

## **Mediating effect of strategic orientation on the relationship between dynamic capabilities and competitive advantage of small and medium retail enterprises in Kenya**

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**Abstract:** *According to the Vision 2030, Kenya intends to become a Globally Competitive and Prosperous economy. It aims to transform Kenya into a newly industrializing, “middle-income country providing a high quality life to all its citizens by the year 2030”. Remarkable transformation has seen the entry of large shopping malls examples the Sh450 million shopping mall developed by Oasis Capital having 300 parking spaces, several supermarkets, cinema halls, conference centers and offices plus the coming soon multinational Scandinavian supermarket chain, IKEA, which specializes in furniture. Fierce competition from mass merchandisers, changing demographics and shifting consumer purchasing patterns is threatening the very survival of the local small and medium retailers with statistics already indicating a slow decline in their performance.*

*The strengths of an enterprise are grounded in its resources, capabilities and competencies that helps it competitive advantage based on-superior efficiency, innovation and quality and customer responsiveness. This proposes to examine how strategic orientation mediates dynamic capabilities of sensing, seizing reconfiguring and competitive advantage relationships in small and medium retail enterprises facing dynamic situations especially from large retail enterprises. This study will specifically focus on three hypothesized dynamic capabilities, which are; sensing and seizing of market opportunities and reconfiguring the resource base, the mediating effect of competition orientation and customer orientation for competitive advantage among retail SMEs within a developing country given the business environmental pressures.*

**Keywords:** *competitive advantage, sensing, seizing and reconfiguration capabilities, customer and competitor orientation*

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### **I. Background**

In the globalization, integration and liberalization era, the business environment is becoming fiercer than before, businesses of all types and sizes are facing continually changing situations externally and internally. Furthermore, the question at the heart of every strategist in every business enterprise is how to cope with these ambiguities, leverage competitive edge and expected level of performance (Vazquez, Santos, & Alvarez, 2001). These trends are transformed by many factors which according to Hall (2003) can be summarized in terms of five key trends; globalization and the increasing intensity of competition, changing organizational structures, new worker profiles, preferences and predispositions, advances in information and communication technology and the rise of knowledge management all of which are pushing firms to rethink of ways to become more competitive and efficient (Wijnands et al., 2008; Banterle and Carraresi, 2007). Business enterprises especially in the retailing sector have to strategize on acquiring greater bargaining power due to their increasing concentration level.

All these features are well reflected in the Kenyan retail market especially among the large retail formats due to their resource endowment. This leaves the small and medium sized retail enterprises (SMREs), which constitutes the majority in the sector at a disadvantage (Banterle et al., 2011). Thus, they are forced to rethink of successful strategies in order to survive in the market alongside large retail competitors which benefits from economies of scale within the rapidly changing consumer market. In this context of high market dynamism and difficulties, it is useful to understand the potential sources of competitive advantage for retail SMEs (Azevedo and Ferreira, 2007).

### **1.1 Retail sector in Kenya**

In Kenya, the small and medium retail enterprises play a crucial role in the overall economy contributing 10% to GDP and an estimated 76% total wage payment according to the Sessional paper No. 10 of 2012 on Kenya Vision 2030 (Gok, 2012). According to the Kenyan Economic Survey year 2012, the retail and wholesale trade grew by 19 per cent over the past five years becoming the second largest driver of economic growth after transport and communication (Gok, 2012). Citibank in the year 2012, ranked Kenya as having the second most developed retail system in Africa after South Africa (Citibank survey report, 2012). The retail industry has now become crucial as one of nation's growth engine playing the role of delivery window for nearly 40 million people in the country.

Over the last five years, the FMCG retailing sector in Kenya has experienced phenomenal growth and changes. These changes are characterized by the growing Kenyan population and rural urban migration, infrastructural boom key being the construction of the 30 billion shillings Nairobi Thika Superhighway, real estate boom, rapidly growing middle-class population which is pushing up consumerism and the high demand for diverse products coupled with rising incomes all set to drive consumer sector vibrancy, thus making the retailing outlook especially between Nairobi and Thika region to continue being positive for new retail ventures (Knight Frank, 2012).

