



**RISK TAKING AND FIRM PERFORMANCE AMONG FAMILY OWNED ENTERPRISES IN NAIROBI COUNTY**

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**Abstract**

Majority of the multinational corporations started as Family Owned Enterprises. Currently, the SMFEs sector in Kenya contributes over 70% of the country's GDP. This is in spite of the many issues surrounding this vital sector including low performance as compared to non family enterprises, high mortality rate especially after the founder exits, and lack of finances among others. The study seeks to establish the effect of risk taking and the performance of small and medium family owned enterprises performance in Kenya. Psychological / Trait Entrepreneurship theory and McClelland Motivation theory were the theoretical framework for this study. Descriptive and exploratory research designs were adopted. The study population was the manufacturing family owned enterprises registered by Kenya Association of Manufacturers based in Nairobi City County. The respondents were the Founders, C.E.Os, Directors and Managers of the firms. Data was collected using a questionnaire and the quantitative data was analysed by calculating the response rate with descriptive statistics such as mean, median, statistical deviation and proportion using Statistical Packages for Social Scientists (SPSS) version 21 and Microsoft Excel. Inferential data analysis was carried out by the use of factor analysis and correlation analysis to determine the strength and the direction of the relationship between the dependent and the independent variables. A regression model was fitted and hypothesis testing carried out using multiple regression analysis and standard F tests and t-tests. The qualitative data was analysed using content analysis. Microsoft Excel was used to analyse the frequencies of the emerging themes. Data was presented in form of graphs, tables and pie chart among others. Results of the study revealed positive and significant relationship between risk taking and family owned enterprises performance.

**Key Words:** Risk Taking, Family Owned Enterprises, Firm Performance

## INTRODUCTION

Family enterprises dominate the economic environment of majority of the nations in the world (Kuratko and Richard, 2004; Heck and Stafford, 2001). The enterprises constitute between 80 and 98% of all businesses in the world's free economies, generate 49-50% of the GDP in the U.S. and more than 75% in most other countries. In African countries, the sector accounts for about 90% of all enterprises and over 80% of new jobs in any given country (Kiraka et al, 2013). This means that the enterprises must engage in entrepreneurial activities/ entrepreneurial orientation in order to enhance their performance especially in today's competitive markets.

Entrepreneurial Orientation (Eo) refers to the specific organisational-level behaviour to perform risk-taking, self-directed activities, engaged in innovation and react proactively and aggressively to outperform the competitors in the marketplace (Lumpkin and Dess, 1996). According to Rauch, Wiklund *et al.*, (2009) "EO represents the policies and practices that provide a basis for entrepreneurial decisions and actions" that is, how the firm acts entrepreneurially. Previous studies showed that EO is a key ingredient for organisational success and has been found to lead to higher performance (Zahra and Covin, 1995, Wiklund and Shepherd, 2005). Lumpkin and Dess (1996) also suggested that EO is source of competitive advantage. Firms that possess higher levels of EO will perform better than those with lower level of EO (Lyon *et al.*, 2000; Rauch *et al.*, 2009). EO was conceived by Miller (1983) whereby he argued that it's composed of innovativeness, proactiveness and risk taking dimensions. An enterprise is perceived to be innovative if it has the capability to support since conception the creation of new products and services till their introduction in the market. It should also be able to come up with novel solutions to the challenges its encountering as well as new administrative techniques and technologies for performing its functions, (Knight, 1997). Proactiveness ensures that the enterprise will have the capability to pursue opportunities and rivalries with others in

anticipation there are chances of new demand on specific firm products and services (Lumpkin and Dess, 1996; Lumpkin and Dess, 2000; Rauch 2009). On the other hand an enterprise with risk taking behaviour makes daring decisions to venture into the unknown borrowing heavily and committing significant resources to projects in uncertain environments motivated by the prospects for better and high returns (Rauch *et.al.*, 2009).

According to the Kenya National Bureau of Statistics (2011), 3 out of 5 SMFEs fail within the first few months after the retirement/death of the first generation entrepreneurs or in the first 3 years of establishment. The increased competition exerted on the firms translates that the small and medium family enterprises must adopt an entrepreneurial culture i.e be more innovative, proactive and risk taking as well as formulate successful competitive strategies that will bring about actual changes in the environment leading to high firm performance (Malburg,2000).The study focuses on the effect of risk taking on the performance of small and medium family owned manufacturing enterprises that are registered by the Kenya Association of Manufacturers in Nairobi.

