneur, referred to in the literature review, refer to the franchise industry generally, unless specifically stated as referring to Australia. A generic approach was used due to the lack of documented information available.

## LITERATURE REVIEW

This review will focus on Entrepreneurial Orientation. Lumpkin and Dess (1996) developed Entrepreneurial Dimensions – innovation, proactiveness, risk taking, competitive aggressiveness and autonomy – which represented the key entrepreneurial processes or the firm's Entrepreneurial Orientation (EO). This next section considers some of the literature related to these dimensions. Generally, it would be expected that if the franchise organisation was entrepreneurial, then the EO dimensions would be identifiable over time.

*Hypothesis 1. All dimensions of EO will be found to be present in the beginning and over-time most will still be present.*

Stevenson and Gumpert (1985) state that the “heart of entrepreneurship” is **Innovation** and Covin and Miles (1999) suggest that without it entrepreneurship does not exist. A key area of innovation is creativity, however, Amabile, Conti, Coon, Lazenby and Herron (1996) suggest that, whilst creativity may initiate innovation, it may not necessarily be the main motivation or driving force behind it. Peters (1990) notes that innovation requires creativity and obsession to see it through.

Quinn (1985) adds to the importance of innovation by suggesting that innovation brings out the learning strength of the organization, for it requires “personal and group obsession” to see the innovation through, and a context to absorb “learn from failure”. Brazeal and Kruger (1994) believe that the experiences gained through the innovative processes will further enhance the probability of future innovative outcomes.

Damanpour (1991), Poole and Van de Ven (1989) also suggested that innovation is more than someone with a new idea; they believe that it is the process of being aware, observing, accepting and implementing.

*Hypothesis 2. Innovation is considered the most powerful dimension.*

**Proactiveness** - Lumpkin and Dess (1996) suggested that a proactive firm is a leader because it has the ability to seize opportunities. They referred to proactiveness as providing the forward-looking perspective that can be usually associated with innovation or “new venturing activity”. Through proactiveness, plus innovativeness and risk-taking, a firm is more likely to be able to compete in a dynamic environment, Dess, Lumpkin and Covin (1997), Miller and Friesen (1984), and Morris and Paul (1987).

*Hypothesis 3. Proactiveness is difficult to initially achieve, but over-time the infrastructure enables new products and services to be introduced into the market with greater ease.*

Baird and Thomas (1985) referred to three types of **Risk-taking** when referring to risk strategy by suggesting that it was proceeding into the unknown, committing resources, and borrowing heavily. Low and Mac Millan (1988) found it unclear if there was actually a high propensity to risk taking in entrepreneurs. Cooper, Dunkelberg and Woo (1988) also observed that it was difficult to identify if they were different from the general population. Recent research by Falbe and Larwood (1995) has found that risk-taking was more likely to be observed with entrepreneurs than with non-entrepreneurs. Their proposition was supported by Cromie (1994 p.64).

The problem appears in identifying risk; some people perceive risk-taking as in financial investments or the risk of further career opportunities; to others, family relationships, and particularly marriage, are often seen as severe risks. Kimberley and Miles (1980) and Scott and Bruce (1987) found that risk taking propensity in entrepreneurs diminished over time as the entrepreneur assumed a role of manager or caretaker.

*Hypothesis 4. Risk taking will be present, but the entrepreneur will not identify with risk taking. They will identify with calculated risk and leveraging and identify that risk taking is part of the environment.*

**Competitive aggression** in EO shows the willingness to be unconventional. Lumpkin and Dess (1996) believe it to be the firm’s tendency to continually challenge the competitor and out-perform them, taking them head on at every opportunity.

Also important, as suggested by Stinchcombe (1965), is the ability for new organizations to be able to create a legitimacy and power with their suppliers, their customers, and their competitors by using competitive aggressiveness.

*Hypothesis 5. Competitive aggression will be a key dimension to the entrepreneur in ensuring a secure supply base and in growing market share.*

It is therefore necessary that a strong and decisive leader has the **Autonomy** to make decisive and risky decisions and is at the helm of the entrepreneurial firm, Mintzberg and Waters (1985). Schein (1994) also observed that highly autonomous leaders should be added to any list of entrepreneurial characteristics. He also argued that these autonomous entrepreneurs initiate ventures rather than enter businesses for economic reasons.

