1. INTRODUCTION

INTRODUCTION TO THE STUDY

1.1. Introduction

Ethiopian business organizations have been operating in different regulatory systems. Under those systems, they have experienced different rules and regulations that have both favorable and unfavorable impact on their business performance. However, currently these business organizations have a support from the government. The current government of Ethiopia has an objective of industrializing the country. For this purpose, manufacturing firms, especially large-scale manufacturing firms take the lion’s share in order to attain the objectives of the government. Not only attaining, they must also perform better than their counter parts as they face similar competitive environment calling for proper strategic alignment.

The success of a given company is then dependent on how well it focuses on its strategic management. For superior business performance, management is trying to focus on varied areas of strategy issues. The management of the organization is dealing with the external environment, the internal environment or a combination of both. In doing this, the top management may focus on the market where it can be defined as the customers to be served, the competitors surrounding its business and the way to serve these customers (Narver and Slater, 1990). The company also deals with the role of entrepreneurship in achieving the corporate goal of its business performance; and the company is focusing on the innovation and technology that help improve their performance in different measures (Freeman, 1994; Lawless and Anderson, 1996).

In today’s competitive environment, managements’ of several companies are pursuing how to gain higher business performances than their competitors. These managers are therefore engaged in dealing with the role of strategic orientation in achieving higher business performance. Strategic orientation of firms can then be a combination of market orientation, entrepreneurial
orientation and proclivity towards technology (innovation) (Mu & Di Benedetto, 2011). This thesis outlines how strategic orientation influences the performance of business organization with specific analysis of large-scale manufacturing firms in Ethiopia. This study provides a methodology for measuring the impact of strategic orientations on business performance in case of Ethiopian manufacturing firms that can then be replicated in other developing nations.

1.2. Overview of Ethiopian Manufacturing Industries

1.2.1. Introduction

In any countries all over the world, the role of manufacturing is so crucial in determining their level of development. Manufacturing leads to the creation of products that are obtained through the transformation processes. Thus, it is critical and is perhaps the most important instrument of long-term growth and development. Better revenues can be generated from the transformation of primary agricultural based economy to manufacturing-based economies. Based on the study conducted by Addis Ababa Chamber of Commerce and Sectoral Associations/ AACCSA (2015), the history of modern manufacturing industry in Ethiopia started in the years of 1920s mainly following the construction of the Ethio-Djibouti railways. During this period, manufacturing started with a simple processing technology that produces agriculture-based products. Growing demand for balancing the cost of importing manufactured goods and the rising cost of transportation for the imported goods were put the pressure to produce at home base. Thus, because of this, Ethiopian manufacturing firms are assumed to have profited from the entrepreneurial skills of foreigners like Armenians, Italians, Greece, and Indian citizens who had started living in the country at the time (Befekadu et. al., 2000; Wodajo and Senbet, 2013).

The sector is still young, even infant as compared to African standards, mainly focusing on semi-processing. A few commonly strengthening components have schemed to keep the development of a more grounded manufacturing base in
the nation. Nevertheless, Ethiopia has the way to change those elements that are meeting up in the meantime, for example, shoddy work drive and accomplished, trainable and cheap work and supplies of utilities. Also, the strategy structure is helpful for manufacturing development as it proposes to drive manufacturing development through vertical and even connections to the rich asset base of agricultural and mineral, both of which have strong development prospects in their own privilege, AACCSA (2015)1.

Manufacturing is a wealth making a sector of an economy, and firmly associated with engineering and industrial development and gives vital material backing to the national framework. It includes the mechanical or physical change of items into a new mixture or substances into new products. It makes products from raw materials by the utilization of physical work or machines and is typically done systematically with a division of work. In a more constrained sense, manufacturing is the creation or transformation of parts of completed items on a genuinely substantial scale (CSA, 2012)5.