## THEORETICAL DEVELOPMENT AND LITERATURE REVIEW

### Psychological/Trait Entrepreneurship Theory

According to this theory, the psychological makeup of an individual determines most of his behaviour towards entrepreneurial activities. The psychological traits include need for high achievement, risk taking, foresight, aggressiveness, proactiveness and creativity. Others include high level of intelligence, decisiveness, good judgement and alertness to environmental changes. Lumpkin and Dess (1996) argues that there is a link between psychological traits and entrepreneurship. People with a certain set of psychological traits might have a tendency to portray some inclination towards entrepreneurship. Coon (2004) defines personality traits as "stable qualities that a person shows in most situations." Therefore according to the trait theorists, there are enduring inborn qualities of an individual that naturally makes him an

entrepreneur. Bwisa (2011) also argues that entrepreneurship is all about an individual. The difference is usually the attitude (internal) and the ability to judge and forecast on the situation at hand in order to become a successful entrepreneur. Prior research studies have identified high need for achievement, tolerance for ambiguity, locus of control and risk taking as important in successful entrepreneurs, (Ahmed, 1985; Begley and Boyd, 1987).

Entrepreneurs are also known to be opportunity driven, innovative and creative, show high levels of management skills, optimistic, committed, and persevering and thrive on competitive desire to win and excel. They are dissatisfied with the status quo, are transformational, dynamic, visionary, people of integrity and they use failure as a springboard to greater heights. The personality trait model is still unsupported by research evidence thus we can only look at an individual's behaviours and conclude that one has the inborn qualities of becoming an entrepreneur. This theory is relevant to this study since the founders of family owned enterprises must have inborn traits which have enabled them to start their own ventures and sustain them through generations in spite of the economic turbulences and other challenges they have experienced in the past.

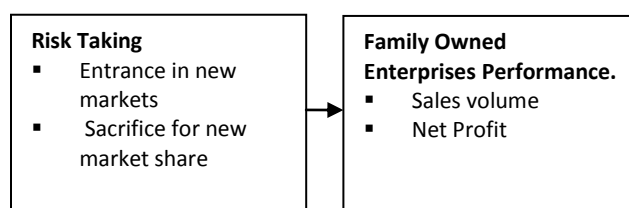
### McClelland Theory

McClelland Theory also known as Acquired Needs Theory argues that, human beings have 3 types of needs at any given time. These are the need for achievement (need to get success with one's own effort), need for power (dominate or influence others) and need for affiliation (maintaining friendly relations with others). Entrepreneurs are driven by this need to achieve and excel, (MacClelland, 1961) While there is no research evidence to support personality traits, there is evidence for the relationship between achievement, motivation and entrepreneurship (Johnson, 2009).

Risk-taking and innovativeness need for achievement, and tolerance for ambiguity has a positive and significant influence on entrepreneurial inclination (Mohar, Singh and Kishore, 2007). However, locus of control has a negative influence on entrepreneurial inclination. The locus of control

is said also to be highly correlated with variables such as risk taking, need for achievement, and tolerance for ambiguity. Further evidence suggests that some entrepreneurs are risk averse to some extent (Brockhaus, 2008). These individuals prefer risks and challenges of venturing to the security of a stable income. The founders of family owned enterprises usually possess an entrepreneurial spirit which drives them to start enterprises and they wish the enterprises to succeed. They will thus go an extra mile to make risky and daring decisions in order to see their businesses performing well and growing thus creating wealth. It is until they achieve their goals that the risk taking propensity lessens.

### Conceptual Framework



**Independent Variables    Dependent Variable**

**Figure 1: Conceptual Framework**

### Risk taking and Firm Performance

An enterprise with risk taking behaviour makes daring decisions to venture into the unknown borrowing heavily and committing significant resources to projects in uncertain environments motivated by the prospects for better and high returns (Rauch et.al. 2009). As a dimension of entrepreneurial orientation, risk taking indicates how far an enterprise processes' involves and or ignores risks ( McMullen and Sherpherd, 2006). Risk-taking has for a long time been associated with good SME performance (Bears, 1982). Entrepreneurs are known to engage in calculated and moderate business risks which in the end lead to high performance (Brockhaus, 1980; Otieno, Bwisa and Kihoro, 2012) in comparison to those that assume extremely high or extremely low risks. Research has in the recent past shown that entrepreneurs take more risks compared to non-entrepreneurs since they face a less structured and a more unpredictable set of possibilities ( Bears,

