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## Relationship between Knowledge Management and Organizational Performance: A Test on SMEs in Malaysia

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### Abstract

Generally, small and medium enterprises (SMEs) play a crucial role in supporting the nation's economy. Nevertheless, Malaysian SMEs have not developed their full potential. Therefore, it is essential for the entrepreneurs to search for and shift towards better strategies to become more successful. In the present turbulent environments, knowledge has been viewed as a major strategic competitive resource. Given the importance of knowledge, entrepreneurs are encouraged to develop their capabilities to manage knowledge which will move them to become more competitive and innovative. Extensive research is available in the knowledge management literature investigating the process of knowledge management as a composite construct; nonetheless little research has been done to examine the independent effects of the individual dimensions of knowledge management process. In particular, little empirical evidence has been found to determine the implementation of knowledge management practices in the context of developing countries and small business. This study aimed to fill the perceived gaps by investigating the relationship between knowledge management process capabilities and organizational performance in the context of Malaysian SMEs. Knowledge management process capabilities were conceptualized as four dimensional constructs: knowledge acquisition, knowledge conversion, knowledge application, and knowledge protection while organizational performance were divided into two dimensions namely, non-financial performance and financial performance. This paper anticipates that the four knowledge management process capabilities are important antecedents of organizational performance, which have in turn a positive relationship with both non-financial performance and financial performance of SMEs. The findings of this study will provide insights to entrepreneurs and help them to identify and develop effective strategies towards enhancing their overall performance.

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## 1. Introduction

Globalization has created new challenges for businesses to remain competitive. Nowadays, businesses have to face high competition between businesses and run the risk of losing their customers easily because most of them have difficulty in understanding and responding to rapid changing market trends. The growing importance role of knowledge has motivated businesses to move on from other management practices to knowledge management (Cho & Korte, 2014; Tubigi & Alshawi, 2015).

Knowledge management is regarded as the capability to manage knowledge such as acquiring knowledge from either internal or external organization, converting it into new strategy or idea, applying and protecting it (Gold, Malhotra, & Segars, 2001). By adding the concept of knowledge management capability into operations, abundance of information of customers can be captured and this can further assist the service industry to improve on their overall service quality and faster service response time (Runar Edvardsson & Kristjan Oskarsson, 2011).

Investigating on the relationship between knowledge management capability and organizational performance is essential as the findings can help the businesses to further explore the consequences of knowledge management (Liu & Deng, 2015). Besides, there is a lack of study that investigates the relationship between knowledge management capability and non-financial performance (Cho & Korte, 2014). Moreover, the findings of previous researches are still inconclusive with regards to the knowledge management capability-performance link which, some researchers found that not every dimensions of knowledge management capability is significantly correlated to performance (Mills & Smith, 2011). This study aims to bridge the gaps by examining the relationship between individual dimensions of knowledge management capabilities and a more specified organizational performance that includes non-financial performance indicators among SMEs in the service sector of Malaysia.

## 2. Literature review

### 2.1. Knowledge management capabilities

Knowledge is perceived as an important success factor for achieving and sustaining competitive advantage of organizations (Lee & Lan, 2011; Liu & Deng, 2015). Notwithstanding, knowledge can be easily obsolete and useless if without proper management within the organization (Karimi & Javanmard, 2014). Therefore, it is very crucial for an organization to develop a series of processes or procedures in order to better manage their knowledge assets (Ou Yang, 2014).

Following an extensive review of prior research, model of knowledge management capabilities developed by Gold et al. (2001) has been adopted in this study, whereby knowledge management is described as a process made up of knowledge acquisition, knowledge conversion, knowledge application, and knowledge protection.

### 2.2. Organizational performance

Organizational performance reflects the ability of an organization to fulfil its stakeholders' requirements and survive in the market (Griffin, 2003). It also known as the outcome of the actions or activities carried out by the members of organization to measure how well an organization has accomplished its objectives (Ho, 2008; Chung & Lo, 2007).

