

The Influence of Innovativeness on the Growth of SMEs In Kenya

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ABSTRACT

Innovation is the process of creating a commercial product from an invention. Innovation can deliver four types of benefits besides cash: knowledge, brand, ecosystem and culture. The main objective of the study was to establish the influence of innovativeness on the growth of SMEs in Kenya. The study adopted descriptive survey and exploratory design. The study targeted 4560 SMEs in Nairobi County who are registered by Ministry of Industrialization and Ministry of Trade. Regression models were used to examine the influence of innovativeness skills on growth of SMEs in Kenya. Questionnaires were used as the main data collection. Descriptive statistics and inferential data analysis method was to analyze the gathered data.

The findings indicated that innovativeness influences the growth of SMEs in Kenya. The tendency of owner/manager to engage in and support new ideas, novelty, experimentation and creative processes results in new products, services or technological processes which has a great influence on the performance of SMEs.

INTRODUCTION

Lehtimaki (1991) attributed the emergence of new ideas for product innovations in SMEs to entrepreneur. SMEs very actively explored new product ideas and the most frequent way of achieving this included contacts with customers. Daley (2001) identified demand placed on business by customers/clients, close working relationships with a key customer and close analysis of competitor products are the major drivers of innovation in SMEs covered in three different countries: UK, France, and Portugal.

Vonortas&Xue (1997), while studying the process innovations of small firms in the USA, observed that economic incentives, internal resources, and technical and organizational competencies that a firm has developed or accumulated over time and a firm's linkage to external sources of expertise for learning about new technological development were the major forces that influenced these firms in adopting a process innovation. Danneels & Kleinschmidt (2001) in the context of new product development argued that it consists of bringing together two main components: markets and technology. According to them, product innovation requires the firm to have competences relating to technology (enabling the firm to make the product) and relating to customers (enabling the firm to serve certain customers).

Schumpeter (1934) was the first writer who used innovation in explaining entrepreneurship. Lumpkin and Dess (1996, p. 142) defined innovation dimension as "the tendency of a firm to engage in and support new ideas, novelty, experimentation and creative processes that may result in new products, services or technological processes. Beside Covin & Slevin (1991) proposed innovation as "the extensiveness and frequency of product innovation and the related tendency toward technological leadership.

SMALL MEDIUM ENTREPRISE

An enterprise is considered to be any organized effort intended to return a profit or economic outcome through the provision of services or products to an outside group (Carland, Hoy, Boulton & Carland, 1983). The operation

of an enterprise traditionally requires the investment of capital and time in creating, expanding or improving the operations of a business. (Meredith, 2001).

Small to medium enterprises are considered those enterprises which have fewer than 250 employees. In distinguishing between small and medium sized enterprises, the small enterprise is defined as an enterprise which has fewer than 50 employees. These businesses are often referred to as SMEs and are associated with owner proprietors (Meredith 2001; Schaper & Volery 2004)

According to Carland et al. (1983), an SME owner is an individual who establishes and manages a business for the principle purpose of furthering personal goals. The business is their primary source of income and will consume a majority of the owner's time and resources. The owners perceive the business as an extension of their identity and are intricately bound with family needs and desires.

STATEMENT OF THE PROBLEM

Markets are changing all the time. It does depend on the type of product the business produces, however a business needs to react or lose customers. SMEs often attempt to benchmark competitors or related service industries to improve key business processes. Competition is escalating, both from traditional players and from new entrants, owing to deregulation. Changing consumer behavior and needs, globalization, disintermediation are all the dynamics being faced SMEs. Information technology is also having its impact (Chorafas, 1987). The increase in innovation adoption is a largely defensive measure against increasingly sophisticated and highly demanding consumers, escalating competition, and the necessity to control and reduce rising costs (Barra, 1990). Previous studies done on innovation include Mwangi (2007) who did a study on the effect of innovation in Kenya Financial Institutions, Gitonga (2003), who studied the factors influencing innovation in Kenya's banking industry. It was evident that no known local study had been done on this phenomenon and it was against this background that this study sought to establish the influence of innovativeness on the growth of SMEs in Kenya.

