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DYNAMIC CAPABILITIES AND STRATEGIC ENTREPRENEURSHIP: A STUDY OF SRI LANKAN SMES

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Abstract

Strategic entrepreneurship has been widely acknowledged as the appropriate context representing the way of creating value in business organization. However, yet we do not fully understand the process of strategic entrepreneurship or elements of it that give rise to them and as such strategic entrepreneurship remains in need of further explanation. This study primarily believes that any concept or business model is required to address the dynamic changes in the markets. Thus, this study explains the dynamic capability concept and its role in perpetuating entrepreneurial and strategic actions in the SMEs. The dynamic view of resource based theory is adopted from firm level framework used to identify the unique bundle of dynamic capabilities that promote firm's entrepreneurial and strategic actions. The identified framework was validated from the empirical data gathered through the explorative questionnaire survey of 488 manufacturing SMEs in Sri Lanka. The finding suggests that SMEs are better able to address market challenges when they have strong dynamic abilities that engaged them in strategic entrepreneurship. The study thus encourages SMEs to create and develop dynamic capabilities, not only because it sustains their livelihood over generation, but because it also facilitates the entrepreneurial and strategic actions in creating the firm's wealth.

Key words: Dynamic capabilities, Entrepreneurial learning, Strategic entrepreneurship.

1. INTRODUCTION

The dynamic capabilities are considered as a central concern of the firm's strategy and value creation and competitive advantage (Teece et al, 1997; Eisenhardt & Martin, 2000; Winter, 2003; Teece, 2007; Helfat et al. 2007). Resource Based View (RBV) argues that firm's bundles of tangible and intangible resources that are valuable, rare and inimitable can be the sources of competitive advantages. This line of thinking have been gradually extended to change markets rapidly by highlighting the role of dynamic capabilities as "the antecedent organizational and strategy routines by which managers alter their resource base to generate new value creating strategies" (Eisenhardt & Martin, 2000).

Therefore, dynamic capabilities act as a shield between firm's resources and the shifting business environment by helping a firm adjust its resource base and thereby maintain the sustainability of its competitive advantage, which otherwise might be eroded. The literature however has not yet been adequately explained the role of dynamic capabilities in perpetuating entrepreneurial and strategic activities in the SMEs through the development of strategic entrepreneurship over multiple generations. Thus, new insights are called for investigation for the new landscape to integrate dynamic view to the strategy and the entrepreneurial theories. Having understood this gap in the literature, this study explores the dynamic capabilities and their

roles in perpetuating entrepreneurial and strategic activities in the SMEs.

2. THEORETICAL FRAMEWORK AND HYPOTHESES

Firm's ability to simultaneously explore the future opportunities and exploit today's opportunities in creating sustainable competitive advantages is highly significant in the today's business world. This process is termed as strategic entrepreneurship (Ireland et al. 2001, Kyrgidou & Hughes, 2010; Genc, 2012). Recent years, the increasing interest among researchers, academics and practitioners as well as academic literature show evidence that strategic entrepreneurship helps firms to properly response the challenges which are created by the environmental changes in order to create sustainable advantage in the competitive arena (Ireland & Webb, 2007; [Hitt et al. 2011](#); Covin & Kurotko, 2008).

The concept of dynamic capabilities is an emerging paradigm in the field of strategic management. Intellectual antecedents to dynamic capability approach include resource based view of the firm (Wernerfeld, 1984) and organizational learning (Audretsch & Keilbach, 2007). Teece et al. (1997) noted that winners in the global market place have demonstrated timely responsiveness and rapid and flexible product innovation, along with managerial ability to effectively coordinate and redeploy internal and external competencies. They term this ability to achieve new forms of competitive advantage as "dynamic capabilities" to emphasize two aspects of strategy that previously were not the main focus. According to Makadok (2001) dynamic capabilities are constructed within the firms rather than bought in the outside. Dynamic capabilities are considered as organizational routines in the most general context (Helfal et al. 2007; Zollo & Winter, 2002). These processes then become rooted in the firm over time and are employed to

modifying of resources or recombination of old resources in novel ways (Simon & Hitt, 2003). In general, dynamic capabilities comprise four key processes. They are termed as "reconfiguration, leveraging, learning and integration" (Teece et al. 1997). Reconfiguration deals with the alteration and recombination of the firms' assets and resources. Leveraging involves the reproduction of procedures, processes, actions or systems that are used in one area into another area. It also involves the processes of expanding resource scope and breadth into new domain. Learning, as discussed earlier, acts as mechanism that helps to perform tasks more effectively and efficiently. Integration involves the processes that combine and manage firms' assets and resource in a certain manner to the development of a new resource base (Teece et al. 1997).