Previously, organizational performance has been mostly assessed through financial based performance measures. Most widely used financial measures are return on assets (ROA), return on investments (ROI), return on equity (ROE), market share, sales growth, and profitability. Even though these indicators are still the ultimate aim of most organizations' operation, but measuring performance solely on these indicators are no longer adequate to measure competencies that modern organizations are looking for (Gomes, Yasin, & Libsboa, 2004; Kaplan & Norton, 1992).

According to Richard, Devinney, Yip, and Johnson (2009), organizational performance should be viewed as a multidimensional construct. A balance and complete assessment of organization's performance should consist of different performance dimensions (Tangen, 2003) because organizational performance could not take place without

integration of systems, operations, people, customers, partners and management (Jyoti & Sharma, 2012). Moreover, the researcher claimed that non-financial performance measures are more useful on predicting future performance and facilitating the performance of the organizations (Crabtree & DeBusk, 2008). Therefore, it is necessary for organizations to include non-financial performance measures too in order to assess their intangible benefits such as client satisfaction, employee satisfaction, innovation ability, internal business process efficiency, and performance enhancement from intangible assets (Kaplan & Norton, 2001).

For the purpose of this study, the researchers tend to use both non-financial and financial performance indicators to measure organizational performance because they should be viewed as complementary to each other (Kaplan & Noton, 1992; Chow & Van der Stede, 2006; Kihn, 2010).

### 3. Conceptual framework

In line with the extensive review of prior research, a conceptual framework as shown in Figure 1 is constructed to demonstrate the relationships between knowledge management capability and organizational performance. We argue that the four underlying dimensions of knowledge management capability (knowledge acquisition, knowledge conversion, knowledge application, and knowledge protection) have a positive relationship with two aspects of organizational performance, namely, non financial performance and financial performance.

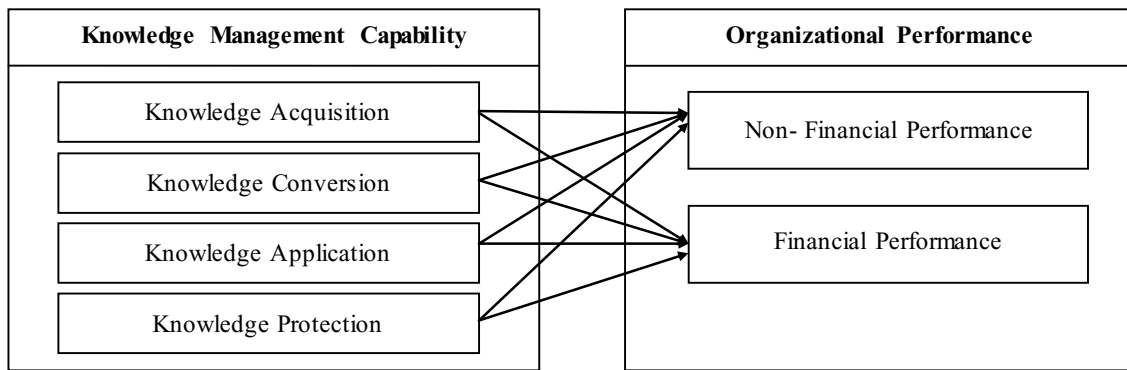


Fig. 1. Conceptual framework.

Knowledge acquisition is expected to have a significant influence on organizational performance. It involves the process of acquiring knowledge from either inside or outside of the organizations (Cho & Korte, 2014). Appropriate acquisition of knowledge increases the stocks of knowledge available to the organization, thereby providing organizations better capability to make timely decisions that are essential to superior organizational performance (Chen, 2004).

Knowledge that is acquired has to be organized, integrated and presented in a more effective way in order to be useful (Reisi, Hoseini, Talebpour, & Nazari, 2013). Knowledge conversion enables organizations to improve their expertise and efficiency by converting acquired knowledge into applicable organizational knowledge, and distributing the knowledge to where it is needed (Bhatt, 2001; Gold et al., 2001; Daud & Yusoff, 2010; Mills & Smith, 2011).