1892; Oscar, 2013). Lumpkin and Dess (2006) identify venturing into the unknown as a definition for risk taking which leads to great firm performance. It is that will to commit huge resources to a project whose costs and failure rates are high (Keh et al 2006, Baker and Sinkula, 2009). On the other hand, it provides the enterprises with the foundation to grow and venture into new products without worrying much about the outcomes (Lumpkin and Dess, 2006). According to Leko-Simic and Horvat, 2006, 2013 risk taking is a personal trait. The top management of a firm decides whether to take the risk or not. This is mostly determined by the risk perception and propensity of the firm. The higher the risk propensity, the lower the anxiety over risk taking and vice versa. The study will measure risk taking by looking at a firm's entrance in new markets and the sacrifices made for the new market share.

## RESEARCH METHODOLOGY

The study adopted cross sectional survey research design. The study population was the registered family owned small and medium manufacturing enterprises by Kenya Association of Manufacturers (KAM 2015) located in Nairobi City County. Non probability convenience sampling procedure was used as it is an effective way of obtaining a large number of completed questionnaires (Zikmund 2005). To select 201 SMFEs simple random sampling was used. Primary data was collected using questionnaires whereby a total of 201 questionnaires were given to the C.E.Os, founders, directors and managers of the enterprises as they were more conversant with the operations in the enterprises. Out of the 201 questionnaires administered, 196 were filled and returned, which represents 97.5% response rate. This response rate is considered very satisfactory to make conclusions for the study. Mugenda and Mugenda (2007) observed that a 50% response rate is adequate, 60% is good while 70% response rate is very good. The questionnaire was used to measure risk taking and firm performance. The questionnaire used a five point likert scale whereby the founders, C.E.Os,

directors and managers had to indicate to which extent the items represented level of innovativeness in the firms. 1= strongly disagree, 2= disagree, 3=neutral, 4=agree and 5= strongly agree. Firm performance was measured by asking the founders/owners, directors, C.E.Os and managers to indicate their sales volume for the last five years and also the net profit of the enterprises for the last five years. The quantitative data was analyzed by calculating response rate with descriptive statistics such as mean, median, standard deviation and proportions using Statistical Package for Social Sciences (SPSS) version 21 and Microsoft Excel. Inferential data analysis was carried out by the use of factor analysis and correlation analysis to determine the strength and the direction of the relationship between the dependent variable and the independent variables. Regression model was fitted and hypothesis testing carried using multiple regression analysis and standard F tests and t tests.

## RESEARCH FINDINGS AND DISCUSSION

The study sought to determine the effect of risk taking on the performance of manufacturing small and medium family owned enterprises. To achieve this objective, primary data was analyzed using mean, standard deviation, frequency and percentage. Results in Table 1 reveal that majority (mean =3.7, Standard deviation= 1.2) agreed that their firm has a strong inclination for low risk projects (with normal and certain rates of return). Secondly, majority 30.1% agreed and 21.4% strongly agreed that, their management does not hesitate to take loans for new project ventures. Thirdly, majority agreed (mean = 4.2, standard deviation = 1.4) that their firm has strong inclination towards projects with high rates of return. In addition, 56.1% strongly agreed that their firm does not shy away from funding new methods and processes even if they have not been tested in the market and may be risky. Finally, 43.4% agreed, 36.7 strongly agreed and 7.7% disagreed that their firms goes to the extent of sacrificing profit to gain market share.



**Table 1: Risk Taking and Performance of Manufacturing Family Owned Enterprises**

	Risk taking n=196											
	M	SD	Sd		D		N		A		SA	
			n	%	n	%	n	%	N	%	n	%
Our firm has a strong inclination for low risk projects (with normal and certain rates of return)	3.7	1.2	12	6.1	27	13.8	12	6.1	96	49	49	25
The firm's management does not hesitate to take loans for new projects ventures	3.8	1.5	47	24	39	19.9	9	4.6	59	30.1	42	21.4
The firm has strong inclination for high risk projects with high rates of return	4.2	1.4	23	11.7	11	5.6	34	17.3	74	37.8	54	27.6
The firm does not shy away from funding new methods and processes even if they have not been tested in the market and could be risky	4.4	0.9	1	0.5	11	5.6	8	4.1	66	33.7	110	56.1
Our firm goes to the extent of sacrificing profit to gain market share	4.1	1.0	3	1.5	15	7.7	21	10.7	85	43.4	72	36.7

