Firm reputation and financial performance of SMEs: the Ghanaian perspective

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Abstract: Our paper examines the effects of firm reputation on financial performance of small and medium scale enterprises (SMEs) in Ghana by controlling for firm specific variables such as firm age, firm size, owner/manager's age, leverage and access to capital. It contributes to our knowledge on how firm reputation enhances the financial performance of SMEs in developing economies. We employed primary data from 423 SMEs within the Accra Metropolis. Standard regression analysis was used to analyse the data. We documented a significant positive association between firm reputation and firm performance, denoting that high corporate reputation by an SME enhances its performance. In addition, with the exception of firm size, there was a significant positive relationship between all the control variables and financial performance of SMEs.

Keywords: firm reputation; financial performance; small and medium scale enterprises; SMEs; firm reputation of SMEs; financial performance of SMEs; access to capital by SMEs; firm image; organisational identity; corporate reputation and performance; developing economies; Ghana.

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1 Introduction

The need for business organisations to stay competitive in a globalised economy promotes the essence of identifying the drivers of sustainable competitive advantages. This quest now transcends searching for tangible resources that can enhance corporate worth to include the field of intangible assets such as firm reputation. Many scholars, consultants, and practitioners (Barnett et al., 2006) have been working on the development of tools to measure these intangibles and their relevance to business organisations (Bontis et al., 2007).

The interests in firm reputation studies have increased significantly in recent years for several reasons. The foremost being that organisations have realised that a strong reputation can assist them align with the demands of the marketplace, attract investment, motivate employees and serve as a means to differentiate their products and services. In addition, firm reputation is now widely recognised as an effective strategic resource and a means to achieve competitive advantage (Schmidt, 1995). Corollary to this, an in-depth research underpinned by the resource-based view (RBV) perspective is imperative. This paper narrows on examining an aspect of firm reputation known as corporate identity and its influence on financial performance.

Corporate identity represents the controllable subset of associations which encompasses the organisation’s notion of self, aiming to express relevance, uniqueness, and distinctiveness (Brown et al., 2006; Simões et al., 2005). Certain characteristics of an effective corporate identity include a reputation for high quality goods and services, a robust financial performance, a harmonious workplace environment, and a reputation for socially and environmentally responsible behaviour (Einwiller and Will, 2002).

With the emergence of globalisation and integration of markets where both large corporations and small and medium scale enterprises (SMEs) are seeking new ways to achieve competitive advantage; corporate identity, image, and reputation strategies have the potential to make a useful and ongoing contribution to both the competitiveness and financial performance of SMEs. Several scholars have proved that the concept of corporate identity is applicable to every organisation, regardless of size and location (Abimbola and Kocak, 2007; Abimbola and Vallaster, 2007; Balmer, 2012).

Both developed and developing economies have generally come to acknowledge the SME sector as the key driving force for growth due to the employment opportunities it creates (Hu, 2010). In emerging economies, it is estimated that SMEs employ about 22% of the adult population (Daniels and Ngwira, 1993; Daniel and Fisseha, 1992; Fisseha, 1991; Fisseha and McPherson, 1991). In Morocco, about 93% of industrial enterprises are SMEs, contributing about 38% of total production, 30% of exports and 33% of investment. In South Africa, about 91% of the formal enterprises are SMEs, accounting for about 52–57% of GDP. In Ghana, this sector is a significant source of employment

creation and national revenue through taxation (Kayanula and Quartey, 2000; Keskin, 2006; Abor and Quartey, 2010). Abor and Quartey (2010) posit that SMEs contribute about 75% to Ghana's GDP and account for 85% of employment in the manufacturing sector.

More importantly within the context of development, a growth in this sector has a relationship with poverty alleviation (Gebremariam et al., 2004). Hence, empirical investigations directed towards unearthing the success factors in the SME sector is relevant. This study seeks to contribute to literature by examining the effects of firm reputation on financial performance of SMEs. Different from previous studies (for instance, Lee and Roh, 2012; Eberl and Schwaiger, 2005; Inglis et al., 2006), this research examines the influence of reputation on firm performance of SMEs from a developing economy, Ghana.

