ABSTRACT

SMEs are the main engine of economic growth and development after oil and gas sector in Nigeria. However more than 50% of them fail within the first three years of their formation owing to the complex and rapidly changing business environment. The role of dynamic capability in addressing these trends and sustaining firm’s performance is a contentious issue among scholars. Therefore, this study examines the relationship between dynamic capabilities and competitive advantage among SMEs in Lagos, Nigeria. Three hypotheses were formulated and tested using correlation and regression statistical techniques on data collected from 400 study participants through questionnaire survey design and simple random sampling technique. The correlation analysis showed no significant relationship between adaptive capability competitive advantage. However, the correlation result showed absorptive capability have a significant positive relationship with competitive advantage; and same for innovative capability and competitive advantage. The regression analysis showed that each of the three dimensions made statistical significant contribution to the predictive variable. The regression analysis further showed that the predictor variable (dynamic capability) contribute 27% to competitive advantage among SMEs in Lagos. The study suggested that firms should identify which dimension of dynamic capability will enhance and sustain their competitive advantage as the relevance of each dimension vary among firms and industries.

Key words: Dynamic capabilities, competitive advantage, SMEs, environment.

JEL Classification: M10
INTRODUCTION

How business managers get things done has been a challenge since the evolution of man majorly because of the dynamic and complex nature of the business environment (Okon et al., 2018) which create uncertainty for businesses. Uncertainties interrupts plans and courses actions; and this has become a major source of concern for business entrepreneurs and other decision makers (Ebegbetale, 2021). Over the last three decades, uncertainty which is the changing nature of business environment has been characterised by shortened products life cycles, attendant consequences of globalisation, rapid rate of technological change and development, and glut industries (Zhou et al., 2019). Competing in an environment that is dynamic and full of uncertainty have been linked to the development of relevant capabilities (such as knowledge, resources and unique skills) (Appiah-Adu et al., 2018). Firms are being advised to look beyond production inputs and functions to appreciate how firms learn and use their assets to create and sustain competitive advantage in ways that are unique and difficult for competitors to replicate (Teece, 2017).

Two types of capabilities: ordinary also called necessary, operational or zero level capabilities and dynamic also called higher level capabilities have been identified in the literature (Rajagopal et al., 2018; Teece, 2017). Ordinary or necessary capabilities are for short term survival of firms while dynamic capabilities create, modify and/or extend ordinary capabilities. In other words, ordinary capabilities are needed by any firm who wants to be a player in an industry while dynamic capabilities differentiate a firm’s offerings from those of rivals in the industry. Teece (2017) notes that Ordinary capabilities are gaining attention but dynamic capabilities are gaining much more attention because strong dynamic capabilities help firms to address market changes, competitors’ actions and the general business environment. Dynamic capabilities can make organisations cope, react, and respond proactively to issues pose by a rapidly changing environment (Zhou et al., 2019).

The core issue in the discussion and debate on dynamic capabilities among scholars is whether they lead to competitive advantage which represents a situation where an organisation confronts the dynamism in the business environment by offering products or services that satisfy customers’ needs better than its competitors in the industry (Kaur & Mehta, 2016; Li & Liu, 2014). While some assume a direct impact, others contend such assumption, arguing that dynamic capabilities may not result in better performance or competitive advantage (Zhou et al., 2019). Thus, this paper examines if dynamic capabilities have any relationship with competitive advantage.
This study adopts an empirical approach and is conducted among small and medium enterprises (SMEs) that operate in Lagos State, Nigeria, a fast developing and largest economy in Africa. The choice of Lagos is borne out of its strategic position in the Nigerian, African and the world economy. Recent publications place Lagos, with a gross domestic product (G.D.P.) of $91 billion, as the largest economy by state categorisation in Nigeria, and the fifth in Africa (Babatunde, 2018; Banwo et al., 2017; https://lagosstate.gov.ng). It is located in Nigeria which is ranked among the first twenty five largest economies by GDP (Lawal et al., 2018; IMF, 2016). Of more worthy of note is that Lagos is the fifth largest city in the world (Ilesanmi, 2010). Tacitly, it is a first choice destination for investment. Hence, many of the characteristics of the business environment highlighted by Zhou et al. (2019) are dominant in this economy.

The choice of SMEs is informed by two factors: its contribution towards the Gross Domestic Product (GDP) of their respective countries and the stage many occupy in firm’s life cycle. SMEs promote private sector development and partnership, and are the main engine of economic growth and development in Nigeria (Ebitu et al., 2016). Oladele and Olayiwola (2018) put the contribution of SMEs to the GDP of Nigerian economy at 37% making it the second largest contributor after the oil and gas sector. Furthermore, while SMEs form the bulk of private businesses in Nigeria (Igwe et al., 2018), many have not reached the growth stage of firm’s life cycle when compared to their counterparts in developed countries owing to problems of infrastructure like stable power supply (Banwo, et al. 2017). While many have not left the initial or introductory stage, only between 5%-10% reach maturity (Igwe, et al., 2018). This study proposes that without the adoption of dynamic capabilities, the challenges pose by the complex and dynamic business environment will continue to threaten, weaken existing capabilities (Kaur & Mehta, 2017) of Nigerian SMEs which have a life cycle: introduction, growth, maturity and decline (Helfat & Peteraf, 2003).