**\*M-Mean SD – Standard deviation, n-Frequency, %-Percentage Sd- Strongly disagree, D- Disagree, N-Neutral, A-Agree, SA-Strongly agree**

42.9% argued that risk taking influenced performance of manufacturing small and medium family owned enterprises to a great extent; this was followed by 29.1% who perceived it to have a very great extent. In contrast 2.6% perceived it to had a very low extent. From the findings, it was deduced that small and medium family owned enterprises ought to take higher levels of risk in order to enhance their performance.

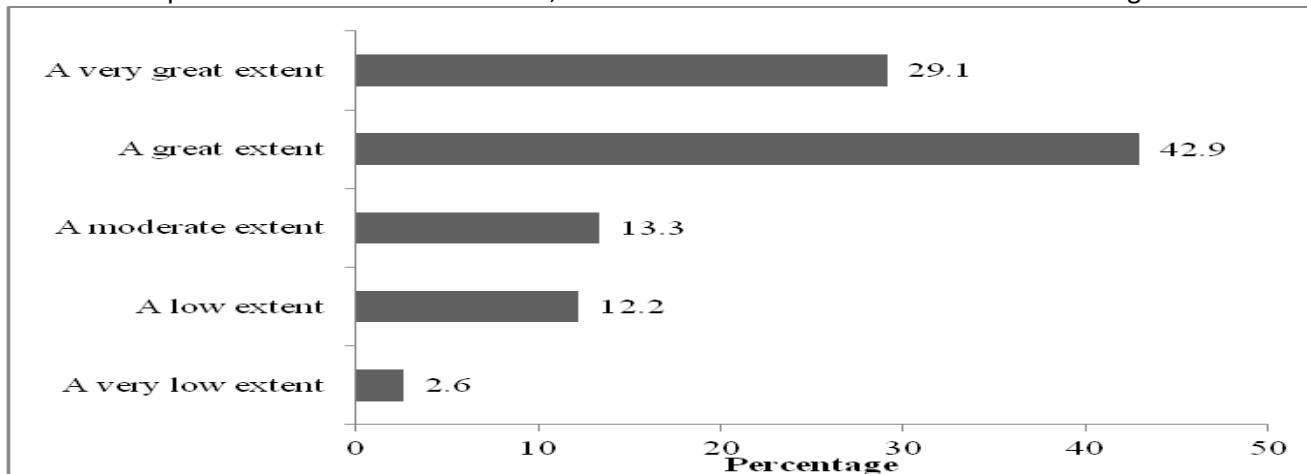
Ali and Abdel (2014); Verhees, Kloplic and Kuipers (2008) revealed a positive and significant relationship between risk taking and firm performance. Risk taking enabled firms to realize a higher growth and long term profitability in

comparison to those firms that avoided taking risks (Abimbisimbwe & Ahabo, 2013). Wambugu (2015) also showed that risk taking positively contributes to firm success. On the other hand, Wiklund (2010) found that family firms do take risks but at a smaller scale as compared to non family firms and that risk taking is negatively related to firm performance. This concurs with a study by Kiprotich (2015), that risk taking has no significant effect on SME performance.

There is a belief that entrepreneurs are risk takers and that family owned enterprises are risk averse. The underlying fact is that, they do take calculated risks based on the risk return concept. Osborne

(1995) reported that entrepreneurs are able to discern the risk levels that they can manage. Entrepreneurial firms take calculated risks; however, they should put in place effective risk management strategies so as to avoid business failure (Cadiuex, 2007). Ansong, (2013) study on risk management argues that risk taking enables the firm to expand its horizon. However, risk

management and uncertainty are important entrepreneurial traits. Kyrgidou and Hughes (2009), cited that risk acceptance is an important factor in strategic entrepreneurship. Opportunity recognition and creation involves risk taking, (Ireland et.al 2003). As a result, SMFEs must not evade risk taking but instead should act entrepreneurially and take moderate risk in order to enlarge their horizons.



