



## The moderating impact of internal social exchange processes on the entrepreneurial orientation–performance relationship

Dirk De Clercq<sup>a,\*</sup>, Dimo Dimov<sup>b,1</sup>, Narongsak (Tek) Thongpapanl<sup>c,2</sup>

<sup>a</sup> Brock University, Faculty of Business, 500 Glenridge Avenue, St. Catharines, Ontario, Canada L2S 3A1

<sup>b</sup> University of Connecticut, School of Business, Department of Management, 2100 Hillside Road Unit 1041 Storrs, CT 06269-1041, United States

<sup>c</sup> Brock University, Faculty of Business, 500 Glenridge Avenue, St. Catharines, Ontario, Canada L2S 3A1

### ARTICLE INFO

#### Article history:

Received 23 May 2008

Received in revised form 13 January 2009

Accepted 15 January 2009

#### Keywords:

Entrepreneurial orientation

Social exchange theory

Procedural justice

Trust

Organizational commitment

### ABSTRACT

This paper applies a social exchange perspective to understand the internal contingencies of the relationship between entrepreneurial orientation (EO) and performance. It focuses on two aspects of social interactions among functional managers (procedural justice and trust), as well as on their organizational commitment, as potential enhancements to the firm's successful exploitation of entrepreneurial opportunities. A study of 232 Canadian-based firms finds several positive moderating effects: The EO–performance link is stronger for higher levels of procedural justice, trust, and organizational commitment. In addition, consistent with a systems approach to organizational contingencies, the EO–performance relationship is stronger when the organization's social context comes closer to an “ideal” configuration of procedural justice, trust, and organizational commitment that is most conducive to knowledge exchange within the organization. The study's implications and future research directions are discussed.

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### 1. Executive summary

This study examines the roles of social relationships between functional managers and their commitment to the organization in shaping the entrepreneurial orientation (EO)–performance relationship. In the context of prior studies that typically focus on the external factors that affect the EO–performance relationship, as well as recent research that has begun to explore its internal contingencies, limited attention centers on how the successful exploitation of entrepreneurial opportunities might depend on social interactions within the firm. Because social exchanges are instrumental for the firm's ability to combine knowledge across different functional areas, they can interfere in the successful enactment of the firm's entrepreneurial posture.

Drawing from prior work on social exchange relationships, we consider three characteristics that collectively represent an organization's internal social context and that affect the extent and quality of internal knowledge exchange and thus the strength of the EO–performance relationship: (1) procedural justice in cross-functional relationships, (2) trust between functional managers, and (3) managers' commitment to the organization and its goals. Examining a sample of 232 Canadian-based firms representing a broad range of industries, we find that the overall positive relationship between EO and performance becomes nuanced once we account for social exchange processes. In particular, the relationship is positive only at high levels of procedural justice, trust, and organizational commitment; it is further amplified to the extent that the organization's social context approaches an “ideal” configuration of procedural justice, trust, and organizational commitment.

This study contributes to entrepreneurship literature by drawing attention to and providing a theoretical elaboration of how the internal social context affects the EO–performance relationship. Specifically, internal social exchanges influence the firm's

\* Corresponding author. Tel.: +1 905 688 5550x5187; fax: +1 905 984 8068.

E-mail addresses: [ddeclercq@brocku.ca](mailto:ddeclercq@brocku.ca) (D. De Clercq), [dimo.dimov@business.uconn.edu](mailto:dimo.dimov@business.uconn.edu) (D. Dimov), [nthongpa@brocku.ca](mailto:nthongpa@brocku.ca) (N.(T.) Thongpapanl).

<sup>1</sup> Tel.: +1 860 486 3638; fax: +1 860 486 6415.

<sup>2</sup> Tel.: +1 905 688 5550 x5195; fax: +1 905 378 5716.

ability to combine knowledge across functional boundaries, which in turn affect its ability to exploit new opportunities successfully. By discussing how cross-functional procedural justice and trust promote the quality of decision making when confronted with entrepreneurial opportunities, we offer new insights into the role of formal and informal collaboration among functional departments for the successful implementation of a firm's EO. Furthermore, we highlight how functional managers' commitment to their organization can act as a catalyst to collaboration and knowledge exchange. By internalizing the entrepreneurial goals of their organizations, committed managers can enhance the cohesion and critical thinking that organizations require to realize their entrepreneurial potential. We also contribute to literature on entrepreneurial orientation by using a systems perspective to understand how internal social contingencies collectively help translate a firm's entrepreneurial posture into successful performance.

From a managerial point of view, this study suggests that when a firm seeks to adopt an entrepreneurial orientation, top managers should focus not only on navigating the external environment but also on ensuring that procedural justice and trust permeate the relationships between functional departments. Ultimately, strong social relationships might make functional managers less likely to identify themselves as marketers, salespeople, product designers, or engineers and instead encourage them to perceive each other as "partners" with common interests in identifying and exploiting entrepreneurial opportunities for the firm. Finally, by fostering commitment and inspiration throughout the ranks of the organization, top managers can create further impetus for cross-functional initiatives and collaboration that facilitate knowledge exchange and ultimately help fulfill the firm's entrepreneurial potential.

