



Entrepreneurial orientation in turbulent environments: The moderating role of absorptive capacity



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ABSTRACT

The literature on entrepreneurial orientation (EO) has confirmed the positive relationship between EO and firm performance and that relationship's dependence on several contingencies. The present study connects the resource-based view and its dynamic capability extension to introduce absorptive capacity (ACAP) as a moderator of the relationship between EO and firm performance. This theoretically derived research model is empirically validated using survey data from 219 small and medium-sized enterprises in Germany. Our empirical findings are that ACAP strengthens the EO–performance relationship in turbulent markets.

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1. Introduction

Entrepreneurial activity in both start-up and corporate contexts has been identified as a major engine for the generation of employment and the creation of economic growth and welfare (Wong et al., 2005). Accordingly, there is a strong interest in what entrepreneurial behavior looks like and in its antecedents and concrete consequences. In the corporate context, the literature has examined the construct of entrepreneurial orientation (EO), a strategic posture that reflects the specific processes, practices, and behaviors that allow a firm to act in an entrepreneurial way (Covin and Slevin, 1991; Lumpkin and Dess, 1996). In 1983, Miller introduced EO into the academic literature, conceptualizing the construct along three firm-level dimensions: innovativeness, proactiveness, and risk-taking. Since then EO has developed into one of the most established constructs in the entrepreneurship literature (Wales et al., 2011). A major tenet is that firms with strong EO outperform other firms.

However, while many studies and a meta-analysis (Rauch et al., 2009) largely confirm the positive performance contribution of EO,

a few studies find no positive relationship between EO and performance (e.g., Ireland et al., 2003). Extant research is more consistent in showing that the strength of the EO–performance relationship depends on various contingencies (Lyon et al., 2000), including external conditions (e.g., Zahra and Covin, 1995) and internal variables (e.g., Covin et al., 2006). In terms of the latter, recent research finds that firm-level resources and capabilities, both tangible (e.g., financial resources; Wiklund and Shepherd, 2005) and intangible (e.g., leadership styles; Engelen et al., 2013a), moderate the EO–performance relationship, pointing out the general importance of firm-level resources and capabilities in facilitating the EO–performance relationship.

The present study extends research on how EO interacts with firm-level capabilities to increase firm performance by arguing that dynamic capabilities play a central role in converting EO into improved performance. Dynamic capabilities differentiate from “ordinary” resources and capabilities, as they allow the firm to reconfigure its existing resource and capability base (Teece et al., 1997). We argue that, in order to implement inherently uncertain entrepreneurial activities smoothly, a reconfiguration of the existing resources or capabilities that dynamic capabilities can provide is necessary, as the inertia of stable, “ordinary” resources and capabilities may not allow the full potential of an EO to be realized (Eisenhardt and Martin, 2000). The strategic management literature discusses which capabilities qualify as dynamic and has largely agreed that the firm's absorptive capacity (ACAP) is a major dynamic capability (van den Bosch et al., 1999; Floyd and Lane, 2000; Zahra and George, 2002). ACAP, which refers to “an ability to recognize the value of new information, assimilate it, and

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apply it to commercial ends” (Cohen and Levinthal, 1990; p. 128), is a dynamic capability that appears particularly relevant to EO since a major obstacle in effectively and efficiently implementing entrepreneurial activities is the handling of uncertain situations in which typically established knowledge and information are missing (Lumpkin and Dess, 1996).

In order to develop a nuanced understanding of how EO and ACAP interact, we also examine how the turbulence of the market in which the firm operates is related to the interaction of EO and ACAP. We argue that *the facilitating role of ACAP on the EO–performance relationship should be strongest in turbulent markets* based on the assumption that dynamic capabilities like ACAP are most valuable in dynamic environments (Zahra et al., 2006). In these environments, the generation of new information and knowledge appears particularly important for entrepreneurial firms, as does a timely response to new circumstances.

In order to validate our theoretical arguments empirically, we analyze survey data from small and medium-sized companies. The empirical findings provide support for our core expectation that the link between the interaction of EO and ACAP to firm performance strengthens, as market turbulence increases.

We contribute to the EO and dynamic capabilities literatures in two major ways. First, in terms of EO literature, we develop a theoretical rationale for how EO interacts with ACAP as a major dynamic capability that is required in order to increase firm performance. In so doing, we link EO to the theory of dynamic capabilities and address Miller's (2011) call to embrace theories of related disciplines, such as strategic management, in order to clarify which resources and capabilities foster a robust entrepreneurial process. Dynamic capabilities, which have been conceptually expected to be the “key means for linking EO to firm opportunity exploitation and subsequent performance” (Covin and Lumpkin, 2011; p. 861), still require examination in this context. Second, we contribute to the literature of dynamic capabilities. Barreto's (2010) recent review of the dynamic capability literature claims that it is centrally important to determine whether dynamic capabilities like ACAP lead directly to performance consequences and to understand the dynamic capabilities' boundary conditions. We establish theoretical arguments and provide empirical validation that the dynamic capability of ACAP interacts with a strategic posture (i.e., EO) in order to reap the full performance benefits of EO and that the degree of market turbulence determines the strength of ACAP's role. In so doing, we add market turbulence as an important boundary condition to the dynamic capability literature.