Knowledge application is the process involving the actual use of knowledge for decision making and problem solving (Gold et al., 2001). Besides, knowledge application can help to transform knowledge from being a potential power tool into actual innovations or inventions which can enhance overall performance of organizations (Madhoushi, Sadati, Delavari, Mehdivand, & Mihandost, 2011; Matin, Nakchian, & Kashani, 2013).

Since knowledge is considered as an important source of sustainable competitive advantage for modern business, increasing attention should be paid on protection of knowledge in order to prevent imitation by competitors

(Desouza & Vanapalli, 2005). The use of certain knowledge protection processes such as patents, trademarks, trade secrets or nondisclosure contracts are essential in order to allow knowledge to be secured (Cho & Korte, 2014; Jean, Sinkovics, & Hiebaum, 2014; Roy & Sivakumar, 2011). In view of the above, the following hypotheses are formulated:

- H1: Knowledge acquisition is positively related to non financial performance.
- H2: Knowledge acquisition is positively related to financial performance.
- H3: Knowledge conversion is positively related to non financial performance.
- H4: Knowledge conversion is positively related to financial performance.
- H5: Knowledge application is positively related to non financial performance.
- H6: Knowledge application is positively related to financial performance.
- H7: Knowledge protection is positively related to non financial performance.
- H8: Knowledge protection is positively related to financial performance.

#### **4. Previous research**

A study was conducted by Reisi et al. (2013) to investigate the relationship between individual dimensions of knowledge management process capability and organizational effectiveness among selected sport organizations in Iran. Employing multi-variant regression analysis, the results demonstrated that all dimensions of knowledge management capabilities (knowledge acquisition, knowledge conversion, knowledge application, and knowledge protection) have direct and a significant relationship with organizational effectiveness. They further suggested that knowledge and learning activities are necessary for organizations to improve their effectiveness.

Furthermore, Liu and Deng (2015) found that each dimension of knowledge management capability has a positive effect on business process outsourcing performance. Knowledge application was found to be the most significant dimension correlated to business process outsourcing performance. They concluded that knowledge management capability is an effective tool to enhance performance as it provides organizations with competitive advantages that their competitors difficult of imitate.

In addition, Kimaiyo, Kapkiyai and Sang (2015) mentioned that all processes of knowledge management are very important for enhancing firm performance. Firms are suggested to apply knowledge management continuously by creating new knowledge, converting knowledge into new design or strategy, learning from previous experience, and protect their knowledge in order to achieve better performance.

On the other hand, Mills and Smith (2011) conducted a study in Jamaica to examine the relationship between knowledge management capability and organizational performance. They found that knowledge acquisition, knowledge application, and knowledge protection are positively related to organizational performance, but not knowledge conversion. They argued that the relationship between knowledge management and performance is complex which, each knowledge management process is not necessary directly linked to performance even they are found to be correlated to performance from a composite model.

#### **4. Potential implications**

This study would have theoretical and practical implications for both scholars and practitioners, especially in the domains of marketing and management. From the perspective of scholar, the contradictorily findings of previous studies make further investigations necessary and this study is expected to further enhance the understanding on the relationship between dimensions of knowledge management and organizational performance by testing it in the context of emerging market. Furthermore, this study is expected to have interesting findings to be added to existing body of knowledge regarding the link between knowledge management capability and a more specified organizational performance that includes non-financial performance indicators.

From the perspective of practitioners, the findings of this study may be useful to businesses by determining the most effective knowledge management capability that may enhance their performance.

## 5. Conclusion

The growing importance of knowledge has motivated businesses to adopt knowledge management as an important practice in developing their business strategies. In order to further convince businesses to apply knowledge management, businesses should have a better understanding on the consequences of implementing knowledge management. This study is expected to provide insights to the businesses by demonstrating the empirical evidences of the relationship between knowledge management capabilities and organizational performance.

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