The development of empirical literature pertaining to the influence of dynamic capabilities on strategic entrepreneurship has been hindered by vague description, operationalization, and measurement of the two concepts. However, there is a sufficient evidence to support the view that a firm's capabilities significantly influence strategic entrepreneurship that characterized with opportunity exploration and opportunity exploitation activities which lead to creation of competitive advantage (Cockburn, 1994; Zollo & Singh, 1998, Eisenhardt and Martin, 2000)

SMEs are often characterized with a simple organizational structure where the managers closely monitor the firms operations. This gives the managers an opportunity to monitor the available resources constantly and thereby evaluate their potentiality. Greene et al. (1999) argue that small firms need to build a broader set of resource bases and competencies to promote their search for new opportunities and competitive landscape. The ability to combination of resources in novel way is a driver for the new opportunity creation process. So, firm has to identify new combinations of productive resources within

the firm and to extend the frontiers of capabilities. This process creates the synergetic effects of resources to use in new value creation activities (Venkataraman et al. 1992). Such combination, integration and linkages with various parties improves overall strategic capability which enables the firm to reconfigure its resources and provides ways to encourage firm's opportunity exploration and exploitation activities (Borch & Madsen, 2007).

2.1 Resource integration and coordination capabilities and strategic entrepreneurship

SMEs' capability of capture or realign business concepts where resources are added, combined or split is widely recognized as an important strategic feature in their search for competitive advantage (Eisenhardt et al. 2000). Greene et al. (1999) suggest that small firms have to develop a broader set of resource base and competencies that are presented and evolved within their firms. This process is facilitated by the competitive strategies and the value chain activities that serve the present strategy of the firm (Argyres & McGahan, 2002). The combination of resources is the driver for the firm's search for new opportunities as well as exploits them for attain superior performance in competitive landscape. This process is facilitated by a synergetic effect of combining and reconfiguration of the resource combinations with new resources of the firm (Venkataraman et al. 1992). SMEs may have benefited from a simple firm structure, flexible operations, direct ownership involvement and low formalization, quick decision making process, few organizational boundaries and more opportunities for linking resources into different parts of the organization (Webb et al. 2010; Messeghem, 2003; D'Amboise & Muldowney, 1988; Miller & Toulouse, 1994).

Hypothesis 1 (H₁): Resource integration and coordination capabilities have a positive

influence over strategic entrepreneurship in SMEs

2.2 Entrepreneurial learning and strategic entrepreneurship

Research has evident that the success of strategic entrepreneurship is widely facilitated by the firm's ability to involve in the process relating to continuous development and radical renewal of its resources and capabilities (Simon & Hitt, 2003; Hitt et al. 2002). Thus, learning how to acquire, bundle, leverage, and renew the firm's strategic resources is vital important to realizing competitive advantages and creating a value through the process of strategic entrepreneurship (Hitt et al. 2011). In general, even though prior strategic management and entrepreneurship literature recognize the strategic role of organizational learning, research has not yet been critically examined the effect of entrepreneurial learning on strategic entrepreneurship and creating of competitive advantage (Covin & Kuratko, 2006). However, building on the RBV and knowledge based view, research has given increasing attention to the learning theories to provide insights into how organizations can interpret, distribute and incorporate strategically important knowledge to facilitate and continuously recreate competitive advantages (Hamel, 2000). Some scholars (Kuwada, 1996; Thomas, 2004) refer the learning behavior and processes that generate a firm's long term adaptive capabilities as strategic learning which has later been identified as a dynamic capability by some of studies (Collis, 1994; Eisenhardt & Martin. 2000). Firm that pursues exploration strategies concentrates on managing and designing their operations in which add extra value the current operations. Simsek et al. (2009) argues that such explorative actions create new technical, social, and organizational knowledge. In general, however, explorative actions do not yield returns without investing them in the creation,

evaluation and implementation of the new knowledge generated (McGrath & MacMillan, 2000). This argument highlights the importance of exploitation strategies to translate the new ideas into marketable products and services (Crossan & Berdrow, 2003). In this juncture, Crossan and Berdrow (2003) state that the success of firm's explorative and exploitative insights is depend on effective learning at all firm levels.