Significant studies on the usefulness of dynamic capabilities in large firms have been conducted, however, limited knowledge exist on its relevance in smaller firms such as SMEs (Owoseni & Twinomurinzi, 2018). This study, therefore, intends to fill this gap by examining the link between dynamic capabilities and SMEs sustainable performance in the context of a developing economy like Lagos, Nigeria. Existing studies on dynamic capabilities in SMEs have mainly focused on chief executive officers (CEOs) of the firms (Annunziata et al., 2018; Teece, 2007; Helfat & Martin, 2015; Zhou et al., 2019), this study will include other levels of management hierarchy because they also play key strategic roles in the organisation. This study intends to contribute to extant literature by examining the dimensions of dynamic capabilities that are relevant to the competitive advantage of Nigerian SMEs in Lagos.
LITERATURE REVIEW

Dynamic Capability-based Theory

Dynamic capability as an idea was conceived by Teece et al. (1990) who in 1997 defined it as organisation's ability to build, integrate and reconfigure their internal and external competences that enable them to address the rapidly changing business environment. Dynamic capability is an off-shoot of resource-based view (Gutierrez-Gutierrez et al., 2018; Zaidi & Othman, 2012; Teece, 2007) which postulates that competitive advantage will only come when the resources and capabilities deployed are valuable, rare, non-imitable and non-substitutable (Barney, 1991 VRIN Framework). Consequently, the pursuit, development, deployment, and renewal of dynamic capabilities must incorporate the Barney’s (1991) VRIN model for sustainable competitive advantage.

In the past, differences in performance can be explained by knowing what the resources of an organisation are (i.e., Resource-Base View), however, addressing environmental changes in our contemporary time requires an understanding of what organisations can do with their resources (capability-based view). Staying relevance requires both operational capabilities for routine tasks and dynamic capabilities for high level skill activities (Stancu et al., 2020). Capabilities can be eroded in volatile markets (Salvato & Vassolo, 2018). However, the capability that can use resources and other capabilities to secure competitive advantage in an environment that is complex, dynamic and turbulent is the highest order capability or dynamic capabilities (Zaidi & Othman, 2012). Dynamic capabilities enable a firm to use its resources and capabilities to identify opportunities/threats and to exploit/neutralise them (Teece, 2017; Zhou et al., 2019) in an adequate and proactive manner (Appiah-Adu et al., 2018). Hence, Dynamic capability-based theory is relevant as it explains how firms can use their resources and competencies to exploit opportunities and neutralize threats.

Zhou et al. (2019) and Wang and Ahmed (2007) reported lack of empirical studies as well as theoretical framework to guide firms in using dynamic capabilities to achieve competitive advantage. The lack of consensus among scholars of dynamic capability studies on which mechanisms dynamic capabilities best influence firm's competitive advantage could be due to the main focus of the researchers on theoretical development (Zhou et al., 2019). Although there are different dimensions of dynamic capabilities, scholars consider adaptive, innovative and absorptive capabilities as the most important industry-level dynamic capabilities (Kaur & Mehta, 2017; Wang & Ahmed, 2007). At the macro-level, some studies have considered sensing, seizing, integrating and reconfiguring as important dimensions of dynamic capabilities when addressing opportunities and threats in the external environment (Lin et al., 2015). However, this study is looking at how a firm can achieve competitive advantage at the
industry level and the dynamic capability dimensions that address this are adaptive, absorptive and innovative (Kaur & Mehta, 2017; Wang & Ahmed, 2007).

Adaptive Capability focuses on how flexible and proactive firms are when coordinating and reconfiguring their resources, processes and structures to address sudden environmental changes in order to achieve their objectives (Owoseni & Twinomurinzi, 2018; Kaur & Mehta, 2017). Absorptive Capability focuses on how firms create, value and use new knowledge (Owoseni & Twinomurinzi, 2018; Lin et al., 2015) or external knowledge (Kaur & Mehta, 2017) to address the current environmental trend. Lin et al. (2015) highlights the four factors/processes of managing knowledge as acquisition, analysis, transformation/combination of existing and new knowledge, and exploitation or creating further new knowledge. Innovative Capability focuses on how creative and innovative behaviours that bring about better products and services, or convert risks to opportunities are encouraged within the firms (Owoseni & Twinomurinzi, 2018; Kaur & Mehta, 2017). Based on theory and argument, the following hypotheses will be tested in this study:

H$_1$: There will be a significant relationship between adaptive capability and competitive advantage Nigerian SMEs.