Our choice of Ghana is informed. The development of strong corporate reputation has become a focal point in recent years in Ghana. This calls for Ghanaian firms to be more proactive in social responsibility issues. Even though issues on corporate reputation are not new in Ghana, it is still not well developed among Ghanaian SMEs as compared to advanced countries. This is as a result of low level of awareness and conservative thinking of SME owners and shareholders. This has therefore, created a gap for more research into corporate reputation activities in Ghana to put forward updated insight on the ongoing discussion between firm reputation and financial performance. We believe that the results of this study will interest SME managers in Ghana who engage in behaviour resulting in or maintaining strong corporate reputation mechanisms, Ghanaian financial analysts who conduct research on corporate reputation and financial performance of firms and investors who want to increase their confidence in investing in firms with strong reputation.

By controlling for age of firm, owner-manager age, firm size, leverage and access to finance, our results confirm that SMEs with better reputation attain higher financial performance. In addition, apart from firm size, our study documents a significant positive relationship between all the control variables and financial performance of Ghanaian SMEs. The paper is organised as follows: the next section presents review literature related to this study. Ensuing is the methodology. Finally, methodology, analyses and conclusions are presented respectively.

2 Literature review

Existing marketing literature is not clear on the difference between the terms 'image' and 'reputation'. Some authors have used these concepts interchangeably while investigating the issue of company reputation (e.g., Dowling, 1993). However, Grunig (1993) opined that the concept of 'image' consists of several important constructs, including perception, cognition, attitude and schema, which identify symbolic objectives for public relations. More specifically, Bromley (2000, p.241) viewed 'image' as "the way an organisation presents itself to its publics, especially visually".

The import of these explanations is that 'image' focuses on external stakeholders and the creation of some form of perception among observers. In addition, 'image' creation is directed at 'products and services' rather than an overall assessment of the organisation or firm. In a similar vein, Fombrun and van Riel (1997) supports the assertion that

research into 'image' had primarily focused on understanding how consumers use cues to create 'pictures in their heads' about predominantly products and services rather than an overall corporate reputation. This is different from the concept of 'identity', which is known to be internally focused and connected to executives' sense making and self-perception of the firm (Fombrun and van Riel, 1997).

As with concepts of reputation and image, a substantial amount of research has been devoted to defining identity. For instance, Fombrun's (1996, p.36) defined corporate identity as "the set of values and principles employees and managers associate with the company". Similarly, Bromley (2000) viewed corporate identity from the perspective of internal stakeholders on their conceptualisation of the firm from within, or, put another way, how key members of the organisation see their firm.

The corporate reputation model developed by Hatch and Schultz's (1997) emphasises the important role top management plays in the formulation of corporate identity (Balmer, 1998). Bernstein (1986, p.8) argues that "managers should be concerned with image not because they want to manufacture it but because they need to discern how organizational signals are being received and decoded and how these perceptions square with the management's own perception of the organization". Fombrun and Shanley (1990) advanced that it is at the executive level that management of organisations attempts to influence a firm's reputation by communicating the firm's salient advantages to various stakeholders.

This suggests that senior executives are equally in a unique position to send signals (whether good or bad) via various mediums of communication about the state of the reputation of their firms to both internal and external stakeholders based on their perception. Hence, the actions and statements of senior executives simultaneously affect the formulation, definition and development of both identity and image (Hatch and Schultz, 1997), and therefore corporate reputation (Fombrun and van Riel, 1997; Chun, 2005). This study acknowledges the central role that owner/managers of SMEs play in the process of formulating firm reputation and utilises their self-assessment of the state of the reputation of their firms to deepen the understanding of the nexus between organisational identity and financial performance.

Many authors have acknowledged that firm reputation encompasses aspects of both external (image) and internal (identity) perceptions of the firm (Dowling, 1993; Fombrun and Rindova, 1996; Post and Griffin, 1997). In their analysis of earlier definitional statements of corporate reputation, both Chun (2005) and Barnett et al. (2006) observed the relatively high occurrence of the terms 'image' and 'identity', connected with the concept of 'corporate reputation'. This paper focuses on unearthing how the 'identity' (internal) component of firm reputation influences financial performance of SMEs.