The legislature of Ethiopia changed the economy since 1991. The legislature has composed and embraced Agricultural Development Led Industrialization (ADLI) procedure to annihilate destitution. The Industry Development Strategy of the nation has set up the rule that basically concentrate on the advancement of agricultural-led industrialization, export-led improvement, and extension of work serious commercial enterprises. As obviously expressed in the nation's industrial development strategy, values adding private sector is viewed as the motor of the areas' development. During the implementation of Growth and Transformation Plan (GTP) of the country, the manufacturing sector received greater emphasis by way of boosting export based and import-substituting industries. Agricultural and industrial sector have been promoted through vertical and horizontal linkages between them. This also stresses the commercialization and agro-industrialization of the agriculture sector and value chain approach, AACCSA (2015)1.
Regardless of remarkable efforts made and the economic growth achieved, the Ethiopian economy remains struggling with structural problems. The manufacturing sector in Ethiopia is still at its young age. The manufacturing sector, for example, has a limited share in terms of production, employment, and exports when compared to the agriculture and service sectors (AACCSA, 2015).

1.2.2. Productive Capacity and Capacity Utilization

Ethiopian manufacturing industry has been characterized by low productivity and hence the competitiveness of this sector has been principally attributed to a number of reasons. The principal reason is that the sector is using outdated or obsolete machinery, lacks skilled labor and application of backward production technology. Based on the report from CSA’s manufacturing business survey, the industry sub-sector of the manufacturing firms in Ethiopia was utilizing only 54.3 percent of their production capacity. In other words, 45.7 percent of the total capacity remained unexploited. Average capacity utilization of the textile, leather, agro-processing and pharmaceutical industries in 2009/10 was at 40 percent, 10 percent, 60 percent, and 30 percent, respectively. Moreover, based on this survey report, a relatively high degree of capacity utilization was observed in the manufacture of wood and products of wood and cork are 99.8 percent while a low level of capacity utilization was recorded in manufacture of furniture 26.93 percent, (AACCSA, 2015).

There are variations in time on the prime reason for lower rates of capacity utilizations. However, lack of raw materials, shortage of demand, threats of new entrants into the sector that leads them to share the existing market, frequent power interruption, and water supply are seems to be the main and more persistent reasons for under capacity utilization. Moreover, according to AACCSA (2015) report, about 62% of manufacturing firms reported that they are not operating at full capacity mainly due to lack of market demand. Added to this, electricity and water were quoted as a reason by 13.9 percent of the manufacturing firms. However, there are several new entrants into a
manufacturing sector, for example, from industries like food and beverage, textile, chemical and other non-metals creating a misallocation of scarce resources, which could have been used in other potential areas.

1.2.3. Access to Raw Materials and Technology Utilization
Higher reliance on imported raw materials and semi-processed good has remained the recognizing highlight of the Ethiopian manufacturing segment. The fundamental purposes behind greater dependence on imported raw materials were inaccessibility of these materials in the nearby market and absence of adequate domestic supply. Insufficient and lower quality of imported raw materials and technologies, alongside the low level of specialized labor skills, are the major problems facing the sector. A study by Central Statistical Agency (CSA) shows that manufacturing firms associate their lower level of capacity utilization with the inadequate and poor quality of the raw material they use. This number accounts for more than half of the firms operating in the sector. This requires a coordinated effort both by the government and different partners to look for ways and method for upgrading availability local and assembly of raw materials thereby minimizing the outflow of foreign currency for importing the raw materials. Ethiopia is pursuing the strategy of industrialization through labor-intensive technological advancements. However, the system of production become capital intensive than labor intensive.