H$_2$: There will be a significant relationship between absorptive capability and competitive advantage Nigerian SMEs.

H$_3$: There will be a significant relationship between innovative capability and competitive advantage Nigerian SMEs.

Conceptual Framework

The researcher presented here a model (figure 1) that depicts the relationship between the predictors and the predictive in this study. Dynamic capability (adaptive, absorptive, and innovative) constitutes the independent variable of interest while competitive advantage constitutes the dependent variable.

Dynamic capability

![Conceptual model for the Study]
Relationship between industry-level dynamic capabilities and competitive advantage of Nigerian SMEs

**METHODS**

**Research Design**

The study employed cross-sectional research design since data collection involves a one-time observation of study variables.

**Sample**

The sample of the study consists of top, middle and first line managers from selected SMEs in Lagos State, Nigeria. SMEDAN (2017) defined SMEs as small enterprises if their staff strength ranges from 10 to 49 and medium enterprises if their staff strength ranges from 50 to 199. The agencies noted in their survey that 71,288 small businesses and 1793 medium sized businesses totalling 73,081 exist in Nigeria. For Lagos, the population of SMEs was put at 8,396 which was adopted for this study.

Since the entire population of SMEs in Lagos, Nigeria could not be included in the study, 478 SMEs were selected through simple random sampling technique. In determining the sample size, the formula presented in Yamane (1976) was used: \( n^* = \frac{N}{1+N(e^2)} \) Where: \( N = \) population size = 8396 SMEs in Lagos, and \( e = \) level of precision = 5% (at 95% confidence level). Therefore, \( n^* = \) sample size = 382 SMEs in Lagos. Due to attrition rate, the sample size was increased to 478 SMEs.

**Data Collection**

A questionnaire was employed as the data collection instrument for the study. Informed consent of the study participants were sought and their anonymity guaranteed. Out of the 478 copies administered, only 411 copies were returned and from which 400 copies were found useable. For a robust analysis, Hair et al. (2010) recommended a minimum threshold of 20:1 sample-to-variable ratio. Four variables were measured in this study and with a response rate of 400, the ratio of 100:1 obtained exceeded the recommended threshold.

**Measurement of Variables**

In order to determine whether dynamic capability sustains competitive advantage of Nigerian SMEs, a structured questionnaire (section A, B and C) was employed for data collection. Section A consists of socio-demographic variables. Section B includes an independent variable (dynamic capability: adaptive, absorptive and innovative) which were all assessed using existing scales from Kaur and Mehta (2017) study. The three measuring variables of dynamic capability: adaptive, absorptive and innovative respectively have three, five and five items which summed up to thirteen. Section C contains the dependent variable (competitive advantage) which was assessed using a five-item scale from Kaur and Mehta (2017) study. All
the measuring items summed up to eighteen and a 5 point Likert scale (strongly disagree (1) to strongly agree (5)) was used.

**Statistical analysis**

The data was analysed employing correlation and regression analysis with the aid of SPSS version 23 software. Correlation and regression analyses were used. Correlation according to Saunders et al. (2012) deals with the relationship between the variables of the study while regression show the degree of causation between these variables.

**Preliminary Analysis**

**Factor Analysis**

The eighteen measuring items were subjected to principal component factor analysis and their Kaiser-Mayer-Olkin (KMO) measure of sampling adequacy was 0.813 which was above 0.6 and acceptable (Allen & Bennett, 2010). For the individual items, all the KMO values were above the acceptable limit 0.5 (Field, 2013). The Bartlett's test of sphericity was 0.000 and statistically significant ($p< 0.001$) (Allen & Bennett, 2010). The value of the Chi-Square was 4329.081 while that of the degree of freedom showed 153. All the items were loaded into one common factor and 4 factors showed eigenvalues of over Kaiser's criterion of 1 which together explained 31.741% of the variance. This suggested that common method of bias did not affect the data and that the research instrument was fit (i.e. 31.741% < 50% cut-off point). After rotation, the factor loadings presented items that cluster on the same factor. Factor 1 stood for absorptive capability, factor 2 represented competitive advantage, factor 3 innovative capability, and factor 4 adaptive capability.

