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Innovativeness among small businesses: Theory and propositions for future research

Angela Hausman*

The University of Texas - Pan American, 1201 W. University Drive, Edinburg, TX 78539, USA

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Abstract

Small businesses represent the lifeblood of the economy. Variations in the innovativeness of these firms may help explain why some succeed, but many fail [Frambach, R. T. (1993). An integrated model of organizational adoption and diffusion of innovations. *European Journal of Marketing, 25*(5), 22-41; Nord, W. R. & Tucker, S. (1987). *Implementing routine and radical innovations.* Lexington, MA: Lexington Books.]. To understand how small businesses develop and use innovations, a series of depth interviews were conducted with small, family-owned firms in the US and Spain. Results suggest several factors affect innovativeness, including industry-specific, firm-specific, and innovation-specific factors. The study ends with a series of propositions, potential managerial implications of the study, and suggestions for further research.

Keywords: Innovation; Innovativeness; SME; Small business

1. Introduction

Despite their public prominence and political influence, the economic impact of large businesses is about equal that of small businesses. For instance, nearly one-half of the US GDP in 1999 was attributable to small businesses, which employed 68.2 million people or 58% of the 1999 employment (Small Business Administration, 2001). EU countries show lower, but still substantial, economic contributions attributable to small businesses (Bednarzik, 2000). In fact, most businesses started as small ventures. These factors argue strongly for a more thorough understanding of factors influencing the success of these businesses. Among the most important aspects of success in small firms is innovativeness, as exemplified by the phenomenal growth of start-up ventures like Starbucks, Apple Computers, Dell, and Kinkos (Daily & Thompson, 1994). These firms are able to capitalize on customer closeness and flexibility to satisfy rapidly changing customer demands, thereby creating valuable competitive advantages (Hausman & Fontenot, 1999). Problems retaining this nimbleness might help explain why such a large percentage of these businesses fail (Drozdow & Carroll, 1997).

But, how do small firms remain innovative when they face scarce resources and have little market influence? The answer, while obfuscated by a relative paucity of research, is that they conceivably do it in different ways than large businesses (Yap and Souder, 1994). The purpose of this study is to fill this void by developing an understanding of factors affecting innovativeness among small businesses. Unfortunately, the literature does not provide sufficient detail for deductive model development; hence we used an inductive, multiple informant procedure similar to that utilized by Rogers and Shoemaker (1971) and Rogers (1995). A grounded theory interpretation of qualitative data was combined with extant literature to develop a series of propositions related to innovativeness in small businesses (Glaser & Strauss, 1967; Strauss & Corbin, 1994). The following sections will first review extant theories of

* Tel.: +1 956 381 2826; fax: +1 956 384 5065.
E-mail address: hausman@panam.edu.

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innovativeness, then develop a series of propositions with suggestions for future research.

2. Innovativeness in small firms

Small firms are more than simply smaller versions of major corporations, especially when one talks about family-owned businesses. Not only do they lack the financial and human capital common in large businesses, their governance and reward structure are often entirely different. Thus, it is unclear whether theories developed to understand large firms apply to small businesses.

Some characteristic features of small businesses suggest an increased ability to respond to changing environmental needs. As mentioned earlier, closeness between small business customers and managers can provide impetus for innovation due to the ease with which these managers can identify unmet customer needs. Less bureaucracy and more clannish structures, which are common in small businesses, might also improve inter-organizational trust, communication, and cooperative competency that contribute to innovativeness (Olson, Walker, & Reukert, 1995; Sivades & Dwyer, 2000). Owners also normally have more operational expertise, which, combined with superior customer knowledge, might translate into innovative solutions (Dahl & Moreau, 2002).

Counteracting the benefits of these internal strengths are external weaknesses. Among the weaknesses is the somewhat parochial nature of small businesses, resulting in fewer external contacts that might otherwise increase the "seek and respond" capability of the firm (Srinivasan, Lilian, & Rangaswamy, 2002). As a result, small businesses become less innovative over time as they become less aware of environmental changes or innovative solutions. This relative paucity of weak ties was identified by Hausman and Fontenot (1999) as a major impediment to innovativeness in small businesses.

Other features of small firms support the contention that they have a difficult time adapting to changes in the economic, technological, or competitive markets (Drozdow & Carroll, 1997; Gallo & Sween, 1991). For instance, small business managers often lack the types of education and training that have been linked with innovativeness (Romano, 1990). This lack of strategic expertise prevents small firms from transforming their superior customer knowledge into new products and services (Davis, Hills, & LaForge, 1985; Gruner & Homburg, 2000; Sethi, Smith, & Park, 2001).

Small businesses are also closely held, with power and decision-making concentrated in the owner/manager (Dyer & Handler, 1994). Thus, innovativeness may translate into the innovativeness of the owner/manager rather than the innovativeness of the firm (Verhees & Meulenberg, 2004). Commonly these owners reject the advice of others and are reluctant to delegate authority or decision-making to others, which conspires to reduce innovativeness (Dyer & Handler, 1994). In addition, over-involvement by the owner in operational level decisions and family considerations might reduce their tendency to take risks (Sethi et al., 2001). Moreover, strategic decisions are often framed within the constraints of family and individual goals, rather than maximization of firm potential, which might encourage firms to reject changes due to their concomitant conflict (Davis et al., 1985; Donckels & Fröhlich, 1991; Dyer & Handler, 1994). Empirical and theoretical evidence linking these variables with innovativeness in small business is limited and mostly anecdotal, suggesting further study is needed to explicate their importance in small business innovativeness.

Manager/owners are also risk averse and conservative (Donckels & Fröhlich, 1991; File & Prince, 1996). Since innovation and adoption involve risks, risk-aversion and conservativeness reduce innovativeness. From a practical perspective, small firms have limited financial capacity, suggesting they lack the financial resources to capitalize on innovative opportunities that can be very risky and costly (Davis et al., 1985; Sivades & Dwyer, 2000).

3. Description of research activity

To fully understand the forces affecting innovativeness in small businesses, quantitative research is often less valuable than qualitative research mainly because there is little guidance regarding what factors to measure. Supporting this, Rogers and Shoemaker (1971) provide pages of potential variables that have been tested for their impact on either individual or organizational adoption in prior research. In fact, Rogers (1995) identifies the large number of variables and contrary findings across studies investigating them as one of the fundamental problems in this research area. In small business research, this problem is compounded by the lack of prior research and questions regarding the validity of existing measurement tools and theories in firms that differ in organizational structure and firm characteristics from the large firms used in developing the tools (Romano, 1990).

To investigate the most salient features accounting for firm innovativeness, small family-owned businesses were chosen since they are the most common type, representing 90% of all US small businesses (Daily & Thompson, 1994). In-depth, qualitative analysis was used as it provided an opportunity to develop theory from observations, rather than imposing pre-determined models on the data (Huberman & Miles, 1995). Multiple sites provided both greater generalizability and explanatory ability by highlighting commonalities and particular factors affecting innovativeness (Huberman & Miles, 1995). By comparing features of innovative and less innovative firms, we were able to identify aspects that might account for this difference. This methodology is particularly useful when the underlying