Thriving amid Uncertainty: How Enterprise Risk Management Shapes the Confluence of Business Strategy and Financial Performance of Micro, Small and Medium Enterprises in Ghana

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Abstract. The paper research examines the moderating role of enterprise risk management on the effect of business strategy on the financial performance of micro, small and medium-sized enterprises in Ghana. The study utilized a quantitative research design, wherein survey data was gathered from a sample of 356 micro, small and medium-sized enterprises. The research examined the effects of implementing a differentiation strategy, cost leadership strategy, and product/service diversification on the financial performance of an organization. Furthermore, the study investigated the moderating influence of enterprise risk management on these associations. The findings established that the implementation of a differentiation strategy and diversification of products or services can lead to a positive effect on financial performance. Conversely, adopting a cost leadership strategy may have an adverse impact. Furthermore,the research illustrates that the proficient execution of enterprise risk management practices amplifies fiscal efficacy and mediates thecorrelation between corporate strategy and financial performance. The implications of these findings are significant for managers of micro, small and medium-sized enterprises, policymakers, and researchers. Specifically, the findings underscore the importance of strategic decision-making and risk management as critical factors in achieving financial success.

Keywords: Enterprise risk management, business strategy, financial performance, micro, small and medium enterprises.

1 Introduction

Micro, Micro, Small and Medium Enterprises (MSMEs) face numerous challenges in achieving sustainable financial performance in the current global business landscape [1]. Market fluctuations, consumer shifts, and regulatory structures exacerbate these difficulties. To effectively manage uncertainties, MSMEs must strategically align their business strategies and risk management [2]. The integration of enterprise risk management (ERM) practices has gained a growing

R. Hurriyati et al. (eds.), *Proceedings of the 8th Global Conference on Business, Management, and Entrepreneurship (GCBME 2023)*,
Advances in Economics, Business and Management Research 288,
https://doi.org/10.2991/978-94-6463-443-3_138

attention as a viable approach that can impact the nexus between business strategy and financial performance [3].

Empirical research has demonstrated that well-defined business strategies, such as differentiation, cost leadership, and product/service diversification, can positively affect financial performance by providing a competitive advantage, cost savings, and the ability to explore new market prospects [4]. Efficient ERM practices are crucial in reducing potential risks, safeguarding financial assets, and safeguarding operational resilience [5]. Successful differentiation strategies enable MSMEs to distinguish themselves from competitors, attract dedicated customers, and demand higher prices for their products or services [6]. Implementing efficient ERM strategies is essential in safeguarding investments made towards differentiation and maintaining a competitive edge. Cost leadership strategies can aid MSMEs in attaining operational efficiency, providing competitive pricing, and augmenting profit margins [7].

Effective implementation of ERM is essential for managing risks and uncertainties that arise from diversification [8]. By incorporating these strategies in conjunction with effective risk management protocols, MSMEs can enhance their financial performance and optimally navigate the unpredictable nature of the contemporary business environment. However, there needs to be more empirical research, particularly within the context of MSMEs in Ghana, which mainly focuses on larger corporations [8].

Theoretically, there needs to be more comprehensive research investigating the combined influence of business strategy and ERM on the financial performance of MSMEs in Ghana [9]. This study addresses this gap by investigating how ERM influences the nexus between various aspects of business strategy and the financial performance of MSMEs in Ghana.

2 Methods

The research utilized a quantitative methodology grounded in a positivist philosophical perspective and implemented a descriptive survey design [10]. The population of the study is 2.1 million MSMEs in Ghana, out of which 900,000 were documented in the National Board for Small-Scale Industries (NBSSI) database. The study targeted MSMEs that were registered in the NBSSI database. A sample of 385 MSMEs was chosen using stratified and simple random sampling techniques. To examine the nexus between business strategy and financial performance of MSMEs and the moderating role of ERM, Ordinary Least Square (OLS) regression techniques were employed. The empirical model is stated as follows:

$$ROA = \beta_0 + \beta_1 DIS + \beta_2 CLS + \beta_3 PDS + \beta_4 M + \beta_5 FA + \beta_6 FS + \varepsilon \qquad (1)$$

Where ROA is the dependent variable, the independent variables are DIS, CLS and PDS as defined earlier, M is the moderating variable, which denotes infarctions between ERM and the independent variables (*ERM*DIS, ERM*CLS, ERM*PDS*), the study controls for firm age and firm size to account for confounding factors *β0* is constant, and β_1 - β_6 are the coefficients and **ε** represents the error term.

3 Results and Discussion

The reliability analysis results indicate that all constructs' internal consistency is deemed acceptable. Besides the Table, the descriptive statistics offer a comprehensive summary of the measures of central tendency, variability, and distributional characteristics of the variables under investigation in the research.

Table 1. Descriptive Statistics

	N	Min	Max	Mean	SD	Skewness		Kurtosis	
						Stat	Std. Err	Stat	Std. Err
ROA	356	0.23	1.42	0.70	0.33	0.52	0.13	-0.12	0.26
DIS	356	1.00	7.00	5.37	1.28	-1.77	0.13	1.12	0.26
CLS	356	1.00	7.00	5.47	1.05	-1.09	0.13	0.86	0.26
PDS	356	1.00	7.00	5.53	1.18	-1.95	0.13	0.25	0.26
EMR	356	1.00	7.00	5.53	1.18	-0.95	0.13	0.45	0.26
FA	356	1.00	23.0	7.87	5.02	1.07	0.13	0.32	0.26
FS	356	6.78	7.67	7.15	0.25	0.79	0.13	-0.93	0.26

ROA: return on assets, ERM: enterprise risk management, DIS: differentiation Strategy, CLS: cost leadership strategy, PDS: product/service diversification, FA: firm age, FS: firm size.