1.2.4. Investment Incentives Schemes
Though the government gives a due consideration to all types of manufacturing industries while articulating a development plan, the actual performances of these firms are unsatisfactory implying a scrutiny for further adjustments for the sector's growth problems. Accordingly, there is a provision of attractive incentive packages from the government side to motivate investors to invest in the manufacturing sector. AACCSA(2015)\(^1\) has included the lists of incentives available to investors under the Investment Proclamation number 768/2012 that has listed duty draw-back, voucher, bonded export factory manufacturing warehouse and bonded input supply schemes as important tools to promote
manufacturing and export. There are also duty-free imports of raw materials and machinery, equipment for manufacturers that are included in the Ethiopian tax law. Nevertheless, a significant size of investment has not been flowing into the sector as expected. The reason can be traced back to other alternative business sectors with smaller payback periods where investors are inclined to invest in.

1.2.5. Employment

Employment generation is a key factor in the promotion of the manufacturing industry. Transformation towards industrialization entails increased share of employment, value added, and export earnings of the manufacturing sector in the economy. The government of Ethiopia has classified manufacturing sector among the key productive sectors of the economy that are identified under Growth and Transformation Plan I (2010-2015). The sector can boost economic growth and development because of its massive potential for creating wealth, generating employment opportunities and mitigating poverty. Though there are some deviations on the reports of different studies (e.g., AACCUSA, 2015\(^1\) & Amare and Raju, 2015\(^2\)), the manufacturing sector employs about 173 thousand people in the year 2012/2013 making an important contribution to the Ethiopian economy resulting in an annual average employment growth rate of 11.48% during 2008-2012 compared to 14.15% of output growth (Amare and Raju, 2015\(^2\)). However, as compared to the total population of Ethiopia the contribution is pretty insignificant to praise this sector.

1.2.6. Ownership Structure and Sources of Finance

The scale of manufacturing industries varies by ownership structure. Public owned manufacturing industries are mainly large scale while privately owned are mostly medium scale. Hence, most manufacturing industries are under the control of either the government or distinct forms of the private actor (individuals, groups, and institutions).

Amid the Imperial administration prior to 1974 private ownership was prevailing (most of the organizations being owned by foreign nationals either completely or partly as joint ventures) in the manufacturing sectors. The part of the
administration was constrained at the time as it is owned (either completely or as a shareholder) a little extent of the assembling firms (Befekadu et. al., 2000)\(^4\). During the period of the Dergue administration (1974–1991), the manufacturing sector got to be under full control of the legislature as an aftereffect of the communist belief system the administration pursued. Therefore, the legislature nationalized all exclusive large and medium scale manufacturing commercial enterprises, denied responsibility for firms in a few segments (especially in large scale producing), forced a roof on a capital venture on others, and established different tenets and directions that debilitated private interest in the manufacturing area (MEDaC, 1999)\(^15\). These had incredibly compelled the improvement of the manufacturing division amid that period.

After the current government comes into power in 1991, it lifted the confinements (most likely not all) levied by its forerunner and took different change measures. Due to privatization policy in Ethiopia most state-owned firms are transferred to private ownership in the form of shareholders. The proportion of public (state owned) sector has extremely contracted to leave the position for the private ownership thereby leaving the dominant position they held to the private sectors in economic activity. For example, privatization of state-owned commercial ventures and public undertakings adjustment program, which restrict public possession, support extension of the private area, and improve effectiveness and intensity (ICC, 2004)\(^10\).

Ethiopian manufacturing sector estimated to run with a total value of fixed capital assets to reach 40 billion birr in 2012/2013. The new investment in this sector in fixed capital for the same fiscal year worth about 3.7 billion where investment in the food and beverage industries was taking the lion’s share of about 1.6 billion birr. Annual expenditures for wage and salary also reached about 10 billion Birr in the same year. For these and other related purposes, domestic banks are the major sources of finance for most projects in Ethiopian manufacturing industries.
Moreover, AACCSA (2015)\(^1\) has interviewed 270 respondents and their response revealed that majority of the respondents reported that domestic banks are their main financier followed by own saving, foreign investment/partners, and domestic capital market.