RESEARCH OBJECTIVES

General Objective

The main objective of the study was to establish the influence of innovativeness on the growth of SMEs in Kenya.

LITERATURE REVIEW

Resource Based Theory

Resource-based view has become one of the most influential and cited theories in the history of management theorizing. It aspires to explain the internal sources of a firm's sustained competitive advantage (Kraaijenbrink, Spender & Groen, 2010). It was Penrose who established the foundations of the resource-based view as a theory (Roos & Roos, 1997). Penrose first provides a logical explanation to the growth rate of the firm by clarifying the causal relationships among firm resources, production capability and performance. Her concern is mainly on efficient and innovative use of resources. She claimed that bundles of productive resources controlled by firms could vary significantly by firm, that firms in this sense are fundamentally heterogeneous even if they are in the same industry (Barney & Clark, 2007). Wernerfelt (1984) took on a resource perspective to analyze antecedents of products and ultimately organizational performance and believed that "resources and products are two sides of the same coin" and firms diversify based on available resources and continue to accumulate through acquisition behaviors.

The knowledge based literature of the firm fosters and develops the resource based theory in that it considers knowledge to be the most complex of an organization's resources (Alavi & Leidner, 2001). According to resource-based theory, the intellectual capital (IC) is a main source to improve enterprise growth. Therefore, intellectual capital has been studied by many past researchers who investigate the influence of intellectual capital on business performance. However, most past researchers focused on the impact of individual intellectual capital on performance while neglecting the effects of specific elements of intellectual capital.

The currently dominant view of business strategy – resource-based theory or resource-based view (RBV) of firms – is based on the concept of economic rent and the view of the company as a collection of capabilities. This view of strategy has a coherence and integrative role that places it well ahead of other mechanisms of strategic decision making. Ganotakis & Love (2010) used the Resource Based Theory (RBT) to explain the importance of human capital to entrepreneurship. According to RBT, human capital is considered to be a source of competitive advantage for entrepreneurial firms. Ownership of firm-specific assets enables a company to develop a competitive advantage. This leads to idiosyncratic endowments of proprietary resources (Barney, 1991; Peppard & Rylander, 2001). According to RBT, sustainable competitive advantage results from resources that are inimitable, not substitutable, tacit in nature, and synergistic (Barney, 1991). Therefore, managers need to be able to identify the key resources and drivers of performance and value in their organizations.

The RBT also states that a company's competitive advantage is derived from the company's ability to assemble and exploit an appropriate combination of resources. Such resources can be tangible or intangible, and represent the inputs into a firm's production process; such as capital, equipment, the skills of individual employees, patents, financing, and talented managers. As a company's effectiveness and capabilities increase, the set of available resources tends to become larger. Through continued use, these “capabilities”, defined as the capacity for a set of resources to interactively perform a stretch task or an activity, become stronger and more difficult for competitors to understand and imitate. (R&D expenditures) and can be used to augment future production possibilities.

EMPIRICAL REVIEW

Zerenler, (2008) made a research in the Turkish automotive supplier industry in order to investigate the influence of innovativeness upon the SMEs performance. 117 questionnaires were sent to managers of marketing department, R&D department and production department. The response rate of this study is high (78% or 92 respondents). Main conclusion from this study is: SMEs growth had significantly positive relationships with innovation performance.

In the study of Wu et al. (2008), they attempted to explore the mediating effect of innovation on SMEs growth. The research was made in Taiwanese manufacture and non-manufacture industries. Seven hundred survey questionnaires were mailed to firms. The response rate of the study is 22.71%. They found that effects of innovation exist at significant levels, suggesting a perfect mediating effect of innovation on growth.