Other key observations are large retail stores leading the expansion of malls, hypermarkets and convenience stores especially along the Thika superhighway. The infrastructure boom in Kenya and specifically along the superhighway has seen the region that has traditionally been occupied by large low income group now struggling to satisfy the needs for the uprising middle class. Positive macroeconomic conditions (average GDP of 5.1% expected through to 2014) is making it an appealing choice for retailers seeking more "contained" markets. Other indicators are, improving economic conditions such as, trade liberalization which has been evaluated generally positive in terms of economies of scale, intensified competitiveness level, technology innovation and management efficiency of the large retailing chains (Deloitte, 2011).

Owing to the fore mentioned change drivers, Kenyan retail market has become attractive as a target sector for Foreign Direct Investment (FDI). According to a recent report by Knight Frank (2012), the appetite for Kenya's retail industry continues to grow, with the impending entry of four major global retail chains. South African supermarket giant, Mass mart, which is owned 51 per cent by US retail giant, Wal-Mart, has booked space in the Garden City shopping mall along Thika Road and has planned entry by May 2014. Game Stores, Jet stores and Edgars plan to open shop in Kenya by 2014. The report says that seven malls are scheduled for completion by 2014. The malls will be located in the outskirts of Nairobi and Mombasa. This will further heighten competition in Kenya's retail market. The report indicates that, the international retailers are positioning themselves to take advantage of Kenya's increasing consumerism as they seek to enter other African markets through Kenya.

Additionally, Kenya's retail sector is further dominated by six major local supermarkets which are also on an aggressive expansion especially along Thika highway. Examples are; Nakumatt and Tuskys opened branches in Thika town and Roysambu Thika Road Mall (TRM). Uchumi is set to revamp its existing Ruaraka branch to match the rivals and modern stores by constructing a mall opposite the TRM. They are all dominating the retail landscape with their nationwide coverage and fair priced quality product offerings especially targeting the upper and middle class customers, achieved by leveraging large scale economies across the value chain and now strategically locating themselves in the residential areas and other convenient locations which have ease of access (Knight Frank, 2012).

With this trend, one would almost summarize that small and medium retail enterprises that have been in existence for long can no longer find competitive space in the retail sector in Kenya since this trend has heightened competition in the retail sector thus threatening the very survival of the small and medium retail businesses which comprises 76 per cent of the country's retail market. This implies that, SMRE's must compete in a complex and challenging context so as to survive the stiff competition in markets where large and multi-national retail firms also operate. Though large retail firms face the challenges that small and medium retail enterprises also face, the SMRE's have the added struggle of developing dynamic capabilities that will enable them to build and maintain high levels of relative competitiveness against the large retail firms given the environmental context they operate in.

### **1.2 Trend analysis of retail SMEs in Kenya**

Retailing SMEs in Kenya are faced with numerous challenges including intense competition, demand for satisfying the needs of sophisticated customers, delivery of new and quality products efficiently, among other challenges. Consumers are also expecting that the retailers will offer the right match in terms of right product offering, place and time and by the right appeal. Also, the market is exploiting certain retail enterprises advantages such as, the accessibility, convenience and quality to shop for consumables such as bread, milk and groceries on a daily or weekly basis (consumer insight survey, 2012). While the growth of the large retail chains

has meant convenience, variety and cost effectiveness for most consumers, small and medium scale retail traders are losing out and are slowly being cut out of the value chain, since the large retail chains are offering virtually all range of products under one roof (Citibank survey, 2012).

Conversely, following the invasion of the retail sector by the large retail chains, there's evidence of a slow death of small and medium retail stores which are being driven by the changing consumer behaviors and how frequently they shop. A survey by consumer insight showed that 55% of shoppers now buy their necessities monthly as opposed to 16% in the year 2011. The survey conducted in the second half of the year 2012 showed the small and medium retail enterprises for years the preferred choice for many Kenyans were losing the battle for survival to large retail stores that have set up hundreds of branches across the country with a keen emphasis on entering the residential markets. It was found that 86% of shoppers considered convenience and quality, 43% pricing and 22% good facilities (Consumer Insight Survey, 2012).