**Figure 1 Risk Taking and Performance of Manufacturing Family Owned Enterprises**

**Test for Significance of Risk Taking and Performance of Manufacturing Family Owned Enterprise**

Null hypotheses: H<sub>01</sub>. Risk taking has no significant effect on performance of manufacturing family owned enterprises in Nairobi County.

Alternative hypotheses: H<sub>11</sub>. Risk taking has significant effect on performance of manufacturing family owned enterprises in Nairobi County.

Results in Table 2 showed that 69.5% of the variation in performance of manufacturing family owned enterprise could be explained by risk taking while the remaining percentage could be accounted for by other factors excluded in the model.

**Table 2: Risk Taking and Performance of Manufacturing Family Owned Enterprise Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.834a	0.695	0.694	0.553259	1.884

a. Predictors: (Constant), Risk Taking

b. Dependent Variable: Performance of manufacturing family owned enterprise

The analysis of variance results in Table 3 showed that there was a significant relationship between risk taking and firm performance.

**Table 3 Risk Taking and Performance of Manufacturing Family Owned Enterprise ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	135.617	1	135.617	443.056	.000a
	Residual	59.383	194	0.306		
<b>Total</b>		<b>195</b>	<b>195</b>			

a. Predictors: (Constant), Risk Taking

b. Dependent Variable: Performance of manufacturing family owned enterprise

There was a positive and significant relationship between risk taking and performance of manufacturing family owned enterprise ( $\beta = 0.834$ ,  $p$  value  $< 0.05$ ). This implied that there was a positive and significant relationship between risk taking and performance of manufacturing family owned enterprises.

Motivation to earn attractive returns had been the quest as to why many entrepreneurs engaged in risk taking behaviors that if executed as planned would result in high returns; otherwise it would be a disaster in waiting. A wise investor would only undertake calculated and tolerable level of risk to remain on the safe side (Brockhaus, 1980). The results of the study had shown risk taking has a significant and strong positive association with performance of family owned enterprises. These results agree with Ali and Abdel's (2014) study that

found risk taking and business performance has a significant and positive linkage.

Wiklund's (2010) study that compared family owned and non-family owned Swedish enterprises discovered that the difference between their performances was mainly determined by the risk taking dimension. Performance of family owned businesses differed in that they tend to take fewer risks as they perceive a higher level of risk to be detrimental in case the worst happens. Unlike their counterparts, non-family owned enterprises consider risk taking as a positive move depending on the returns expected whenever there is a change in level of risk. Contrary to this study findings, an explanatory study of SMEs performance in the Nakuru County by Kiprotich et al., (2015) revealed that risk taking behaviour is insignificant even though there exist a moderate positive effect on SMEs performance.

**Table 4: Risk Taking and Performance of Manufacturing Family Owned Enterprise Regression Coefficient**

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	T	Sig.
1 (Constant)	1.22E-16	0.04		0.00	1
Risk Taking	0.834	0.04	0.834	21.049	0.00

a. Dependent Variable: Performance of manufacturing family owned enterprise

## CONCLUSIONS AND RECOMMENDATIONS

The objective of the study sought to determine the effect of risk taking on performance of manufacturing family owned enterprise among family owned enterprises in Nairobi County. Descriptive analysis revealed that majority agreed since mean ranged between 3.5 to 4, that risk taking had an influence on the performance of family owned enterprises in Nairobi County. Correlation analysis revealed a positive and significant relationship between risk taking and performance of manufacturing family owned enterprise ( $\rho = 0.834$ ,  $p$  value  $< 0.05$ ). Similarly, regression analysis showed a positive and significant relationship between risk taking and firm performance. Moreover, the risk taking accounted for 69.5% of the variation in firm performance.

Although, risk taking enhances manufacturing company's performance, there is need to have an elaborate risk management procedure. Manufacturing companies must evaluate the risk levels they are willing to tolerate, treatment procedures, transfer options available and termination approaches available. The management must evaluate the risk communication strategies in place. The risk assessment procedure ought to be able to assess the risk status before mitigation, evaluate the risk after the application of a given mitigation, the possibilities of the risk recurrence in future and how it can be mitigated. The management should be preparing a risk register detailing the previous risk and how they were mitigated and future opportunities which can be explored by manufacturing companies.



### Suggestions For Further Study

The study had a number of limitations that need to be addressed in future studies. First the study only focused on the manufacturing small and medium

family enterprises in Nairobi County, Kenya. Future research can focus on non family enterprises in other areas in the country.

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