3 Theoretical framework

The concept of corporate reputation has been a major concern of researchers from the 1950s onwards. There is a consensus among scholars and practitioners alike that the way in which the public perceives a company influences the corporate success (Fombrun, 1996). Findings from the Walker's (2010) systematic review of corporate reputation literature show that the most commonly referred theories include institutional theory, signalling theory and RBV.

Walker (2010) advanced that institutional theory is most applicable in studies interested in the pre-action or action stage of a firm's reputational development. The thrust of the theory is used to examine how firms gain legitimacy and cultural support within their institutional contexts to build their reputations (Deephouse and Carter, 2005; Rao, 1994; Staw and Epstein, 2000). To be seen as legitimate, firms must take actions within their institutional contexts.

With respect to the signalling theory, Walker (2010) argues that this theory focuses on strategic signals (images) sent by firms and subsequent stakeholder impressions, hence, signalling theory is often applied at the *action* stage of reputational construction. The theory includes building, maintaining, and defending a reputation based on projected organisational images (Walker, 2010). The essence of the theory is to explain how the strategic choices of firms represent signals, which are then used by stakeholders to form impressions of the firms (Basdeo et al., 2006; Fombrun and Shanley, 1990; Turban and Greening, 1997). Unlike institutional theory or RBV, social performance was identified as an antecedent to corporate reputation with signalling theory (Fombrun and Shanley, 1990; Turban and Greening, 1997).

Finally, Walker (2010) indicated that RBV is the main theory that focuses on the outcome of a strong reputation; RBV is often applied at a *post-action* stage. Specifically, it examines how reputation is a valuable and rare resource that leads to a sustained competitive advantage. Hence, this theory is the lead theory in this paper and it is thus examined further in the subsequent section.

4 The resource-based view

The RBV considers firm reputation as a valuable and rare resource that gives rise to sustained competitive advantage. Corporate reputation emerges as an intangible asset which differentiates a firm from others and attracts customers to repurchase and willingly pay higher price for products (Eberl and Schwaiger, 2005; Roberts and Dowling, 2002). High reputation serves as a cost saver for firms. Employees desire to work for firms with excellent reputations and the firms are able to recruit and retain a competent work force with less contracting and monitoring costs (Boyd et al., 2010; Bergh et al., 2010; Roberts and Dowling, 2002).

A significant strand of research on corporate reputation has seen reputations as critical organisational assets (Flanagan and O'Shaughnessy, 2005; Roberts and Dowling, 2002; Hall, 1992, 1993) and has explored the relationship between firms' reputations and their financial performance (Deephouse, 1997; Sanchez and Sotorrio, 2007; Roberts and Dowling, 2002). Some of the outcomes of reputation identified using RBV include higher profits (Roberts and Dowling, 2002), charging a price premium, and reducing costs (Deephouse, 2000). Existing empirical research has largely supported a positive reputation-performance relationship (e.g., Roberts and Dowling, 2002; Sabate and Puente, 2003).

5 Empirical review

Good corporate governance promotes the quality of corporate reputation which in turn enhances the financial performance of the organisations involved (Salloum et al., 2011; Iwu-Egwuonwu, 2011). Iwu-Egwuonwu (2011) postulates that even accounting literature supports the notion that corporate reputation brings about enormous amount of wealth, usually summed up in what is called goodwill, whereas some conventional wisdom affirm that the reputation which firms earn for themselves do cause sustainable profits. In addition, the resource-based theory of the firm contends that the reputation of a firm can lead to a competitive advantage as it signals to stakeholders about the attractiveness of the firm, who are then more willing to contract with it (Deephouse, 2000).

Roberts (2003) also advanced that a good reputation improves the value of everything an organisation does while a bad one devalues products and services and acts as a magnet that attracts further scorn. Empirically, a number of studies have established a positive relationship between firm reputation and performance. For instance, Chung et al. (1999) investigated how a company's reputation influences the value of its stock. Their study revealed that firms that are highly ranked in reputation outperformed firms that were ranked low on reputation.

