

Democratic organizational culture for SMEs innovation transformation and corporate entrepreneurship

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Abstract. The contribution of the Small and Medium Size Enterprises (SMEs) in every economy is undeniably significant. Still, their existence relies on their leadership's ability to respond to the continuous challenges utilizing best their limited resources. This paper introduces a Democratic Leadership Change Integration Model (DLCIM) that can be used globally to support and institutionalize SMEs' innovation by maximizing their human intellectual capital's effectiveness democratically. Knowledge democratization is a crucial stage in knowledge generation. Its benefits encourage both the employees and the organization to create innovative products and services under ethical management values and principles. The proposed framework helps organizations and SMEs achieve a knowledge-based democratic company-employee relationship. It encapsulates the integration of The Company Democracy Model as the tool and base for innovation, the ADKAR model for change management, and the Self-Determination Theory as a leadership principle.

Keywords: SMEs · Business Transformation · Organizational Culture · Self-Determination · Company Democracy Model · Leadership · Change Management · Knowledge Management · Innovation · Corporate Entrepreneurship · Family Business

1. Introduction

SMEs are known to form the backbone of every economy. They occupy the largest proportion of businesses on a national and global scale and have a critical impact on job formation, GDP, and overall economic development [1]. However, due to their size, operations, and limited financial resources, SMEs are often restricted from effectively accessing and implementing innovation management programs. Reports indicate a dropping rate in the number of innovative SMEs in recent years [2] as innovation activities are reduced [3], [4]. Inadequate innovation adaptation threatens the essential

elements for survival and growth, such as long-term productivity, profitability, and market responsiveness [5]. Thus, most SMEs remain small, under the influence of larger organizations, or die recently after their establishment [6], [7].

Studies indicate that SMEs regard the macro environment as their biggest challenge to innovate [8]. However, evidence shows that external support has become extensively available through the many regulatory frameworks set by public institutions that create SMEs' opportunities to benefit. This proves that governments want SMEs to improve, develop, and grow [9], [10]; however, they must research the SMEs' internal environment and support them in building and maintaining an innovation culture.

Democratizing SMEs' potential is crucial in building the foundation for future innovation explorations. SMEs' leaders can use a tailored framework to promote a democratic innovation culture and operations by focusing on knowledge exploitation and embedment in SMEs through their employees or the society's intellect.

2. Challenges in the SMEs Innovation Culture

Most of the SMEs, besides the startups, belong to the category of family businesses, which restricts the freedom and level of innovativeness, managing intuitively rather than strategically. Such SMEs focus primarily on profit maximization and day-to-day operations. This translates into a lack of long-term organizational goals, development, and implementation strategies that, if present, could ensure higher survival and long-term competitiveness [11].

As family entities, SMEs tend to preserve tradition rather than respond to the need for change. Innovation is treated as a threat to existing products/services rather than an opportunity for further development. It is perceived as a process that requires abundant financial resources and expertise, which SMEs are believed to be lacking [12]. Therefore, there is no understanding and practical application for innovation to be achieved as an added value and a knowledge-sharing collaborative process.

SMEs, and especially the family business, can have many ideas, essential for innovation, from the new generations that succeed the older ones. A successful inter-organizational collaboration can boost the entrepreneurial potential of the firm. However, it requires both generations to align their mentality and vision. Younger members are discouraged by the founding age, which lacks ways to provide the space to think innovatively [13]. This conservative leadership and centralized decision-making disincentivize employees, restricts them within their roles without opportunities or motivation to share constructive feedback or pursue innovation projects [14].

3. Research Methodology, Methods and Results

Academic primary and secondary research based on international literature review, a survey with 100 participants, and 5 interviews with SMEs owners from different industries and sizes of organizations was conducted to understand the level of innovativeness and the cultural elements that SMEs must adopt to innovate and grow. The results were analyzed based on Hofstede's cultural dimensions (Table 1) [15].

