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A Conceptual study of the impacts of innovation to business performance in the context of Malaysian firms and businesses

MUSTAFA AHMED ALI
University Malaysia Sarawak, Kuching
Malaysia
Mälardalen University
Sweden

Abstract:

This research study focuses on assessing the relationship between company performance and innovation and validating the effects or impact of innovation on company performance based on the perspectives of Malaysian companies and business firms. The study's comprehensive background was set within the Malaysian business environment, which as reflected in majority of the literature sources gathered, support the predominant assertion that innovation has the capacity to create positive effects and impact on the companies' overall performance. This study also address the Malaysian business enterprises' lack of application and integration of the concept of innovation within their own business processes. Two innovation theories were applied in this research which included Everett Rogers' innovation diffusion theory and Joseph Schumpeter's innovation theory. From the theoretical evidences gathered through various literatures and journal articles, it was discovered that innovation is being greatly valued by many companies, especially Malaysian firms because of its critical role in improving the business performance of most business organizations. This literature review result therefore validated the study hypotheses that innovation only leads to a positive overall performance of firms and that innovation has a significant positive effect on the firm's financial and operational performances.

Key words: Innovation, business performance, organizational innovativeness, diffusion theory, innovation theory, OECD.

Introduction

Innovation has been a worldly emphasis for organizations and firms in this technology-driven era. Although there are extensive literatures providing elucidation to what innovation really meant, these varied definitions still points out to a broad understanding that innovation simply is the process of creating a new, distinct idea and/or invention that will be applied in the most critical tasks involved in the production, development as well as marketing functions of companies (Garcia & Calantone, 2002). It has also been quite certain that there has is a prominent link between organizational innovativeness and busienss performance, by which this current research is attempting to justify. In order to provide a comprehensive research about innovation-business performance relationship, this particular concept paper will tackle on the theoretical framework that guides the overall research, including the theories underpinning the research questions set forth and the identified variables that are to be explored and analyzed in the research.

Research Hypothesis

H1a: The higher the level of 'commitment to learning' amongst Malaysian firms, the higher the level of their capability to innovate.
H1b: The higher the level of focus on 'shared values' amongst Malaysian firms, the higher the level of their capability to innovate.
H1c: The higher the level of 'open-mindedness' amongst Malaysian firms, the higher the level of their capability to innovate.

H1d: The higher the level of practice of 'intra-organizational knowledge sharing' amongst Malaysian firms, the higher the level of their capability to innovate.

H2: The higher the level of learning orientation in Malaysian firms, the higher the level of firm innovativeness.

H3: The higher the level of learning orientation in Malaysian firms, the higher the level of firm performance.

H4: The higher the level of entrepreneurial orientation in Malaysian firms, the higher the level of firm innovation.

H5: The higher the level of market orientation in Malaysian firms, the higher the level of firm innovation.

H6: The higher the level of Malaysian firms' capability to innovate, the higher the level of firm performance.

Theoretical Framework

Supporting the major concepts, theories and variables as well are the major issues that innovation studies have mainly looked into over the years. As underscored by McDermott and Prajogo (2010), these are as follows:

1. The antecedents of innovation that emerges from either the internal and external perspectives. The internal antecedents refer to the organization, while the external antecedents pertained to the business environment.
2. The impacts of innovation to business performance.

The internal and external forces affecting firm performance through innovation has longed been used as a theoretical foundation in the field of innovation research and organizational competitiveness. In fact, OECD (2007) has provided two essential theoretical frameworks to look into as it best depicts the innovative system model. More so, the system of innovation approach was already acknowledged during the 80's and has been rapidly accepted in the academic field as the framework or policy-making model for innovation. This is illustrated as:

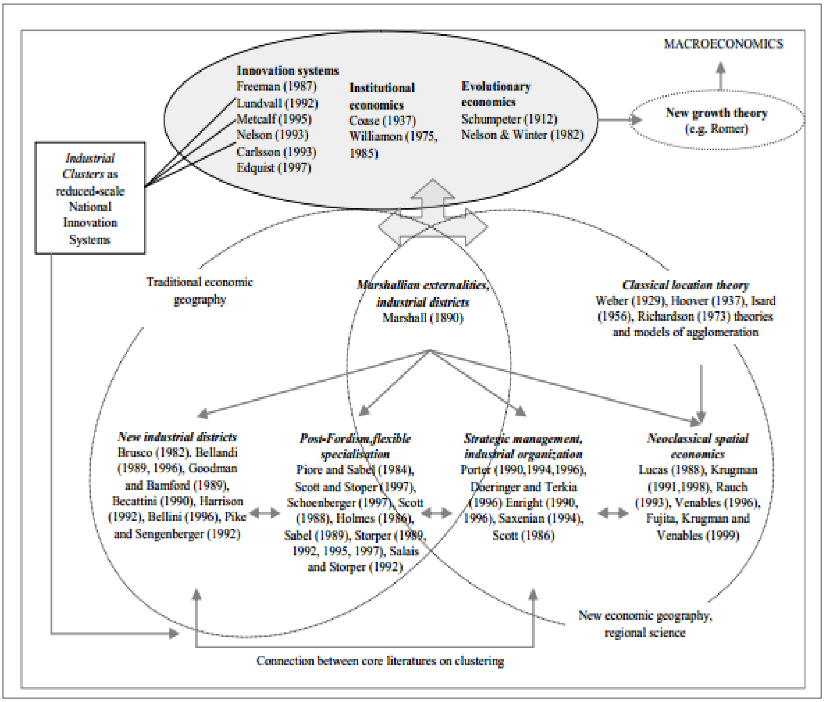


Figure 1 The theoretical foundation of a systemic approach to innovation (OECD, 2007)

Either way, it is essential to look into the above figure to further understand the whole business and innovation setting. Hence, the OECD (2007) underscored that the whole concept of national innovation system contains eclectic theoretical foundations. This can be associated with a number of economic thinking streams. This is as well better justified through the interactions of innovation to other business elements and environments, as illustrated in the figure below.

Figure 2 indicates the web interactions of innovation at different levels, such as between different or diverse organizations like firms, universities and research institutes. These contribute to the development or diffusion of innovation especially through technologies. This is also said to be undertaken through political, economic and social conditions affecting the actors and supply the framework within governments that create and implement policies. These in turn affects the innovation process—making it an interconnected systems or organizations or core actors and wider framework conditions.

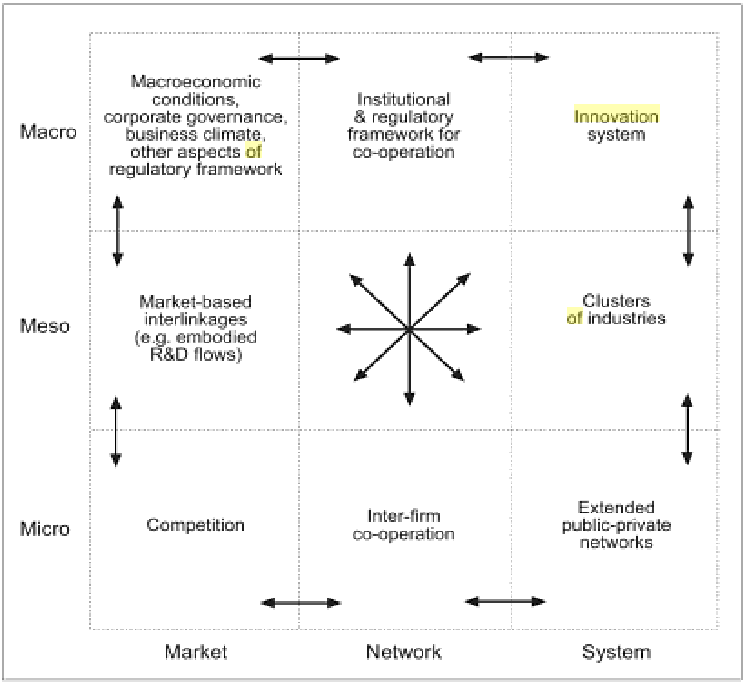
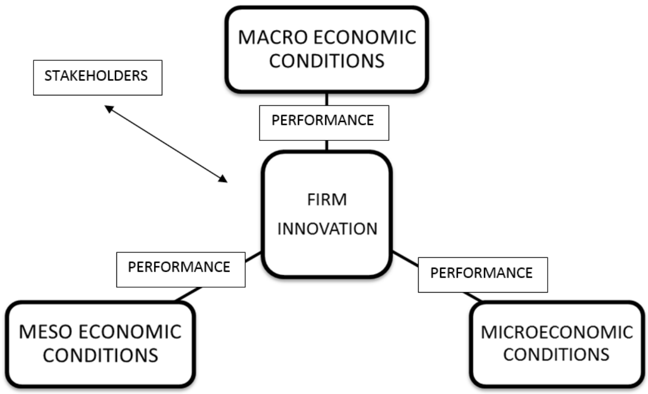


Figure 2 Interactions in innovation systems (OECD, 2007)

Through these, the possible connections between innovation and firm performance is instituted within certain factors, prior to the effects that requires assessment for the attainment or efficiency of firm performance. With the attempt of creating an uncomplicated theoretical framework for research using the theories researched, the figure below shall be used to underpin the concepts in this paper:



Basically, there are three conditions affecting the performance and innovation efforts of the firm. These are generalized as the macro-economic, meso economic and micro-economic conditions, as adapted from OECD. Since every economic and even the political and social status of any country is different, it is very essential to look into these aspects first. In this manner, this research will seek for the three conditions that would distinctly describe Malaysia's overall business environment. In doing so, the effects of the efforts and innovation strategies devised in order to meet the activities or pressures of the three conditions would be identified; prior to also identifying how these are addressed as depicted by the tactics and schemes.