Lumpkin and Dess (1996) discussed the strength of the autonomous independent free spirit of the entrepreneur as necessary to further new ventures, and added that autonomy is implied by ownership or in large organizations through the position. Autonomy can also be gained through the tacit and explicit knowledge of the firm an individual possessed. Shane (1994) found that autonomous leaders could be identified by the manner in which they were able to bend the rules and bypass procedures.

*Hypothesis 6. Autonomy will be seen as the lifeblood of the entrepreneur, without it the entrepreneur cannot function. This dimension will interact strongly with the other dimensions and drive the dimensions of EO.*

Lumpkin and Dess (1996) suggested that the meaning of **Performance** in EO should be further researched, and Wiklund (1999) noted that it was unclear whether EO benefited organisations over time. Authors such as Covin and Slevin (1991), Zahra (1991) referred to the lack of systematic empirical evidence in causal relationships between EO and performance; however, Zahra and Covin (1995) supported the theory that performance was enhanced through EO.

Difficulties arose when establishing common and available data in analysing small business performance as the financial accounts were not publicly available. Many authors have concentrated on growth as a common variable measure in small firms, Chandler and Hanks (1993), Fombrun and Wally (1989), Tsai, Mac Millan and Low (1991).

Lumpkin and Dess (1996), in discussing the relationship between EO and performance, believed that it may be more complex than first thought, and Zahra (1995) added that the environment could influence performance. They have identified that performance can be influenced by both market growth and market conditions in a positive and negative effect.

Wiklund (1999) discussed the aspects of growth and financial performance and suggested that they should be viewed together in order to give a deeper understanding of the actual performance of the firm. Hoy, Mc Dougall and D' Souza (1992) believed that performance should be measured by growth for it was easily attainable and reflected the short and long term changes.

*Hypothesis 7. Through the presence of EO, performance of the organization will be enhanced over time.*

## **METHODOLOGY**

### **Research Design**

This research utilised the case study method within the Australian franchise industry. As Feagin, Orum, and Sjoberg (1991) suggested, this method of gathering data is applicable when “holistic” and “in-depth investigation” is required.

The overall structure for this research was based on the methodology of Yin (1984) and Levy (1988). Multiple case studies follow replication logic and in this research, the different demographics assisted in broadening the knowledge of the phenomenon.

## **Research process**

The decision to proceed with a case study methodology influenced the method of data collection. Survey data was collected through in-depth, face to face interviews. The following procedures were adopted to maximise the accuracy of the observable data:

- Five key attributes were identified for each of the five dimensions from the extensive literature on EO.
- Open questions were created to encompass the key attributes of the dimensions. Each attribute was measured by the interviewer for the dimension of the attribute, as perceived by the interviewee, in the firm. For ease of handling the data, the “dimension” of the attribute was graded by the interviewer from 1 to 5: 5 indicating the attribute is highly observable, recognisable and important to the firm, 1 indicating the attribute is not observable. The questions were designed to be answered twice, first as a reflection of the entrepreneur becoming a franchisor, and second as to how the entrepreneur would view the firm today.
- Entrepreneurs who had operated their firms for at least three years were chosen and their staff and franchisees had to be available to be interviewed. The purpose of interviewing staff and franchisees was to substantiate the data received from the entrepreneurial franchisor.
- Approval was sought from the CEO, being the entrepreneurial franchisor of the firm, for the interview. Approval was then sought to interview a staff member and a franchisee who had been associated with the franchisor for at least the past three years, or longer if possible, that would be able to validate the data collected.
- Following the interviews the cross-validated answers were analysed, in order to provide an overall analysis of the phenomenon.

## **The sample**

The three companies chosen fulfilled the requirements as set out in the methodology

Company A was an automotive franchise organisation with outlets throughout Australia, and has been in operation for 15 years. It has grown in the years 1991 to 2000 from 28 stores and a turnover of \$25 million to 95 stores and a turnover of \$140 million.

Company C provided foam rubber products and recreational items through its franchised retail stores. The operation commenced as a franchise company in 1995. The company has grown from no retail stores to 60 in six years and now has a turnover of \$50 million.

Company O was an office products organization that has been in operation for over 10 years. In 1998 they had a turnover of approximately \$100 million and 110 stores, today it has the same turnover and 91 stores.