Recent studies provide some insights to support the association between learning and exploration and exploitation activities (Covin et al, 2006; Macpherson & Holt, 2007). Wu and Shanley (2009) show that firm's knowledge stocks play an important role in promoting firm's explorative and exploitative strategies which leads to competitive advantages. Covin et al (2006) suggest that small firms require developing awareness about strategic processes to improve their performance. They further argued that since entrepreneurial actions are generally risky and often fail, learning from such experiences would direct firms to make changes where necessary to make future efforts successful. Entrepreneurs who are able to learn from their strategic actions and outcomes are also more likely to respond to truly novel market opportunities (Macpherson & Holt, 2007; Hatch & Dyer, 2004; Jayathilake & Jameel, 2013). These empirical results suggest that strategic entrepreneurship requires specific learning capabilities to exert positive performance effects.

Hypothesis II (H₂): Learning capabilities are positively associated with strategic entrepreneurship in SMEs.

2.3 Strategic competitive response capabilities and strategic entrepreneurship

Small firms are often criticized for being preoccupied with the present strategies and lacking of long term planning. However, research argues that specificity characteristics

of small firms including simple structure, owner dominance decision making and informal planning and controlling activities promote those firms for quick response to the environmental changes. As such, SMEs are occupied with various kinds of strategic capabilities within and outside of their firms. In strategic decision making, entrepreneurs are assumed to combine their different firms' activities and opportunities and decide upon functional links and invest in resources. Within this context, strategic decision making is considered as one of dynamic capabilities in the small firms. These decisions shape current strategies and choose the major strategic movements for the firms (Eisenhard & Martin, 2000;). The strategic decision making sets the vision to give a coherent picture that shows where firm wants to go and what the firm will look like in the years to come (Helfat & Peteraf, 2003). As such, strategic decision making sets course of actions that facilitate the expected strategic movement of the firm. The strategic decision making is centered on ensuring balance the continuity of current strategies with making changes that are necessary for future advantages. The empirical literature on strategic orientation of the entrepreneurial firm also provides sound evidence that small firms' strategic behavior highly influence towards their search for opportunities and exploitation of those opportunities in effective manner (Webb et al. 2010; Barringer & Bluedorn, 1999). These evidences are sufficient to hypothesize strategic competitive responses capabilities leads to promote opportunity strategic entrepreneurship in SMEs.

Hypothesis V (H₅): Strategic competitive response capabilities have a positive impact over strategic entrepreneurship in SMEs

3. METHODOLOGY

The empirical investigation was fundamentally laid on the survey carried out in the SMEs sector with use of a questionnaire which was

specially designed for present study. A number of measures were taken into consideration in selection of the sample as well as designing of the questionnaire to ensure the quality of data and research outcome in terms of validity and reliability.

In an effort to investigate the underline relationship empirically, this study operationalized a composite, unified measure of dynamic capabilities which integrates their constituent dimensions. In doing so, a multidimensional constructs composed of three interrelated, although instinct dimensions; coordination and integration capability, learning capability and strategic competitive response capability were used and developed to measure the dynamic capabilities. The respondents were asked to indicate the extent to which the particular capabilities constitute in their firms on a five point Likert type scale ranging from 1 to 5 (1 = completely disagree, 5 = completely agree). These three constructs were treated as the latent variables for the study. The reliability test revealed good Cronbach alpha values of 0.822, 0.849 and 0.772 for each construct respectively. A nineteen items inventory on a five point Likert type scale was used and developed for this purpose. The scale ranges from 1 to 5, 1 = completely disagree, 5 =

Table 4.14.1 provides a detailed breakdown of the sample by the gender of the respondents and types of businesses.

completely agree, and higher score indicates a higher degree of strategic entrepreneurial ability. The variable is measured as a latent construct since there is lack of properly identified indicators for measuring the underline phenomenon. However, some studies (Lumpkin & Lichtenstein, 2006; He & Wong, 2004) pave a basis for this construction. The reliability analysis is resulted an acceptable Cronbach's alpha coefficient of 0.890 for the construct.