CRITICAL REVIEW

Abouzar Zangouezhad, Asghar Moshabaki, (2009) carried a study on the role of innovation in Iran the study found out that operational, organisational or managerial processes are significantly related in attaining innovation. However, the companies chosen for the study were mainly large companies thus; the results may not be applicable to SMEs. The survey was limited to one country (Iran).

RESEARCH GAPS

Mohammad (2009) did a study on the effect of innovativeness on firm performance: an investigation of Iran state companies. The purpose of this paper was to analyze the role of innovativeness and its relationship with financial performance of Iran state companies during the period 2010-2012. 49 state companies were selected as the sample. The results of the research revealed that value added innovativeness and its components had a significant positive relationship with companies' profitability. Wang (2011) did a study on innovativeness and Firm Performance. The main purpose of the study was to understand the innovativeness of the proxy variables on firm performance and the related expenses of the company's contribution to value creation.

This study therefore intends to fill these pertinent gaps in literature by studying the selected independent variables on the influence of innovation on the growth of SMEs in Kenya. This study will add value to existing

literature by providing empirical evidence on the influence of innovativeness on the growth of SMEs in Kenya and fill the existing contextual and conceptual gaps.

METHODOLOGY

The study adopted an exploratory approach using a descriptive survey design. A descriptive research design determines and reports the way things are (Mugenda & Mugenda, 2003). Data available from the Ministry of Trade and Ministry of Industrialization, (2011) reveal that there are 2500 SMEs in Manufacturing, 1500 SMEs Trading and 560 SMEs in the service industry (RoK, 2012). This makes a total of 4,560 SMEs. Therefore the study targeted 4,560 SMEs in Nairobi County. The study targets this area because of the rural and urban influences. A proportionate sample size of approximate 456 respondents which is 10% of the population was selected using a stratified random sampling technique. The primary research data was collected from the owners of the SMEs in Nairobi using a questionnaire and supported by interview guide who was administered through interviews. A pilot study was undertaken on at least 46 SMEs owners to test the reliability and validity of the questionnaire. Data analysis was done with the help of software programme SPSS version 21 which is the most current version in the market and microsoft excel to generate quantitative reports.

RESULTS AND FINDINGS

Provision of Incentives for Innovative Employee

The study found out that incentives for innovative employee influence the growth of SMEs to a very great extent. These findings correspond with those by Hirschey & Weygandt (1985) who found that a creative and innovative employee who is motivated to develop new products and new markets has strong association to the growth of SMEs. Gary (1993) observed that recognition through incentivizes to the employees is a crucial component to building a sustained and thriving innovation in the enterprise which is a prerequisite for SMEs growth where compensation is pegged on employees creativity associated with emergence of new markets and new products.

Entrepreneurs Support on Employees' Innovation

The study found out that entrepreneurs' support on employees innovation influence the growth of SMEs to a very great extent. The findings concur to those of Barr (2002) who showed that entrepreneurs' support on employees' innovation through material rewards such as bonuses and pay increases encourage innovation.

Number of patents within the enterprise

The study found out that number of patents within the enterprise influence the growth of SMEs to a very great extent. These findings concur with the findings of Meilan (2010) who found that inclination to use patents for innovation protection is positively related to the firm's growth. These findings correspond with those by Grasenick (2004) who established that the numbers of patents within the enterprise are beneficial because they generate an incentive to invest in R&D and as a consequence increase the likelihood of innovation and firm growth. Bollen and Long (1993) also observed that patents grant a temporary monopoly on the exploitation of knowledge which could lead to the translation of invention into successful commercial innovation for a firm and as a result increases firm's growth.

Regression Analysis

The linear regression analysis shows a relationship between the dependent variable which is growth and independent variable which is innovativeness. The coefficient of determination R^2 and correlation coefficient r shows the degree of association between managerial skills and growth of SMEs in Kenya. The results of the linear regression $Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \text{innovativeness} + E$ indicate that $r^2 = 0.746$ and $R = 0.864$ this is an indication that there is a strong linear relationship between innovativeness and growth of SMEs in Kenya. The findings concur with those of Wu, Chang and Chen (2008) who found that effects of intellectual capital including human capital, customer capital and structural capital, on innovation exist at significant levels, suggesting a perfect mediating effect of intellectual capital on innovation.