Given these trends, various strategic models are helpful for the SMREs in countering these trends and hedging their competitiveness given their level of innovativeness, adaptability and flexibility in coping with the changing competitive landscape, changing customer trends and other institutional and infrastructural changes (Odedairo & Bell, 2010). The theoretical model of Resource-based View (RBV) is helpful in this sense as it states that a firm that exploits its internal resources and capabilities could achieve a good performance, as the resources are stable and reliable in the process of strategic management, making the firm able to face market dynamics and competition (Wilkens et al., 2004; Teece et al., 1997; Teece, 2007).

This implies that, to be successful SMREs could identify their idiosyncratic characteristics in order to differentiate themselves from other competitors and carve out a distinctive niche in the market (Barney et al., 2011). Thus, they should select their peculiar resources and find the best way to use and organize them in order to deploy specific capabilities and to set up a successful strategy allowing them to operate profitably in the market (Teece et al., 1997; Teece, 2007).

However, their ability to take advantage of the changing trends depends to a large extent on the internal and external factors that may enable (or inhibit) these enterprises to realize their potential represented by their dynamic capabilities. This means that, it is important to recognize that the value of dynamic capabilities is context dependent (Barreto, 2010). In a similar vein, contingency theory suggests that firm competitiveness depends on the alignment of the organization with the environment as well as the congruence of the organizational elements with one another (McKee et al., 1989).

Thus, the thrust of this research is that the realization of the potential advantage accruing to deployment of dynamic capabilities of sensing opportunities, seizing and configuring resources depends on the business's strategic orientation in the markets in which it is embedded. The competitive pressures, increasing customer sophistication, infrastructural dynamics are among other forces that strengthen and force retail SMEs to strategize on maximum utilization of internal and external capabilities for competitiveness (Mahmoodzadeh, Jalalinia & Yazdi, 2009). Thus, the purpose of this study is to examine the effect of strategic orientation on the relationship between dynamic capabilities and competitive advantage of the retail SMEs in Kenya.

### **1.3 Objectives**

The general objective will be to investigate the mediating effect of strategic orientation on relationship between dynamic capabilities and competitive advantage of small and medium retail enterprises in Kenya. To achieve this overall objective, the research will specifically seek to determine the mediating effect of strategic orientation on the relationship between sensing capabilities and competitive advantage of small and medium retailing enterprises in Kenya, analyze the mediating effect of strategic orientation on the relationship between seizing capabilities and competitive advantage of small and medium retailing enterprises in Kenya, examine the mediating effect of strategic orientation on the relationship between reconfiguration capabilities and competitive advantage of small and medium retailing enterprises in Kenya and analyze the mediating role of strategic orientation on the relationship between dynamic capabilities and competitive advantage of small and medium retailing enterprises in Kenya.

### **1.4 Justification and significance**

The proposed research will be undertaken for five key reasons. First, relatively little is known about how deployment of dynamic capabilities and strategic orientation factors combine in a comprehensive model of firm above average performance (Deshpande and Farley, 2004), particularly in the context of retail SMEs facing survival threats from large retail formats (Tzokas, Carter, & Kyriazopoulos, 2001). Second, there is a need of studies focusing on context dependent strategy in determining the enterprises deployment of its capabilities in highly competitive markets (Tan & Smyrniotis, 2006). Third, influences of dynamic capabilities constructs on strategic orientation have been largely overlooked (Menguc, Auh, & Shih, 2007).

An examination and testing of customer focus and competition orientation strategy formation mediating on the links between dynamic capabilities and competitive advantage a lot remains unexplored

(Vazquez, Santos, & Alvarez, 2007). Additionally, Kenyan retail market has been ranked as the second best attractive after South Africa with so many retail giants strategically entering this market hence a need to examine the competitive position of the already existing smaller and medium retail enterprises.

On the other hand deployment of dynamic capabilities for competitive advantage can be very expensive for small and medium enterprises already facing resource constraints hence the contingency framework will enrich the theoretical and practical understanding of context-dependent capabilities deployment for competitive advantage and survival in a highly competitive and dynamic business environment within a developing country context like Kenya.