Table 1. Research results analyzed with Hofstede's cultural dimensions.

| Cultural Dimension | Non-innovative SMEs | Innovative SMEs |
|--------------------------------|--|---|
| Power Distance | <i>High:</i> (a) Limited sharing of organizational goals, conservative in preserving the already established business forms. (b) Limited collaborative thinking between leaders and selected employees. | <i>Low:</i> (a) Organisational members share the same values and vision. (b) Collaboration and active encouragement for employees and society to communicate ideas. |
| Uncertainty Avoidance | <i>High:</i> (a) Risk and lack of funding discouraged leaders from exploring new spaces and R&D. (b) Innovation perceived as cost-intensive. (c) Fear of failure. (d) Innovation for the family business is regarded as a threat to the reputation of existing products /services. | <i>Low:</i> (a) Lack of funding did not stop innovation. (b) Innovation developed through knowledge management. |
| Masculine vs. Feminine | <i>Moderate:</i> less proactive employees with a focus on security/stability; less equality. | <i>Moderate:</i> a higher level of independence, proactivity, and career development; more equality. |
| Time orientation | <i>Short-term:</i> Unplanned innovation, executed only at times of organizational pressures or incremental changes dictated from the top managers | <i>Long-term:</i> (a) Innovation is part of long-term plans. (b) Innovation is systematically discussed in meetings. |
| Individualism vs. Collectivism | <i>High:</i> No culture of sharing, concentration, and development within existing roles. | <i>Moderate:</i> Autonomy and initiative are encouraged based on reward. |

Hofstede's analysis identified the absence of innovative desire and practices in most firms, showing the correlation between innovation and corporate culture to be distinctive for survival and growth. Most SMEs did not comply with the elements of the innovation culture. They relied on employees with higher education or rank when engaged in innovation, ignoring the rest, losing this way tremendous intellectual capital. Their involvement in entrepreneurial projects was dependent on the availability of financial resources. Contrarily, several SMEs were innovated continuously and improved their products and services despite their limited financial resources. The success element was claimed to be the open mindset of democratic leaders to involve everyone to contribute and experiment on their ideas, some of which emerged into valuable entrepreneurial projects successfully implemented in the firm.

Therefore, innovation is limited by the availability of financial resources and the firm's inability to use its human intellectual capital effectively. The study indicates that knowledge management can be successfully adopted in SMEs despite their limited human resources or financial status. People can think creatively if they are given the space to do so [16]. However, it will be difficult for innovation to be achieved without establishing a strong cultural foundation in such a manners. The adaptation of democratic culture can help SMEs to identify the human resources willing and capable to innovate.

The study acknowledges the nature of the problem as a domino effect (Leadership - Culture - Innovation - Growth) based on which it indicates three central SME needs. The need for: (1) Leadership that can shift SMEs to a more democratic culture which better supports innovation, with knowledge management practices that capture, use, and turn individual knowledge into organizational knowledge; (2) Implementation of a change management strategy for innovation to be planned, applied, and reinforced until it becomes part of the organization. This includes the need to motivate and trigger the desire for contributing knowledge willingly and repeatedly; (3) The creation of a universal framework that will lead to long-term innovation by supporting SMEs' needs. Such a framework shall be a clear path to the democratization of SMEs' internal environment for knowledge creation and utilization.

4. Changing the SMEs Innovation DNA

The SMEs' organizational transformation can be realized through a democratic leadership and culture. Creating this culture requires a strong strategy but also decisive leadership to execute it. Leaders must lead their vision through a clear implementation strategy that fulfills the needs for the transformation to be achieved effectively. Changing SMEs' innovation DNA through leadership can be theoretically presented as a three-step strategic roadmap where the Company Democracy Model (CDM), the Self-Determination Theory (SDT), and the ADKAR change management model are applied. The SDT represents the theoretical change aspirations, the ADKAR demonstrates what needs to change for the firm to facilitate innovation, and the CDM indicates how to achieve these aspirations practically.

The CDM is a knowledge-based democratic culture framework for innovation management. Through the organizational evolutionary spiral method of the CDM, a roadmap is presented to the SMEs for the identification, elicitation, and transformation of data and information into knowledge that is evolved into innovation, competitiveness, and extroversion. As humans are placed at the heart of innovation, their knowledge is welcomed regardless of their social or professional status. Through the CDM, SMEs can create more freedom for thinking and creativity and establish collaborative relationships between leaders, employees, and society [17].