Brammer and Millington (2005) established a positive relationship between a firm's reputation and financial performance among UK companies. Tan (2007) found corporate reputation to be positively correlated with both superior total sales and superior earnings quality in Chinese public companies. Finally, Ghose et al. (2009) studied how different dimensions of a firm's reputations affect its pricing ability and concluded that while positive reputation helps corporate performance, a negative reputation hurts more than a positive one helps.

Specifically on corporate identity, many authors have asserted that it has the potential to enable organisations to secure numerous benefits in the market place (Ackerman, 1984; Balmer and Gray, 2000; Melewar and Navalekar, 2002; Simões et al., 2005) such as identification with the stakeholders, favourable image and reputation, improved sales, investment, and so on. On the other hand, the absence of appropriate corporate identity leads to many disadvantages such as poor organisation's sales and earnings, low employee morale, inability to attract talented people, expansion capital and general financial performance (Ackerman, 1984; Chajet, 1989). In other words, corporate identity just like corporate reputation leads to competitive advantage. Competitive advantage leads to superior financial performance outcomes (Day and Wensley, 1988). Hence, this paper hypothesised a positive relationship between corporate identity and financial performance of SMEs.

6 Financial performance

Extant literature has identified four main approaches to measuring performance within the theoretical frameworks of firm performance. These are the goal approach, system resource approach, stakeholder approach, and competitive value approach (Chong, 2008). Among these, the goal approach is most commonly used in SME studies due to its simplicity, understandability and being internally focused (Chong, 2008). Information is easily accessible by the owner-managers for the evaluation process (Pfeffer and Salancik,

1978). For the remaining three approaches, they are deemed challenging to the owner-managers of SMEs (Quinn and Rohrbaugh, 1981).

The goal approach directs the owner-managers of SMEs to focus their attentions on financial measures (Chong, 2008). Financial measures such as revenues and profitability, indicating an organisation's current state of performance may not necessarily serve as a useful guide or prediction for the organisation's long-term survival (Birley and Westhead, 1994). However, by accumulating such revenues and profits, these may become a useful pool of resources for future growth and expansion that can assist the firm to push over its survival threshold (Barney, 2001) and pursue its growth strategy (Salloum et al., 2016; Haber and Reichel, 2005).

Chong (2008) contend that profitability, even in the short run, is a significant factor in the organisation's ability to attain its long term goals such as increased market share, brand names and reputations. The author further emphasised that low profitability for a specific period, however, may not necessarily mean deficiency on the part of owner-managers. This may be due to large investments in long term projects that may lead to future growth or for meeting the internal or external demands on the organisation.

This implies that while the goal approach stresses on achieving predetermined targets, it is necessary for the owner-managers to consider the time frame of completing the process (Haber and Reichel, 2005). Richard et al. (2008) also indicated that the measurement of performance requires an understanding of the time series properties relating organisational activity to performance. Based on the above discussion, this study concentrates on the financial performance of SMEs and relies on profit growth as the measure of performance.

7 Control variables and financial performance

The study controlled for age of firm, owner-manager age, firm size, leverage and access to finance. In regards to age of firm and its influence on financial performance of firms, extant studies have established a positive relation between them (Ericson and Pakes, 1995; Stinchcombe, 1965). However, other studies have found a negative relationship between age of firm and financial performance of firms (Agarwal and Gort, 1996, 2002; Hannan and Freeman, 1984). With respect to owner-managers' age and financial performance, empirical evidence highlights a positive relationship between them. Kristiansen et al. (2003), Birley and Norburn (1987) and Smith and Amoako-Adu (1999) documented a positive significant relationship between owner-managers' age and financial performance of firms. Further, firm size has been proved to have influence on firm performance. On one hand, larger firms enjoy higher negotiation power over their clients and suppliers (Serrasqueiro and Nunes, 2008). In the light of this, they are able to secure goods from their suppliers at affordable prices which give them the ability to dictate the direction of market prices. On the other hand, it is in contention that small size family businesses are characterised with low agency costs. Thus, such firms are composed of few number of workforce with few varieties of objectives held by these individuals (Dyer, 2006). Moreover, studies on the impact of leverage on financial performance have been mixed. Ward and Prince (2006) stipulated that a profitable business will experience a higher return on equity as borrowing or debt financing increases, since such financing is able to earn at higher rate than it is paying for its

borrowed funds. On the contrary, Myers (1984) argues that successful companies do not need to place much dependence on the external funding since they rely on internal reserves. Finally, access to credit has also been cited by several studies both as a major determinant of the performance of SMEs in both developed and developing economies (Abor and Adjasi, 2007; Kashyap et al., 1996; Nakiyingi, 2010; Dube et al., 2011).