## 2. Introduction

In changing and increasingly competitive environments, firms must constantly seek out entrepreneurial opportunities (D'Aveni, 1994) and translate them into improved performance outputs (Hitt et al., 2001). To this end, a firm's entrepreneurial orientation (EO)—that is, its strategic posture to be innovative, proactive, and risk taking—takes on instrumental importance (Covin and Slevin, 1991). Many studies demonstrate the beneficial influence of EO on firm performance (Wiklund, 1999; Wiklund and Shepherd, 2005; Zahra, 1991; Zahra and Covin, 1995), but studies in which this relationship does not hold (Smart and Conant, 1994) and arguments for the lack of universal applicability of an entrepreneurial strategic posture (Hart, 1992) have prompted further theoretical elaboration of the EO–performance relationship, highlighting its various contingencies (Lumpkin and Dess, 1996). Accordingly, a stream of studies reveals the moderating roles of *external* factors such as environmental hostility, turbulence, and dynamism (Covin and Covin, 1990; Dess et al., 1997; Namen and Slevin, 1993; Wiklund and Shepherd, 2005), external networks (Lee et al., 2001; Stam and Elfring, 2008), and national culture (Arbaugh et al., 2005).

Yet for entrepreneurial orientation to result in performance advantages, it also needs to be properly and successfully managed *within* the organization (Covin et al., 2006; Miller and Friesen, 1986), which involves exploiting opportunities through the development and deployment of resources across organizational units (Ireland et al., 2003; Kuratko et al., 2005). Therefore, understanding how firms can enable and effectively implement their entrepreneurial orientation also requires consideration of *internal* organizational processes (Lumpkin and Dess, 1996; Wiklund and Shepherd, 2005) and the leveraging of resources such as knowledge across functional departments (Floyd and Lane, 2000). In this regard, apart from the roles of the firm's resources (Wiklund and Shepherd, 2005), market orientation (Bhuian et al., 2003), and strategy formation process (Covin et al., 2006), the social aspects of the effective exploitation of entrepreneurial opportunities, which enable and promote knowledge exchange within the organization, have largely remained unexplored. Notably, social exchanges underlie the organization's capability to combine effectively the knowledge embedded in different functional areas (De Luca and Atuahene-Gima, 2007) and are particularly conducive to entrepreneurial behavior when internal relationships are characterized by fairness, trust, and organizational support (Hornsby et al., 2002; Kim and Mauborgne, 1998; Kuratko et al., 2005). Hence, we pose the following research question: How does firms' internal social context influence their ability to exploit entrepreneurial opportunities?

To address this question, we consider the intricate interplay between the content of a firm's strategic posture (i.e., entrepreneurial orientation) and the social processes within the firm's borders (Covin et al., 2006). Specifically, we focus on the interactions and attitudes of mid-level, functional managers (Hornsby et al., 2002; Kuratko et al., 2005), who oversee the sub-processes through which an organization's higher-level, strategic decisions get implemented (Burgelman, 1983; Floyd and Lane, 2000; Floyd and Wooldridge, 1997) and thus epitomize the enactment of a firm's entrepreneurial posture (Kuratko et al., 2005). From their unique position to evaluate and re-direct knowledge flows within the organization (Kanter, 1985) and their engagement in *social* interactions that affect the volume and quality of knowledge flows (De Clercq and Sapienza, 2006; Floyd and Lane, 2000), these managers play instrumental roles in the exploitation of entrepreneurial opportunities (Floyd and Wooldridge, 1997; Mom et al., 2007).

Consistent with prior work that highlights the influence of procedural justice (Sapienza and Korsgaard, 1996), trust (Nahapiet and Ghoshal, 1998), and organizational commitment (Kim, 1998) on effective knowledge sharing in social exchange relationships, we focus on how these three social exchange processes influence the EO–performance relationship. We argue that procedural justice, trust, and organizational commitment *each* facilitate the firm's ability to exploit entrepreneurial opportunities by enhancing the amount and quality of knowledge exchange across functional departments (De Clercq and Sapienza, 2006). In addition, these three factors *collectively* constitute a conceptually meaningful gestalt (Covin et al., 2006; Miller, 1986) that reflects how the organization's internal social context can influence the exploitation of entrepreneurial opportunities (Kim and Mauborgne, 1998). To this end, we apply a systems perspective to understanding the contingent influence of social context (Drazin and Van de Ven, 1985) and focus on the holistic configuration of its characteristics (Govindarajan, 1988; Ketchen et al., 1993, 1997; Meyer et al., 1993; Payne, 2006). To the extent that an "ideal" configuration of factors aligns best with the implementation requirements of a particular strategic posture (e.g., Venkatraman, 1989; Vorhies and Morgan, 2003), the similarity to that

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