The significant role of retailing SMEs in the promotion of national development agenda in Kenya has been well-documented Sessional paper No. 10 of 2012 on Kenya Vision 2030 (Gok, 2012). According to the Vision 2030 development agenda, the sector is considered as the link between production and consumption, both of which are expected to expand substantially as the economy heads to a 10 per cent growth rate (Gok, 2012). The sector accounts for approximately 10 per cent of GDP and 10 per cent of formal employment and it is expected to expand significantly as a result of infrastructural boom, improved economic conditions, population growth, urbanization, a growing middle class and a financially attractive business environment.

To achieve this, small and medium retail enterprises must succeed and achieve sustainable competitiveness, survival and industrialization, thereby leading to results that are more equitable and efficient. Thus firstly, the study will enable retail SMEs sector policy makers to develop and train effective strategies for enhancing the sustainability of SMEs for their growth and survival in the highly competitive environment by leveraging the competences and resources. Additionally, the results of the study will also help the government planners in understanding how to come up with policies that supports the competitive position of SMEs such as institutional, regulatory and infrastructural resources.

## **II. Literature Review**

The chapter shall reviews the theoretical and empirical review underlying the study, conceptual framework that illustrates the relationship between the independent variables, dynamic capabilities and dependent variable competitive advantage along with mediating variable the enterprise's strategic orientation that influences this relationship. The study then proceeds to present on the theoretical model of capabilities influencing business competitive advantage, a critic of the literature, the research gaps and the summary.

### **2.1 Theoretical review**

The proposed study shall review the different strategy management paradigms, such as the competitive forces approach (Porter, 1980), strategic conflict approach (Shapiro, 1989), contingency framework (Burns & Stalker, 1961; Lawrence & Lorsch, 1967) and resource-based view approach (Penrose, 1959; Rumelt, 1984; Wernerfelt, 1984).

### **2.3 Research propositions**

This study proposes that dynamic capabilities are a type of dynamic strategy that influence retail SMEs strategies from external to internal factors, similar to the views provided by Zahra, Sapienza and Davidsson (2006), who considered the deployment of dynamic capabilities to result from different situations rather than the dynamic environment. An enterprise hence needs to learn from observing the internal changes to further influence the external transformation within different changing environments.

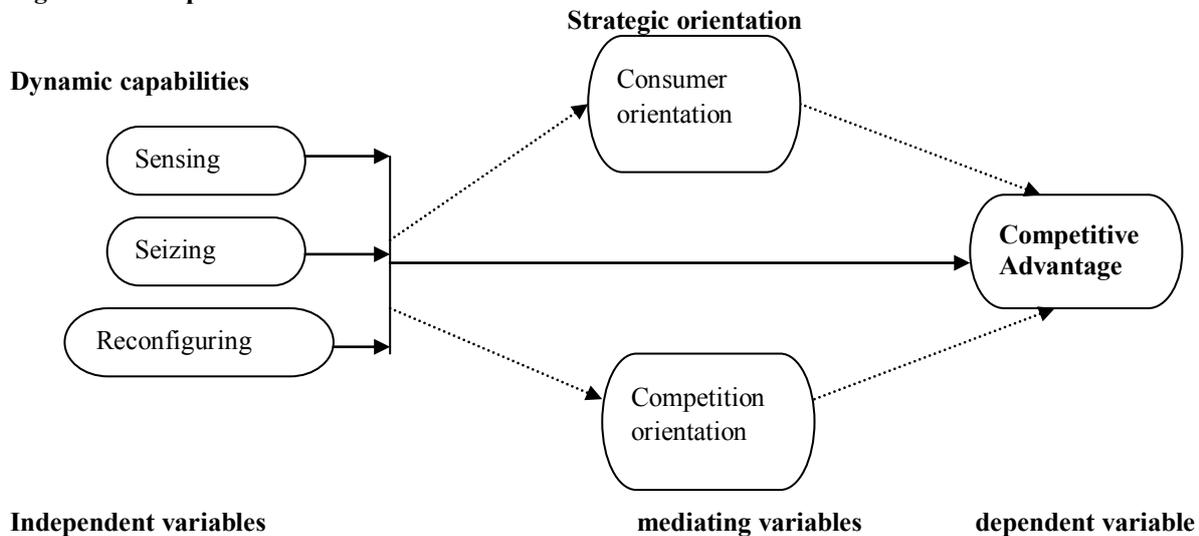
Additionally, 'strategic orientation' as a core value of the contingency theory indicates that the greater the consistency between the competitive strategy and contingent factors, the more positive the impact on organizational above average performance (Miller, 1981). Dynamic capabilities describe the different strategic movements that occur between business capabilities with different dynamics. Competitive strategy is used to deal with the internal and external environment, and represents the mediating force between an organization and its environment (Mintzberg, 1987), with its main goal being to achieve competitive advantages.