8 Methodology

Since the purpose of the study is to establish the relationship between firm reputation and financial performance of SMEs, the correlation research design was employed. The target population comprised all SMEs within the Accra Metropolis. The accessible population was defined as all manufacturing and trading SMEs which had registered with the National Board for Small-Scale Industries (NBSSI) and the Association of Ghana Industries (AGI) in the Accra Metropolis as at September 2013. The total number of SMEs recorded in the NBSSI's and AGI's registers by location in the Metropolis was 2,083 as shown in Table 1. The population was classified using the 11 sub-metropolis and the size of the firms. Following Krejcie and Morgan (1970), to ensure a 5% margin error, 254 medium sized and 302 small-sized firms were randomly selected from 750 medium-sized and 1,400 small-sized firms respectively (see Table 2).

Table 1 Distribution of population by sub-metropolis and firm size

Sub-metropolis	*Medium-sized*	*Small-sized*	*Total population*
Ashiedu Keteke	73	137	210
Osu Klottey	70	127	197
Ayawaso East	23	48	71
Ayawaso Central	15	30	45
Ayawaso West	57	102	159
Ablekuma South	91	152	243
Ablekuma Central	22	59	81
Ablekuma North	85	150	235
Okai Koi North	92	179	271
Okai Koi South	121	232	353
La	78	140	218
Total	727	1,356	2,083

Source: Survey data (2014)

Table 2 Distribution of the sample by sub-metropolis and firm size

Sub-metropolis	*Medium-sized*	*Small-sized*	*Total*
Ashiedu Keteke	26	31	57
Osu Klottey	24	28	52
Ayawaso East	8	11	19
Ayawaso Central	5	7	12

Source: Survey data (2014)

Table 2 Distribution of the sample by sub-metropolis and firm size (continued)

Sub-metropolis	*Medium-sized*	*Small-sized*	*Total*
Ayawaso West	20	23	43
Ablekuma South	32	34	66
Ablekuma Central	8	13	21
Ablekuma North	30	33	63
Okai Koi North	32	39	71
Okai Koi South	42	52	94
La	27	31	58
Total	254	302	556

Source: Survey data (2014)

9 Measurement of variables

A questionnaire was developed in reflection of the extant literature in the area. It was also peer reviewed by academic colleagues who had undergone the process of survey development and analysis previously. This was carried out to ensure clarity and that no irrelevant questions were included in the survey. Following Sweeney (2009), Man (2011) and Burton and Goldsby (2009) the study adopted the subjective approach of measuring financial performance. The rationale for this is that the use of scales is a better alternative to measure SME performance than to use actual figures due to the unwillingness of SME owner/managers to disclose these sensitive figures.

Given that the classical approaches to measuring corporate reputation such as the use of Fortune's America's Most Admired Companies or Britain's Most Admired Companies data are neither available nor applicable to the SME sector, firm reputation was measured based on the items employed by Sweeney (2009). Sweeney (2009) originally intended to use 15 variables to gain insight into firm's reputation as held by customers, employees and other firms within the same industry. Factor analysis technique was then used to reduce this number. Finally, after conducting multicollinearity test, some variables were further eliminated and firm reputation was measured based on ratings other firms in the same sector would award the firm on the basis of quality of products and services, quality of staff, environmental responsibility, community responsibility and quality of management. The variables controlled for included owner/manager characteristics (i.e., the entrepreneur's age) and firm characteristics such as firm age and size, access to capital and leverage.

10 Analysis

This section examines the effects of firm reputation on the financial performance of SMEs. The regression results from Table 3 indicate that the R^2 is 0.514 and the adjusted R^2 is 0.507. This means that 51% of the variation in the dependent variable, financial performance, can be explained by the explanatory variables of firm reputation, access to capital, owner/manager's age, leverage, firm size and age. The remaining 49% can be

explained by variables other than the variables used in the model. The F-statistics confirms that there is a true relationship between the dependent variable (financial performance) and the independent variables.