The data analysis techniques were carefully selected and utilized in order to ensure the trustworthiness and usefulness of the results. Construct validity of the all constructs were initially assessed using the confirmatory factor analysis (CFA) as suggested by the Structural Equation Modeling (SEM). Subsequently bi-variate and structural model were performed using the SPSS and SEM in AMOS and hypotheses then were then tested with associated results.

4. RESULTS AND DISCUSSION

The sample of the study consists of 488 SMEs from manufacturing sector in Sri Lanka. Data were collected from the owner managers of the selected SMEs by using a questionnaire that was principally designed for the present study.

Table 4.1: Sample profile by gender and type of business

Type of business	Gender		Total	%
	Female	Male		
Foods & beverages	67	84	151	30.9
Apparel products	86	69	155	31.8
Furniture & wood products	19	53	72	14.8
Metal & related products	11	50	61	12.5
Paper & printing products	6	29	35	7.2
Chemicals & rubber products	2	12	14	2.9
Total	191	297	488	100.0

As shown in

Table 4.1, the majority of the respondents were male entrepreneurs (60.1%). With respect to the industrial activities, the majority of the firms have been centered the apparel products (31.8) and food & beverage products (30.9%) manufacturing activities. A substantial number of businesses (14.8%) involve with manufacturing of furniture and wood related products. Other firms are engaged in metal related production (12.5%), paper and printing works (7.2%) and chemical and rubber production (2.9%). Although gender representation of the business activities show that both male and female similarly involve in each of business activities, there is

Table 4.2. The result reveals that resource integration and coordination capabilities is positively correlated with strategic entrepreneurship ($r = 0.679$, $p < 0.01$). Likewise, entrepreneurial learning capabilities is also positively correlated with strategic

tendency that female are highly engaged in the apparel related activities.

This study conceptualized dynamic capabilities into three distinctive capabilities; resource integration and coordination capabilities (RICC), entrepreneurial learning capabilities (ELC), and strategic competitive response capabilities (SCRC). The study then proposed that each of these capabilities is positively with strategic entrepreneurship. The correlation analysis was used to find whether empirical data of the study support for these hypotheses. The relevant results are shown in entrepreneurship in power of $r = 0.469$, ($p < 0.01$). Moreover, a positive relationship is also found for the relationship between strategic competitive response capabilities and strategic entrepreneurship ($r = 0.556$, $p < 0.01$). This result stresses the importance of these dynamic capabilities in promoting strategic entrepreneurship in SMEs.

Table 4.2: Result of correlation analysis

Variable	A	B	C	D
A. Resource integration and coordination capabilities	(3.76)			
B. Entrepreneurial Learning capabilities	0.683**	(3.49)		
C. Strategic competitive response capabilities	0.781**	0.540**	(3.63)	
D. Opportunity exploration	0.679**	0.469**	0.565**	(3.75)

Note: **: Correlation is significant at the 0.01 level, * - correlation significant at 0.05, () : mean

The structural model shown in Figure 4.1 shows the proposed relationship between the dynamic capabilities and strategic entrepreneurship in way of a path diagram. The three constructs for the dynamic capabilities (RICC, ELC and SCRC) are the exogenous variables in the model. The construct of strategic entrepreneurship is the endogenous variable of the model. The model fit indices indicate that χ^2 value of 1387.31 is significant < 0.001 , absolute and incremental fit indices evident a better fit of the model. In fact, GFI value of 0.967, as an absolute fit,

signifies that the model has a good improvement over the based model. Moreover, absolute fit indices of RMSEA and RMR are reported the value of 0.047 and 0.023 and indicates that the reasonably fit of the model. In addition, incremental indices of NFI and CIF are reported value of 0.968 and 0.982 respectively. These all values are in well above the general cutoff criteria of 0.95 and confirm that model fit is reasonable. Other two indices, IFI and TLI are also received decent values (0.983 and 0.950) over 0.95 and further confirm the outcome of other indices.