3.1 Regression analysis

Table 2 presents the OLS findings, the diagnostic test, and the model fit, showing that the OLS regression model is reliable. The discussion of the findings is done on two levels. The first discussion was done without interaction effects, and the second was done with interaction effects using conditional and unconditional effects. For example, the net effect of the differentiation strategy is 3.296[(0.596× 5.53)] +(0.633)], where the conditional effect of the interaction differentiation strategy and enterprise risk management is 0.596, the unconditional effect of differentiation strategy is 0.633 and the mean of the moderating variable enterprise risk management is 5.53.

Table 2. Business strategy, enterprise risk management and financial performance

	1	**2**	**3**
Constant	-3.856**	-3.735***	-3.729**
	(0.000)	(0.000)	(0.000)
DIS	0.633***		
	(0.000)		
CLS		-0.145***	
		(0.000)	
PDS			0.858***
			(0.000)
ERM	0.696***	1.681***	0.794***

	(0.000)	(0.000)	(0.000)
ERM×DIS	0.596***		
	(0.000)		
ERM×CLS		1.381***	
		(0.000)	
ERM×PDS			-0.101*
			(0.023)
FA	0.016***	0.015***	5.059***
	(0.000)	(0.000)	(0.000)
FS	0.858***	0.599***	0.145***
	(0.000)	(0.000)	(0.000)
Net Effects	3.296	7.492	0.299
Observation	356	356	356
R^2	0.230	0.229	0.223
Adjusted R^2	0.219	0.219	0.221
F-Statistics	20.94***	20.85***	26.12***

***,**,* P<0.001,P<0.05, P<0.01 respectively. *ERM: enterprise risk management, DIS: differentiation Strategy, CLS: cost leadership strategy, PDS: product/service diversification, FA: firm age, FS: firm size. The mean value of ERM is 5.53.*

The following results were established: The regression analysis, as presented in Table 2, reveals that the coefficient for the differentiation strategy is 0.633, which indicates a statistically significant and positive association with financial performance (p-value = 0.000). This observation implies that MSMEs implementing a differentiation strategy are more likely to achieve superior financial outcomes. The coefficient of cost leadership strategy exhibits a statistically significant negative correlation with financial performance, as evidenced by its value of -0.145 and a p-value of 0.000. This suggests that MSMEs that prioritize the cost leadership strategy may encounter inferior financial performance in comparison to those that do not prioritize this particular strategy. Furthermore, the coefficient of diversification of products or services is 0.858, denoting a favourable and statistically noteworthy correlation with financial performance (p-value = 0.000). This finding implies that MSMEs undertaking product or service diversions are more likely to attain superior financial outcomes.

The study reveals a positive correlation between implementing a differentiation strategy and the financial performance of MSMEs, in line with previous research. The establishment of a singular identity through the provision of exclusive products or services has a positive impact on financial performance. This research provides empirical evidence in favour of the proposition that a positive and statistically significant correlation exists between implementing a differentiation strategy and the financial performance of MSMEs.

The study also supports the relationship between cost leadership strategies and enhanced financial performance in MSMEs. Implementing cost-reduction initiatives, streamlined operations, and competitive pricing tactics can lead to higher profit margins and improved financial performance. The findings of this study support the proposition that there exists a significant and positive correlation between the implementation of a cost leadership strategy and the financial performance of MSMEs. Diversification of products or services has a notable and favourable impact on the financial performance of MSMEs. Studies conducted by [11,12] have shown that MSMEs that adopt diversification strategies tend to experience improved financial performance by acquiring additional revenue streams and capitalizing on market opportunities. The study validates the favourable impact of this approach on the financial performance of MSMEs.

The regression analysis reveals a coefficient of enterprise risk management, which denotes a significant and positive correlation with financial performance. This implies that MSMEs that adeptly execute enterprise risk management practices are inclined to exhibit superior financial performance. The interplay between enterprise risk management and various business strategies yields significant insights. The correlation between enterprise risk management and differentiation strategy yields a favourable outcome on financial performance, suggesting that enterprise risk management enhances the advantageous outcomes of differentiation strategy concerning financial performance. The results suggest that the impact of differentiation and cost leadership strategies on financial performance is more significant than product/service diversification. The study also indicates that the existence of enterprise risk management and the attributes of the organizations, such as their age and size, have a favourable impact on their financial performance.

The study's findings align with prior studies on the moderating function of enterprise risk management. According to [13] and [14], adopting proficient enterprise risk management practices can enhance the favourable impact of corporate strategies on financial performance. The study validates the moderating function of enterprise risk management in augmenting the financial consequences linked with these strategies.

4 Conclusions

The study investigates the relationship between business strategy, enterprise risk management, and financial performance in Ghanaian MSMEs. It reveals that differentiation strategies and diversifying product/service portfolios positively impact MSMEs' financial performance, increasing sales revenues, profitability, and market share. Cost leadership strategies negatively affect financial performance, suggesting that MSMEs prioritizing cost minimization and competitive pricing may struggle to achieve sustainable financial performance. The study also highlights the role of enterprise risk management in the correlation between corporate strategy and fiscal outcomes. Effective implementation of risk management methodologies can reduce potential risks associated with selected business strategies, ultimately improving financial outcomes. The findings have significant implications for managers, policymakers and scholars, emphasizing the need for efficient enterprise risk management practices to mitigate risks and improve financial outcomes. However, the study has limitations, including its focus on Ghanaian MSMEs, cross-sectional data limitations, and the lack of investigation into alternative moderating factors.

5 References

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