Competitive advantage is a product of competitive strategy, which indicates the ability of managers to effectively implement immaterial and material resources to gain more value and performance from the business competition (Jones, 2001). The business-level strategy of constructing competitive advantage can be roughly separated into three types: cost leadership, perceived quality improvement and market responsiveness. Cost leadership involves using low cost to create low price competition; quality improvement describes the differences between the quality products/services of a business and those of its competitors, which are capable of bringing extra value to the consumers (Porter, 1985), and market responsiveness indicates new business methods that can produce or manufacture new products, for example increasing numbers of product types, systems of production management, organizational structure and strategy development (Hill and Jones, 1998).

## 2.4 Proposed conceptual framework

The research conceptual framework will be based on the reviewed variables under study to present graphically the interaction of the different variables in influencing and determining the objective of the study's relationships. Dynamic capabilities will be considered as the independent variables. Competitive advantage of retail SMEs in terms of cost leadership, perceived quality improvement and market responsiveness are considered as the dependent variable, while strategic orientation (customer and competition) will be the mediating variable. This is described in the figure 1 below;

Figure 1: conceptual framework



## 2.5 Research hypotheses

The researcher postulates the following hypotheses which will be tested.

Hypothesis 1 ( $H_{01}$ ): Strategic orientation has no positive influence on the relationship between sensing capabilities and competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 2 ( $H_{02}$ ): Strategic orientation has no positive influence on the relationship between seizing capabilities and competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 3 ( $H_{03}$ ): Strategic orientation has no positive influence on the relationship between reconfiguration capabilities and competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 4 ( $H_{04}$ ): Deployment of dynamic capabilities has no positive association with an enterprise strategic orientation

Hypothesis 4a ( $H_{04a}$ ): Customer orientation has no positive impact on competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 4b ( $H_{04b}$ ): Customer orientation does not mediate the positive association between deployment of dynamic capabilities and competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 4c ( $H_{04c}$ ): Competition orientation has no positive impact on competitive advantage of small and medium retailing enterprises in Kenya

Hypothesis 4d ( $H_{04d}$ ): Competition orientation does not mediate the positive association between dynamic capabilities and competitive advantage of small and medium retailing enterprises in Kenya

## III. Research Methodology

The research will be descriptive with the target population being the 8,601 FMCG retail SME's registered with Thika Municipal Council. Stratified random sampling technique will be used to select a sample of 358 enterprises and data be collected by use of questionnaires and then analyzed using multiple regression analysis. The results of the study are expected to show a significant positive indirect influence of dynamic capabilities on retail SMEs competitive advantage.

### 3.1 Conclusion

Competitive advantage is a relative notion. It can be viewed from various perspectives. Nonetheless, examining organizational competitive advantage from the dynamic capabilities view is indeed crucial as it can be used as a conceptual framework for small and medium retail enterprises in particular facing stiff competition

from giant retailers within a developing country context like Kenya. This is meant to enhance their competitive advantage position and performance via application and manipulation of identified organizational resources, capabilities and systems. Such a research can contribute to the body of knowledge by lending empirical support and further extending the resource-based view (RBV) of competitive advantage by examining the relative magnitude of importance placed upon organizational internal attributes towards attaining competitive advantage and enhancing firm performance. As such, the research will attempt to examine the relevancy and applicability of those related theories and concepts in current condition by testing the hypotheses. From the research, it is hoped that a model can be developed to examine and depict the relationship between organizational resources, capabilities, systems, competitive advantage and performance. The rest of research will be organized as follows first, brief discussion of structure of retail sector in Kenya. Second, reviewing the literature relating to drivers of competitive advantage in retail enterprises as there primarily informs objectives of research. Third, presenting methodology employed as the rationale of research study. Fourth, presenting ample analysis and findings concluding research implications.

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