1.3. Need of the Study

Currently, there are a number of researches conducted in the area of business strategies that deals with identifying the effects of different variables on the performance of any given business organizations. Those studies, either separately or collectively, have been dealing with how to enhance and/or influence the performance of firms by focusing on different strategies. The emphasis of those studies can take the form of analyzing the relationship or the impact of market orientation with/on company’s performance (Kohli and Jaworski, 1993\(^11\); Slater and Narver, 2000\(^18\); Subramanian and Gopalakrishna, 2001\(^19\)); innovation or technology orientation and company performance and/or entrepreneurial orientation and company performance (Gatignon and Xuereb, 1997\(^8\); Zhou et al., 2005\(^a\); Talke et al., 2011\(^20\)). They have included one or two of the firm’s environment either as a moderator or by controlling for the effect of extraneous variables.

However, these studies did not identify the joint effect of the variables of strategic orientation on companies’ performance, where strategic orientation is a composite effect of market orientation, innovation orientation, and entrepreneurial orientation; and their effects on the companies’ performance by controlling for the organizational variables. The controlling variables could be firm’s age (years of operation) and the size of the firm in terms of the numbers of employees in the organization.

Moreover, the studies were conducted in the developed nation and those with higher incomes that may need to have some limitations to conclude whether the same result could happen in developing nations across the globe. So, by considering these two issues, that is, the link between strategic orientation as
described by three variables and performance of the firm, and the context of the researches that have been done, the current research will hope to fill the gap with the help of the following research objectives.

1.4. **Objective of the Study**

The purpose of this study is to investigate the impact of strategic orientation which is defined as a combination of market orientation; entrepreneurial orientation and technology/innovation orientation on business performance with particular consideration of Large Scale Manufacturing Firms of Ethiopia.

More specifically, the study has the following objectives while investigating the impact of strategic orientation on business performance.

- To examine the impact of market orientation on business performance;
- To examine the impact of entrepreneurial orientation on business performance;
- To investigate the impact of innovation orientation on business performance;
- To examine the interrelationship among the constructs of strategic orientations;
- To test the overall fit of the model using a structural equation modeling.

1.5. **Methods**

The data was collected from a sample of 400 respondents out of which 310 responses were found to be valid. The sample size determination has followed the formula developed by Cochran's (1977)\(^6\) and the suggestion by (Bartlett, Kotrlik, and Higgins, 2001)\(^3\). The population under consideration is those large-scale manufacturing firms currently operating in Ethiopia that are in the radius of 100 km from the capital of Addis Ababa. The classification is based on CSA of Ethiopia (2012)\(^5\).
The data analysis method employed in the current research was inferential statistics. The purpose of the study was identifying the impact of strategic orientation on the company's performance. In this case, the researcher has utilized SPSS 20.0 along with AMOS 21.0 SEM modeling (structural equation modeling) to know the impacts of each independent variable on the dependent variable while the interferences of other variables are controlled. Thus, the independent variables (market orientation, entrepreneurial orientation, and innovation orientation) which are assumed to have positive impacts on the dependent variable (company performance) have been analyzed. The model also controls for the influence of firm age and firm size. Moreover, correlation analysis was undertaken in order to know the interrelationship among the independent variables. The model is developed in line with the work of (Han, Kim, and Srivastava 1998; Jaworski and Kohli, 1993; Merlo and Auh, 2009; Wiklund and Shepherd, 2003) though the current study uses SEM modeling. Detail is found in chapter Four.

1.6. Thesis Organization

The following chapter contains an extensive review literature relating to strategic orientations that are, market orientation, entrepreneurial orientation, and innovation orientation, and finally business performance. The third chapter deals with conceptual model and hypothesis development. The fourth chapter provides a detailed explanation of the methods used to perform the research. Chapter 5, 6, 7 and 8 deals with the details related to the analysis of the data obtained from the study. Finally, the last chapter concludes with a summary of findings and discussion of future research opportunities.
Chapter References