Research Justifications

Seeking for the effects of innovation to firm performance may provide several explanations about the organization, which may come beneficial for the attainment of its organizational goals. In addition, innovation has longed been recognized as the one of the core sources of competitive advantages in business firms (Schumpeter, 1934). Inclusive in this are the service factors. This means that innovations in services have also resulted to the highest growth level and dynamism for a long period of time, particularly in the economic aspects. Moreover, innovation in the service firms has also transformed into an essential subject in business competition. This has as well aided the rising position of competitive advantage as a driving role; and thus resulted to the growing body of research.

On an added note, McDermott and Prajogo (2010) have provided important and extremely relevant ideas about the relationship of innovation and business performance, such as de Brentani (2001). de Brentani suggested the level for products and services to lay benefits through business performance, as affected by the innovativeness of the delivered products. These ideas have laid the assumption on how different small and huge companies render services, which in turn affects the delivery and perception of innovation. With these in mind, the research seeking about the effects of innovativeness on firm performance provide room for filling out some gaps, especially in terms of geographical distinctions. The reasons and measures behind the effects of innovation, particularly in Malaysia will also be explored.

Theories Underpinning Research Questions

The current thesis will place great emphasis on two notable and relevant theories that supports the research questions that the research will respond to – Innovation Diffusion Theory and Innovation Theory. These two theories are best fit for the research considering that these two conceptual ideas provide in-depth views on organizational innovativeness, which in the end likely aid in answering the research objectives set forth by the researcher.

Innovation Diffusion Theory

The theory of innovation diffusion is developed and popularized by Everett Rogers which explains the *what, why, and how* of new technologies and ideas as they spread from one culture to another. The innovation diffusion theory was well grounded from different well-established theories in sociology, psychology and communications used by Rogers (Wonglimpiyarat & Yuberk, 2005). This theory articulates and asserts that innovation basically goes through the process of diffusion most importantly when it is communicated through varied communication channels over a period of time.

More so, diffusion of innovation could be of great importance and is very much favourable for firms given the fact that it provides way for disseminating new techniques, products and services into the wider economy, thus giving the chance to gain full benefit for the company (Neely & Hii, 1998). Rogers also noted that this theory highlighted four basic elements that influence the process of spreading new ideas: innovation, communication channels, time frame and social system. To emphasize, diffusion basically involves how, when, and by whom an innovation is adopted. Adoption is defined as the decision to make full use of an innovation as the best course of action available. There are basically five stages through which individuals progress when evaluating an innovation for possible adoption – knowledge, persuasion, decision, implementation, and confirmation. This progress from initial knowledge of an innovation to confirmation of the adoption decision is referred to as the innovation-decision process (Weigel, Rainer, Hazen, Cegielski, & Ford, 2012).

Rogers also stressed out that in order for diffusion of innovation to happen, the innovative idea or the product should be flexible enough to be widely adopted across different culture and be self-sustainable (Greenhalgh, Robert, Macfarlane, Bate, & Kyriakidou, 2004). More so, Roger explained the perceived characteristics of innovation as relative advantage, compatibility, complexity, trialability and observability (Rogers, 2003).

- Relative Advantage – is the degree to which an innovation is perceived as better than the idea it supersedes (Rogers, 2003, p. 15).

- Compatibility – degree to which an innovation is perceived as being consistent with the existing values, past experiences and needs of potential adopters (Rogers, 2003, p. 15).
- Complexity – degree to which an innovation is perceived as difficult to understand and use (Rogers, 2003, p. 15).
- Trialability – degree to which an innovation may be experimented with on a limited basis (Rogers, 2003, p. 16).
- Observability – degree to which the results of an innovation are visible to others (Rogers, 2003, p. 16).

Theory of Innovation

The theory of innovation was developed by Joseph Schumpeter that highlights the importance of innovation as a vital component of economic change process (McCraw, 2007). This theory asserts that economic shifts is likely influenced and only be realized through three elements – innovation, market power and entrepreneurial activities. More so, this theory suggests that market power is derived from innovation with the capacity to endow more favourable results as compared to price competition and invisible hand.

In addition, Schumpeter's theory of innovation proves that through technological innovation, temporary monopolies are created which allow abnormal profits to emerge as well as compete with both rivals and imitators. Schumpeter further argued that the role of the temporary monopolies is important since they provide the necessary incentives for the firms to create and develop new processes and products (McCraw, 2007).