2. Theoretical background and research model

This study is based on Miller's (1983) definition of EO as a strategic posture that primarily applies to entry into new businesses. Miller conceptualizes EO as the simultaneous presence of the three dimensions of innovativeness, proactiveness, and risk taking (e.g., Wiklund and Shepherd, 2005). Innovativeness describes a firm's propensity to experiment with new ideas in order to activate a process that results in new products, services, or technological progress (Covin and Slevin, 1991). Proactiveness is characterized by a high level of opportunity-seeking, ideally ahead of competitors and combined with anticipation of future customer demands. Risk taking refers to bold moves into unknown business areas and/or the commitment of significant resources to business activities under conditions of uncertainty (Lumpkin and Dess, 2001). EO is understood as a firm-wide construct, so most, if not all, firm members are involved in implementing this strategic posture (Wales et al., 2011). There is also agreement that implementing EO is a complex task that requires repeated trial-and-error and experimentation (Covin et al., 2006).

A major interest in the EO literature has concerned how EO improves firm performance. From a conceptual stance, Lumpkin and Dess (1996) argue that entrepreneurial firms achieve superior performance by recognizing new opportunities with potentially large returns, by targeting the most promising premium market segments, and by obtaining first-mover advantages. However, empirical tests of this performance-enhancing role of EO reveal contradictory results. While most studies confirm the performance-enhancing character of EO, a few studies could not determine a positive relationship (e.g., Ireland et al., 2003). Extant research on the EO–performance relationship has more consistently identified various moderating variables that facilitate or inhibit this relationship. Table 1 provides an overview of extant empirical research on these moderators.⁴

Whereas the first studies in the 1980s and 1990s focus on external factors like environmental turbulence as moderators (e.g., Covin and Slevin, 1989), more recent studies examine the moderating role of internal factors like strategic decision-making styles (Covin et al., 2006; Chirico et al., 2011). Most recently, internal resources and capabilities have gained attention and have been shown to impact the EO–performance relationship, which is in line with Kreiser's (2011; p. 1026) view that entrepreneurial firms “are more dependent on their ability to fully utilize resources than other types of firms are.” These studies can be divided into research on tangible resources like financial capital (e.g., Wiklund and Shepherd, 2005) and intangible resources like leadership (e.g., Engelen et al., 2013a).

The reasoning on why internal resources and capabilities are important for the EO–performance relationship is based on the resource based view (RBV). According to the RBV, firms are unequally distributed bundles of resources (Wernerfelt, 1984), creating resource heterogeneity that persists over time and provides a basis for firm performance (Barney, 1991). The “strategic fit” paradigm from strategic management states that, for each strategic posture (such as EO), there is a set of firm-level resources and capabilities that facilitate the performance effects of the strategic posture (e.g., Slater et al., 2006; Song et al., 2007; Desarbo et al., 2005). In other words, firms should allocate their investments in resources and capabilities consistent with their strategic postures (Teece, 2012). In keeping with this rationale, strategic orientation (in our case, EO) describes *what* a firm strategically does, and the capabilities capture *how* this strategy can be implemented and deployed (Slater et al., 2006). In terms of EO, Habbershon et al. (2010; p. 21) support the notion that an entrepreneurial firm requires specific resources since “resources and entrepreneurial orientation taken on their own are necessary but not sufficient conditions for long-term success. Without resources, entrepreneurial orientation lacks the means to be realized.”

However, research has recognized certain shortcomings of the RBV, especially for firms that act in turbulent environments, which is likely to be the case for many entrepreneurially oriented firms (Covin and Slevin, 1989). Therefore, the dynamic capability perspective was developed to extend the RBV and to answer the question concerning what changes or recombines the resource base when the firm's environment is characterized by constant change (Teece and Pisano, 1994; Barreto, 2010). Central to the definition of a firm's dynamic capabilities are the organizational and strategic routines by which its existing resources base is reconfigured (Winter, 2003). However, these dynamic capabilities have largely been ignored in EO research, an observation recently confirmed by Covin and Lumpkin (2011), who speculate that dynamic capabilities

⁴ We identified this list of studies by first taking all studies of the meta-analysis on the EO–performance relationship from Rauch et al. (2009) into account and then studying the reviews on the EO literature from George and Marino (2011) and Wales et al. (2013) to add more recent studies.

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