## **RESULTS**

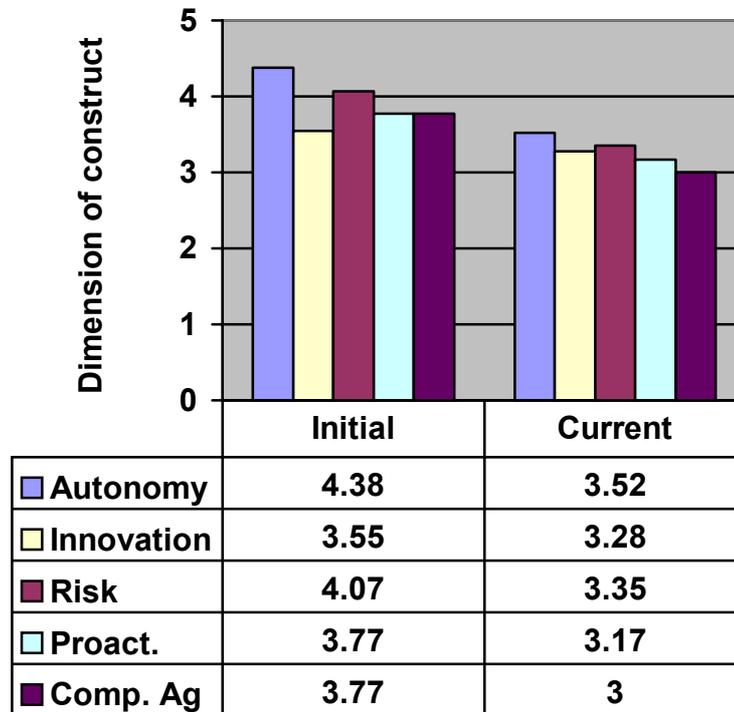
### **Presence of EO**

From the analyzed data it has been shown that EO is observable in the franchise industry, however its observation has reduced from its initial observation of 78 %, to 65 %.

Table one shows the measure of the dimensions grouped together to demonstrate the overall differences between the presences of EO initially observed in the companies and how this

compares with the observation currently. The measure is a continuum from unobservable to 5 being easily recognizable.

**Table 1: Average of Dimensions grouped initially and grouped as observed at the time of interview**



Whilst there were groups that influenced the overall findings within the dimensions, there was no significant impact by any single group. Therefore:

Hypothesis 1. *“All dimensions of EO will be found to be present in the beginning and over-time most will still be present”* has proven correct.

**Innovation**

The results do not rate innovation as that of being observed to the level of importance as hypothesized in this report. From the data, it does appear that one organisation is not as innovative as the other two, and if they had not been included, the results would be higher.

It was found overall that whilst innovation is present, it did not prove to be the most important dimension.

Therefore:

Hypothesis 2. *“Innovation is considered the most powerful dimension”* was not proven in this industry group and from the sample cases surveyed.

**Proactiveness**

The key component of proactiveness is to be able to seek out opportunities and capitalize on them, ensuring that the new product or service is able to shape the market. Responses demonstrated that most firms were working within their proven and tried environment, whereas it had been expected that EO organizations would attempt to be market leaders. The data showed that no

group within firms identified significant importance in proactiveness within this industry. This dimension also diminished over time.

Hypothesis 3. *“Proactiveness is difficult to initially achieve, but over-time the infrastructure enables new products and services to be introduced into the market with greater ease “has proved incorrect.*

### **Risk taking**

It was found that risk propensity, although identified, was not an apparent concern in the surveyed firms. The survey highlights this observation by placing risk as the second most observable dimension.

Hypothesis 4. *“Risk taking will be present, but the entrepreneur will not identify with risk-taking. They will identify with calculated risk and leveraging and identify that risk taking is part of the environment”.* This hypothesis is supported through the data, through the interviews, and through observation.

### **Competitive aggression**

All firms, their staff and franchisees, identified this dimension as the third most identified dimension. As with the other dimensions it diminished in importance over time. The interviews confirmed that competitive aggression was more important to the establishment and initial survival to the organization than current direction.

Hypothesis 5. *“Competitive aggression will be a key dimension to the entrepreneur in ensuring a secure supply base and market dominance”* is therefore supported by the data and from the interpretation of the interviews.