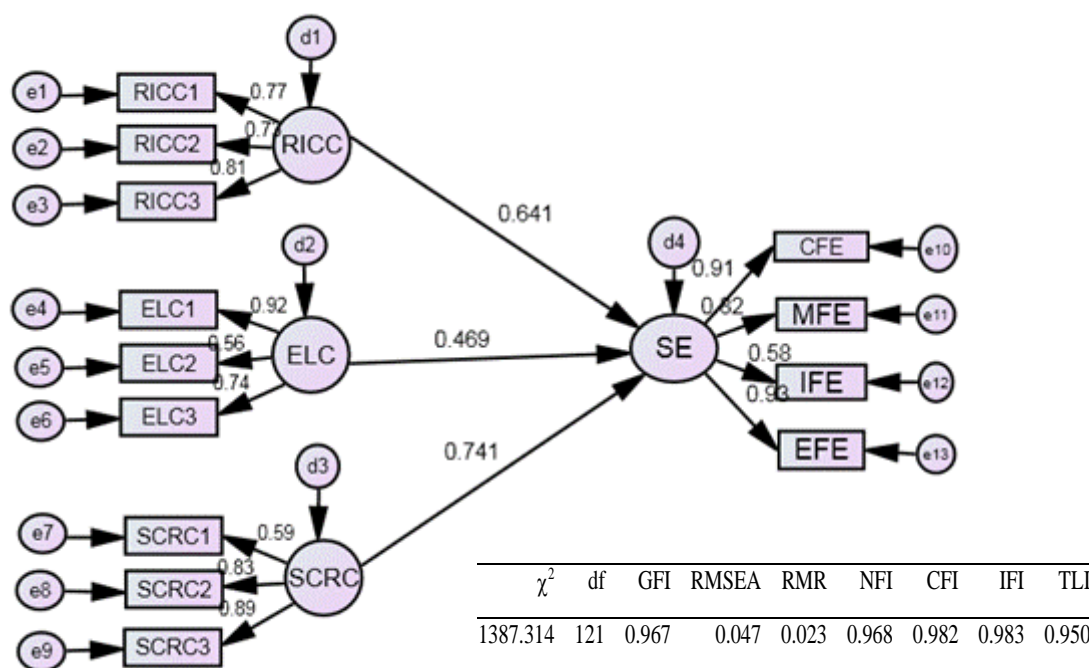


Figure 4.1: Structural model

Table 4.3: Results for the structural model –Direct effect

Path	SRW	p
Resource integration and coordination capabilities (RICC) ---> Strategic Entrepreneurship H_1	.641	***
Entrepreneurial Learning capabilities (ELC) ---> Strategic Entrepreneurship: H_2	.469	.047
Strategic competitive response capabilities (SCRC) ---> Strategic Entrepreneurship H_3	.741	***

Note: *** $p < 0.001$

Table 4.3 reproduces the results for path estimates and their p-values. p -statistics associated with standardized estimates show that path estimates are significant at as a minimum 0.05 level. The standardized estimates are consistent with the proposed relations with not only the statistical significance but in the expected directions as well. Thus, the results support the all the hypotheses of the study.

4. CONCLUSION

This study aimed to explore the dynamic capabilities that promote strategic entrepreneurial actions in SMEs. A review of dynamic capability literature helped to find three kinds of dynamic capabilities which essentially promote and encourage strategic entrepreneurship process in SMEs. Those capabilities are termed as resource integration and coronation capabilities, entrepreneurial learning capabilities, strategic competitive response capabilities. The study found that dynamic capabilities are most influential in driving the firm’s strategic entrepreneurship, by being exposed to internal and external

environments that heighten their ability for opportunity identification and exploiting, by balancing the process, speed and efficacy of decisions. The study confirms a close association between dynamic capabilities and strategic entrepreneurial action in SMEs. The study thus encourages SMEs to create and develop dynamic capabilities, not only because it sustains their livelihood over generations, but because it also assists in creating the firm's wealth.

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