However, for SMEs to maintain an ongoing innovation culture, individuals must be motivated to share knowledge and collaborate. Human beings are subject to intrinsic and extrinsic motivators. They are more prone to reach maximal results when both motivators are present or when the inherent motivation exceeds the extrinsic one [18], [19]. Therefore, the focus is on implementing the Self-Determination Theory to primarily fulfill intrinsic motivation through belongingness, autonomy, and competence. At the same time, individuals pursue the development of their ideas through the CDM. Then, extrinsic motivation is satisfied through a reward scheme based on the participants' contribution at each CDM model level.

Furthermore, the transition from the current to the future state requires a great degree of change that is usually hard to accept as it creates mental barriers for those exposed to it. This transition must repeatedly happen as innovations materialize in the organization. The ADKAR Model, as a Y theory, is the most suitable change model to help individuals understand, embrace, and commit to this change through their

involvement. ADKAR creates the inertia for progressing through every single stage of the process until innovation is embedded in SMEs' DNA [20].

5. The Democratic SME Innovation Transformation (DeSEMIT) Model

The integration of the CDM, STD, and ADKAR compose the Democratic SME Innovation Transformation (DeSMEIT) Model, which creates corporate entrepreneurship within SMEs. When the CDM, STD, and ADKAR are used simultaneously, they form a holistic mechanism where leaders, employees, and society co-exist and co-evolve, reaching their full potential. Practically, evolution follows the six levels of a pyramid structure. Figure 1 presents the integration of the STD and the ADKAR in the CDM 6-level pyramid.

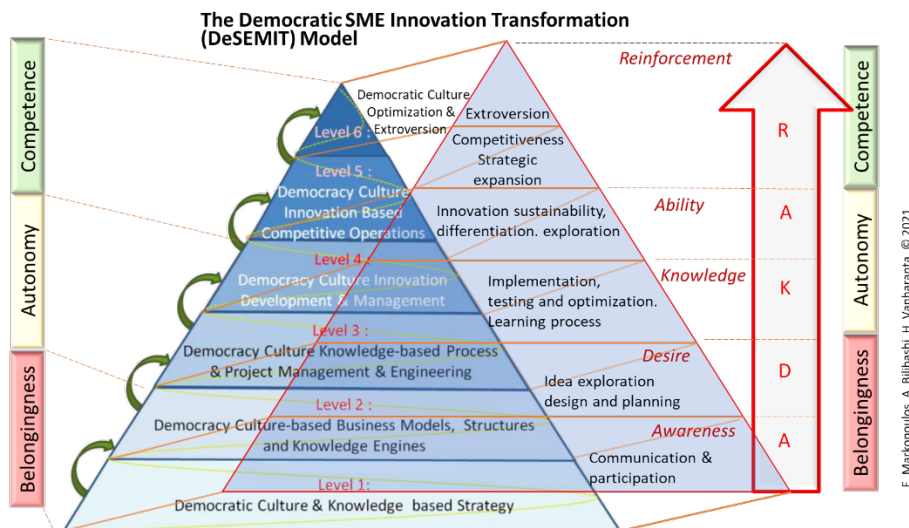


Figure 1. The Democratic SME Innovation Transformation (DeSMEIT) Model.

While progressing through each level, SMEs explore new knowledge spaces and opportunities. Each level is briefly presented:

Level 1 sets the infrastructure for the democratic corporate culture and the change in the SMEs' DNA. The need for knowledge and ideas is communicated, and contribution is required from all employees. Belongingness is achieved gradually as trust and psychological safety is inflicted in the corporate environment, fostering voluntary participation conditions. This first level is related to the Awareness stage (A) of the ADKAR model. Employees are being informed of the existence of the DeSMEIT and are invited to participate.

In level 2, ideas with a potential plan of execution are selected to be developed furthermore. The organization supports the idea holder to enter into a knowledge maturity process. The organizational support ignites the desire to commit to the idea

and work towards proving its value to the organization or the society. The second level is related to the Desire stage (D) of the ADKAR model. As employees receive support to further think and elaborate on their knowledge or ideas, their desire is tested. The ones with strong desire will proceed, while the rest will stop.

Level 3 is the most knowledge-intensive stage. Individuals' experiences change as they learn to work at the small group level, share, develop, and demonstrate their intellectual contributions. Equipped with freedom and autonomy, groups follow their project plans to transform their ideas into prototypes and later into actual products or services offered in the market for use, consumption, and testing. The third level is related to the Knowledge stage (K) of the ADKAR model. Employees are allowed to develop their ideas and test them in the market. This provides practical knowledge on valuating these ideas and what needs to be improved or delivered to sustain a possible success.