Inferences can therefore be made that tendency of a firm to engage in and support new ideas, novelty, experimentation and creative processes results in new products, services or technological processes. Product innovation requires the firm to have competences relating to technology and relating to customers.

Model

Model	R	R Square	Adjusted R Square
1	.864	.746	.662

The table below shows the results of ANOVA test which reveal that innovativeness have significant effect on growth of SMEs. Since the P value is actual 0.007 which is less than 5% level of significance. This is depicted by linear regression model $Y=B_0+B_3X_3+E$ where X_3 is the innovativeness the P value was 0.007 implying that the model $Y=B_0+ B_3X_3+E$ was significant.

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.067	1	2.067	1.351	.007
	Residual	289.263	189	1.530		
	Total	291.330	190			

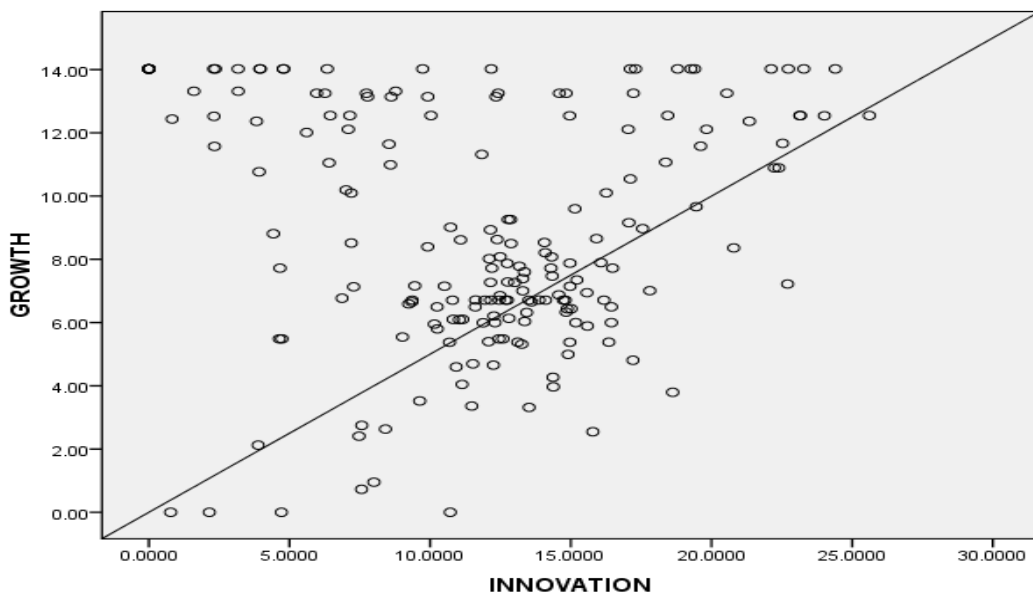
- a. Dependent Variable: Entreprise Growth
- b. Predictors: (Constant), Innovativeness

Coefficients

Model		Unstandardized Coefficients	Standardized Coefficients	Sig.
1	(Constant)	3.514	Beta	.000
	Innovativeness	.033	.084	.007

Dependent Variable: Entreprise Growth

The figure below shows the results of innovativeness on the growth of SMEs in Kenya. The scatter diagram indicates a positive gradient which is an indicative that innovativeness influences the growth of SMEs.



RECOMMENDATIONS

The study is a justification of the fact that an entrepreneur with competitive innovativeness skills has a deep understanding of the small and medium sized enterprises which catapults their growth to a large extent.

The study recommends: Owners/Managers should use technology in controlling the production cost while maintaining competitive prices as it results in continued profitability of a firm and therefore growth. Owner/managers should be efficient time managers with a control on the SMEs cost of operation to help provide a working schedule and competitive prices which fit the SMEs' client needs.

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