The coefficient (0.273) of the firm reputation variable, organisational identity, is also significant ($p = 0.000$) and positive. This means that an increase in firm reputation will lead to an increase in financial performance. A positive constant term is also reported which is consistent with economic theory. The hypothesis sought to establish whether a statistically significant relationship exists between organisational identity and financial performance. With respect to organisational identity, the results showed a t-statistics of 3.727. This confirms that there is a significant positive relationship between firm reputation and financial performance. Therefore, the hypothesis is accepted at 1% level of significance.

Table 3 Multiple regression analysis results for firm reputation and financial performance of SMEs

Variables	*Estimated coefficient*	*Standard errors*	*t-values*	*Sig.*
Constant term	0.789	0.325	2.430	0.016
Organisational identity	0.273	0.073	3.727	0.000***
Access to capital	0.556	0.029	19.023	0.000***
Leverage	0.090	0.028	3.260	0.000***
Firm size	–0.008	0.003	–2.654	0.008***
Owner/manager's age	–0.004	0.005	–0.867	0.387
Firm age	–0.003	0.004	–0.734	0.464
R	0.717			
R^2	0.514			
Adjusted R^2	0.507			
F-statistic	73.255			

Notes: [a]Predictors: constant, organisational identity, access to capital, leverage, owner/manager's age, firm size and age.
[b]Dependent variable: financial performance (profit growth)
***Significant at 0.01 level.

11 Discussions

The purpose of this paper was to examine the effects of firm reputation on financial performance. We focused on SMEs in Ghana. Our analyses support the RBV that firm reputation is resource that brings competitive advantage to an organisation as it signals to stakeholders about the attractiveness of the firm, who are then more willing to contract with it (Deephouse, 2000). It appears good reputation improves the value of everything an organisation does, while a bad one devalues products and services and deters both customers and investors from dealing with an organisation (Roberts, 2003). This finding is consistent with Brammer and Millington (2005) who established a positive relationship between a firm's reputation and financial performance.

Specifically, on corporate identity, many authors (Ackerman, 1984; Balmer and Gray, 2000; Melewar and Navalekar, 2002; Simões et al., 2005) have asserted that it has the potential to enable organisations improve their financial performance because it can enhance sales, investment, and so on of an organisation. On the other hand, the absence of appropriate corporate identity leads to many disadvantages such as poor organisation's sales and earnings, low employee morale, inability to attract talented people, expansion capital and general financial performance (Ackerman, 1984; Chajet, 1989).

Finally, the control variables of access to capital and leverage exhibited a significant positive relationship with financial performance of SMEs. Concerning firm size and financial performance, the results established a significant negative relationship between them. In addition, owner-managers' age and firm age did not have any significant relationship with financial performance of SMEs.

12 Conclusions and recommendation

This study sought to examine the effects of firm reputation on the financial performance of SMEs in the Accra Metropolis. Stratified sampling procedure was used to select the sample from each of the 11 sub-metropolis and a total of 500 owners/managers of SMEs were surveyed using a questionnaire. Primary and secondary data sources were used for this study. Standard regression analysis was also used to test the hypothesis and to meet the objectives of the study. The key findings as they related to the objective of the study are summarised as follows: Firstly, there was a significant positive relationship between firm reputation and the financial performance of SMEs. Secondly, there was a significant positive relationship between all the control variables (except firm size) and financial performance of SMEs.

Based on these findings and conclusions, the following recommendations are made: firstly, SMEs' owner/managers should invest in improving their entrepreneurial competencies; developing quality products and services; engaging in community and environmental improvement initiatives to bolster their image. Secondly owner/manager should relate with their internal stakeholders well since their positive assessment of firms can result in financial gains.

13 Limitation and directions for future research

Our study is inherently characterised by two limitations. Extant literature showed that a comprehensive measurement of firm reputation should elicit the assessment of both internal and external stakeholders, however, this study only concentrated on the evaluation of owner-managers of the SMEs (organisational identity). We could not also address the influence of corporate governance on firm reputation, hence, future studies could address these concerns.

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