In level 4, the best prototype or product is selected by the SMEs' leadership. Further support is given on research, development, and testing to make it part of its innovations. At this level, innovation is achieved. The project and the employee group move to level 5 only if the innovation demonstrates its maturity and proves a strong competitive advantage and market for it. The fourth level is related to the Ability (A) of the ADKAR model. Employees with successful ideas from level 3 must indicate their ability to turn these ideas into innovations that sustain them and the SMEs, long term success, and added value.

In level 5, the innovation becomes part of the SME's competitiveness, strategy, marketing, and communication. It becomes the differentiation element of the SME from other SMEs. The group's competence and the employees are supported, encouraged, and significantly rewarded so that change and innovation can be sustained for a long-time.

Level 6 reveals the highest level of competency achieved by the organization through its employees. In this stage, the firm can run internationally to reach new markets and establish new partnerships that could not have been possible before. This success is also the apex of the self-confidence an employee can get. Being in a SME and being given a chance to lead it with just an idea is an experience that builds character, loyalty, commitment and bonds the employee with the SME. The fifth and sixth levels are related to the Reinforcement stage (R) of the ADKAR model. The competitive advantage gained from the innovation at level 5 and the internationalization opportunities offered at level 6 are used to sustain this success and build on it.

6. The DeSMEIT for Corporate Entrepreneurship in SMEs

The execution of innovation through the DeSMEIT requires extrinsic motivators that do not interfere with the intrinsic ones to recognize employees' contribution. Since every level requires a different amount of energy and effort, the inverse pyramid has been used to assign rewards based on meritocracy. It also represents steps for career progression at the SMEs level and ignites corporate entrepreneurship as a type of business that this term has been excluded. The inverse pyramid (Fig. 2) depicts the minimum rewards, starting at the bottom, and increase as the individual progresses into

the higher stages of knowledge contribution and innovation, similar to the Democratic New Product Development Model [22].

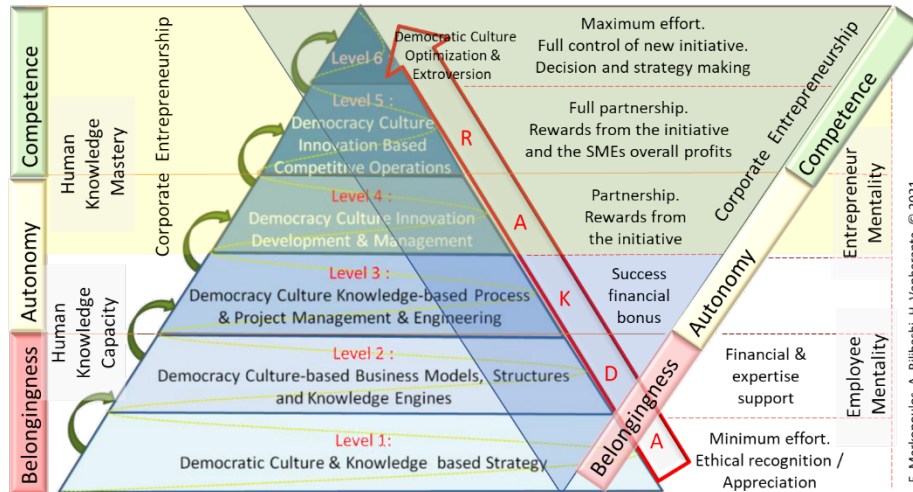


Figure 2. SMEs Corporate Entrepreneurship.

In level 1, the contributors receive an ethical recognition on the knowledge provided or the idea proposed. The reward is minimal as the idea is still hypothetical, and the knowledge is not justified or tested enough. In level 2, the individual increases the efforts and spends more time developing the idea into a project plan. As the attempt remains moderate, the individual receives various compensations reflecting the time and the effort placed. Up to this level, the SME has not made any significant investment other than compensating for the overtime or working time the employees have spent on their knowledge contributions. Level 3 challenges the employees but also the SME.

Given that the idea requires real execution, the SME must invest in developing the knowledge into a product or service. This is a critical stage as SMEs need the courage to make this investment. Moreover, it needs to give practical credit to the employee if the results are successful. This is a stage where the family business type of SMEs step back unless they are confident of the success.