Research Variables

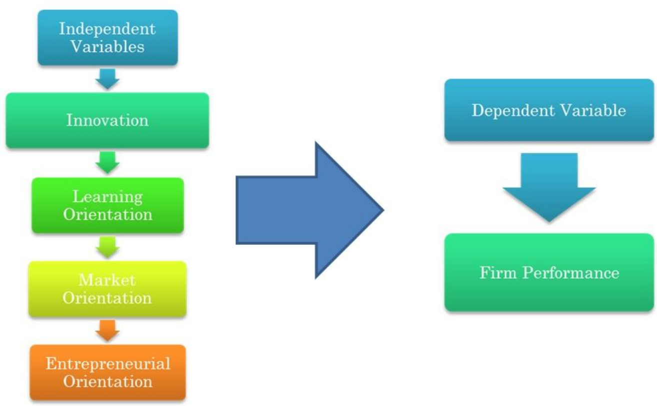
A similar study conducted by Neely and Hii (1998) have provided several important ideas that will be useful to the research. These as well provided supplementary concepts about the research variables to be studied, which will also be also considered as the variables to be looked into. Taking into account Rogers (1995, 2003), these variables are covered under organizational innovativeness, which has been stated to have emerged when researchers have began seeking for the organization's adoption unit. As underscored, these studies have emerged out of the criticisms on two grounds:

1. Most of the organizational innovativeness studies measured dependent variables based on the number of adoption of innovations, and then created composite scored in order to depict the organization's overall innovativeness. The said analysis type deemed to oversimplify the perplex nature of the innovation sources.
2. These studies were basically acquired from the organization's top executives that do not supplement the real measure of the innovation behavior of the whole organization. It has already been mentioned in the study that innovation in organizations has complex and multifaceted history in literature. This was confirmed with the assumption that the determinants of organizational innovativeness are misunderstood, which highlighted at least three sets of factors that influence innovativeness. These are organizational characteristics, managerial characteristics and environmental characteristics.

With these, Neely and Hii (1998, p.22) defined innovativeness as "the propensity to innovate," which is said to be applicable to an individual and the firm. In addition, the details presented by Rogers (1995, 2003) will be used in this paper, especially that it represented the needed variables for firm innovativeness. However, these variables will be mainly used within the context of Malaysian firms and businesses. This sets mainly the difference that this study has over other related research papers.

For this research, firm performance will be the dependent towards any Malaysian firm's approach of innovation. To put it simply, how organizations utilize their idea of innovation will identify their performance. Under the concept of innovation are the factors defining it such as learning orientation, market orientation and entrepreneurial orientation. It is also essential to note the various influencing factors of learning orientation, which are commitment to work, shared values, open-mindedness, and intra-organization knowledge sharing.

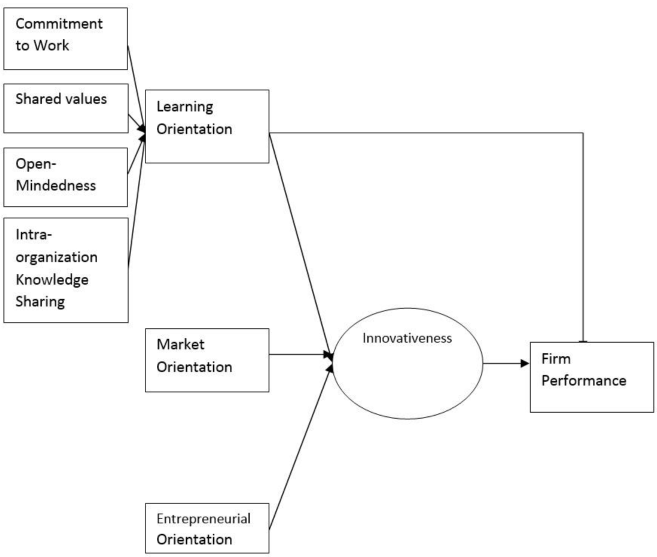
The variables for this study are best depicted below.



Source: Developed For This Research.

Conclusion

It is very much unparalleled that organizational innovativeness plays significant role in every aspect of business processes, which in the end forefront the company in reaching maximum business performance. To reiterate, the research seeks to identify the impacts of innovation to business performance which will be guided with the theoretical framework developed based on the extensive literature. With these as well, this concept paper will underscore the micro-economic conditions of the firms of Malaysia, prior to certain conditions affecting firm performance. These details are also best illustrated in the framework below, which as well represents the paper's overall framework.



More so, the research also utilized the concepts and ideas presented by two of the most popular theories of innovation which are the theory of innovation diffusion and the theory of innovation. These two serves as the basis for the identification of research questions that are sought to be answered by the research.

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