### **Autonomy**

The entrepreneurs demonstrated from their actions and the manner in which they conducted their professional interviews that they were in charge and had a clear focus on where they want to be in the future. They had a sense of purpose and pride, and the observable ethics and artifacts supported this conclusion.

Each staff member and franchisee in all firms said that if it had not been for their CEO (entrepreneurs), they would not be in business today. The driving force appeared powerful and authoritarian; most interviewees prefacing their observation of this topic by stating, "Don't get me wrong, I have the utmost admiration for..." when suggesting alternative methods of handling situations.

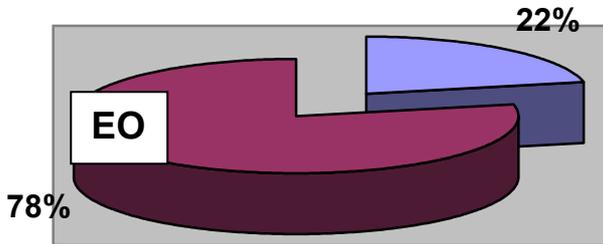
Hypothesis 6. *“Autonomy will be seen as the lifeblood of the entrepreneur, without it the entrepreneur cannot function. This dimension will interact strongly with the other dimensions and drive the dimensions of EO”.* This hypothesis is fully supported in all data.

### **Performance**

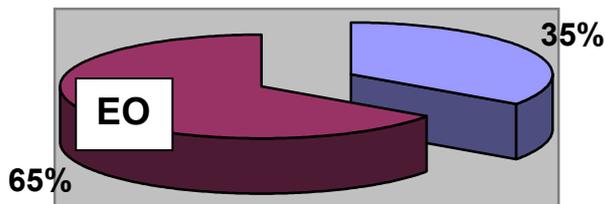
The analysis demonstrated that the sales volume has grown over the years observed. Whilst Company O had not increased sales volume, it had reduced its stores due to rationalization. Therefore considering the reduced outlets, the sales volume presented relates to an overall increase in performance.

In analysing the performance data obtained and shown in figures 2a and 2b, it is possible to identify that EO has been present over time.

**Figure 2a. Initial overall observable EO in all firms surveyed**



**Figure 2b. Current overall observable EO in all firms surveyed**



The relationship of performance and Entrepreneurial Orientation has been established and therefore:

Hypothesis 7. *“The relationship between EO and performance growth has continued over time”* is supported.

**A note on the research data**

This report is based on case study methodology, however, it was felt that there was a strong element from the interviews that was not being recognised as relating to the Lumpkin and Dess (1996) dimensions. In order to understand this, the principles of grounded theory were applied to the nine one-hour taped interviews. The interviews had been constructed in an open format allowing the interviewee to broadly speak about their organization together with the opportunities and problems associated with it.

Each interviewee spoke of the trust that existed between the franchisor, the staff and the franchisee as being an integral component in the operation of this industry. Although there are contracts and laws that protect all individuals, without the integrity and trust, growth would be limited.

## **CONCLUSION**

The purpose of this research was to identify if EO dimensions were a catalyst for the entrepreneurial environment in the franchise industry. If they were, are they still observable and have they continued to influence performance?

The results have proved that all EO dimensions are present in the franchise industry, and that with these dimensions present, all companies researched have experienced performance growth.

Autonomy appeared to be restricted through the increased structure of the franchise companies. Innovation and proactiveness are not as identifiable today as the proven systems add restrictions that would not have been in place with the entrepreneurial flair of the organizations' founders. Competitive aggression remains common within this industry, as the control over suppliers is critical. Changing market conditions and increased competition also focus attention in this area. Risk taking has proved to be another calculated business decision of the firm, with the risks identified not only including the impact on the company, but also the life and family of the entrepreneur.

The limitations in conducting this research included the small number of cases observed, and the available financial information. In addition, a more complete understanding of the environment in which these businesses operated during the period observed would have further assisted in proving the performance growth of the firm could be linked to EO.

From the findings it would appear that further research should be conducted into the performance of the Australian franchise industry as it is a significant employer, represents substantial sales volume, and has the opportunity for Australian export growth.

It has been identified that another dimension could be added to the work of Lumpkin and Dess (1996) to introduce the personal attributes of the entrepreneur and qualities of the entrepreneurial firm. Further research is therefore suggested to consider the qualities of trust, empathy and ethics that support the rationale for business decisions and in the interaction between customers, suppliers, staff and franchisees.

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