The DeSMEIT levels 4, 5, and 6 apply the corporate entrepreneurship principles where the SME is forced to accept or stop the process. Due to the small number of employees in an SME, successful products and services must be handled by those who had the idea and successfully delivered it. There are no innovation units, groups, or teams in SMEs. Everything operates at the individual or small group level, but the individuals need much stronger incentives to continue achieving level 3. It is the time that the SME shall grant ownership rights or partnership to the employee and secure the commitment and passion needed to move forward. The employee must become the product's or service's leader and function as an entrepreneur within the SME, which now has to operate as a new business unit or entity. The corporate entrepreneurship concept, invented to utilize employees' intellectual capital by turning them into corporate entrepreneurs [22], cannot be applied unless the SME commits to sharing

power and control faster and at earlier stages, unlike the large-scale corporations who can take more time for such decisions.

In this case, **level 4** is achieved when the SME's employee status changes into a partner. The product or service success achieved in level 3 supports the employee financially, motivating him/her to continue the success and create innovation out of it.

The incentives of **level 5** are the absolute freedom the employee gets to utilize and the competitive advantage of the innovation through the SME's communication and commercialization strategy. The employee is supported financially not only from the profits derived from the specific innovation but also from the shares received from the company's overall progress due to the contribution and impact of the innovation in the overall brand name, competitiveness, and success.

Level 6 does not provide any incentives to the employee and the SME other than the international development opportunity if the innovation derived has this potential. The primary motivation lies in the employee's ego, passion, and commitment to go beyond the domestic market and reach blue and international oceans. This is the stage where the roles between the SME and the employee get reversed. It's the employee who supports the growth and future of the SME in markets and regions never seen before.

7. Impact, limitations, and areas of further research.

The DeSMEIT supports SMEs to establish a democratic knowledge-based culture that can lead them into the innovation needed to end a survival marathon and grow into large enterprises that drive industrial change and market competitiveness. The creation of democratic company culture is bound to decrease inequalities in the working environment while increasing internal knowledge flow. Knowledge-driven SMEs generate and create the space needed to achieve specialization. The model can be a game-changer not only from the knowledge wealth that can be made in the developed economies but also in the developing economies where reverse, architectural frugal, and other types of innovation can start from the SMEs.

However, the research conducted has been limited to the SMEs' characteristics, as the region and the sector of operations might differ extensively. Most of the SMEs studied are from the Balkan region and operate in the finance, retail, and hospitality sectors. The number of interviews was conducted only with SMEs leaders, excluding employees' perspectives, which might have been different and more insightful. Furthermore, due to the SMEs' restrictions on investments, the study approaches innovation in general terms from a more conservative staged and incremental process.

The DeSMEIT presented has been developed at a theoretical level and requires further research to document its application in practice. This opens an opportunity for understanding discrepancies that might hinder its execution and uncover any crucial features that can be added to complete the model furthermore according to SMEs situation. The model can also be investigated in relevance to the country, the region, the industry the SME operates in, and the overall geo-entrepreneurial perspective [23]. Further research could be conducted to understand SMEs' ability to move with disruptive and radical innovation strategies, revealing the implications of the adaptation of one or the other.

8. Conclusion

The integration of the CDM, ADKAR, and STD composes the DeSMEIT, a reliable mechanism that allows SMEs to reach competitiveness and extroversion through innovation. It is a step staged approach that evolves based on the SMEs' organizational culture and commitment to invest in human capital. Starting from the first level where new ideas emerge until the last level where the ideas are solidified to deal with internationalization strategies or the creation of new business entities, the model promotes corporate entrepreneurship in a category of businesses that have not been considered possible.

The democratic staged internal knowledge evolution that drives the model is aligned with the organizational change management stages of the ADKAR Model as a complimentary Y-theory approach to discreetly empower and engage SMEs' human resources in knowledge sharing for co-petition among themselves and co-evolution with the company. The self-determination theory has been used in the model as a metric instrument on the effectiveness of the democratized organizational culture, the quality of knowledge produced by the employees, and their commitment to continue their efforts and faith in such initiatives. The model intends to inspire SMEs to explore their human intellectual capital and attempt to discover new opportunities.

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