**RESULT AND DISCUSSION**

The result of the bivariate correlation analysis is shown:

| Variables | Mean | Standard Deviation | 1  | 2  | 3  | 4  |
|-----------|------|--------------------|----|----|----|----|
| CA (1)    | 3.69 | .846               |    |    |    |    |
| AdC (2)   | 4.20 | .700               | .001| 1  |    |    |
| AbC (3)   | 3.86 | .936               | .389**| .159**| 1  |    |
| InC (4)   | 4.34 | .412               | .307**| .275**| .224**| 1  |

**P<0.01 level (2-tailed).**

CA: Competitive Advantage; AdC: Adaptive Capability; AbC: Absorptive Capability; InC: Innovative Capability.
Hypothesis one states that there will be a significant relationship between adaptive capability and competitive advantage. From the result of the analysis depicted in table 1 above \((r = .001; \ p > 0.01)\), the hypothesis is rejected. This implies that the predictor variable (adaptive capability) does not have any significant relationship with the predictive variable (competitive advantage).

Hypothesis two states that there will be a significant relationship between absorptive capability and competitive advantage. Based on the result from the analysis depicted in table 1 above \((r = .389; \ p < 0.01)\), the hypothesis is accepted. This means that the predictor variable (absorptive capability) has a significant relationship with the predictive variable (competitive advantage).

Hypothesis three states that there will be a significant relationship between innovative capability and competitive advantage. Based on the result from the analysis depicted in table 1 above \((r = .307; \ p < 0.01)\), the hypothesis is accepted. This implies that the predictor variable (innovative capability) has a significant relationship with the predictive variable (competitive advantage).

| Hypotheses | Decision |
|------------|----------|
| H1 \(\text{AdC} \rightarrow \text{CA}\) | Not supported |
| H2 \(\text{AbC} \rightarrow \text{CA}\) | Supported |
| H3 \(\text{InC} \rightarrow \text{CA}\) | Supported |

\(\text{CA}\): Competitive Advantage; \(\text{AdC}\): Adaptive Capability; \(\text{AbC}\): Absorptive Capability; \(\text{InC}\): Innovative Capability.

Regression Analysis
Furthermore, a multiple regression analysis was done.

**Table 3: Regression Table**

| VARIABLES              | B    | Beta  | t     | Sig  | R     | R Square | Adjusted R Square | F      | Sig    |
|------------------------|------|-------|-------|------|-------|----------|-------------------|--------|--------|
| Constant               | .770 | 1.834 | .067  |      |       |          |                   |        |        |
| Adaptive Capability    | -.154| -.127 | -.2736| .006 | .466a | .217     | .211              | 36.567 | .000b  |
| Absorptive Capability  | .317 | .350  | 7.635 | .000 |       |          |                   |        |        |

\(a\): Significant at \(p < 0.05\); \(b\): Significant at \(p < 0.01\).
A preliminary test was first conducted to ensure that the assumptions of normality, linearity and homoscedasticity were not violated in this study. This was followed by a multicollinearity test to check for any absence of correlation among the independent variables and the following VIF: 1.094, 1.064 and 1.122 were obtained for adaptive, absorptive and innovative capability respectively. This means that there is no problem of multicollinearity as all the values fall within the range recommended by Hair et al. (2006). According to them, a VIF of 0.10 or below and a VIF of 10 or above indicate high collinearity. Then the study proceeded to the actual analysis and the results depicted in table 2 above.

The above table 2 showed the independent and joint effect of the adaptive, absorptive and innovative capability on competitive advantage. The R value for the model is 0.466, the R² is 0.217. This implies that the dimensions of dynamic capability: adaptive, absorptive and innovative capability jointly accounted for a variation of 22% of the total variance in competitive advantage. The other variables that constitute 78% were not considered in this study. The ANOVA performed indicated (F- ratio = 36.567; p< 0.000), implying that the probability of these results occurring by chance is less than 0.001.

The results also show how each dimension of dynamic capability contributed to competitive advantage. Absorptive capability (beta = 0.350; t= 7.635; p<0.005) and innovative capability (beta =0.263; t=5.590; p<0.05) both made unique statistical contribution to the predictive variable (competitive advantage). This is closely followed by adaptive capability (beta =-.127; t=-2.736; p<0.05) which also made a statistical significant contribution to the predictive variable (competitive advantage).

CONCLUSION, MANAGERIAL IMPLICATIONS, LIMITATION AND FUTURE RESEARCH

This study primarily examined the link between dynamic capability and competitive advantage among SMEs in Lagos, Nigeria. To determine this relationship, three important industry-level dimensions of dynamic capability were considered and their impacts on competitive advantage were assessed by formulating three hypotheses which were tested using bivariate correlation and multiple regression techniques.
The result of the correlation analysis of hypothesis one showed that adaptive capability does not have a significant relationship with competitive advantage among SMEs in Lagos, Nigeria. However, the regression result showed that adaptive capability made a statistical significant contribution to the predictive variable. This is not surprising as findings from previous studies also revealed that the significant contributions of adaptive capability to competitive advantage vary from firm to firm and from industry to industry (Kaur & Mehta, 2017). This implies that before any resources is deployed to the development of any component of dynamic capability, its relevance to the firm or industry, or ability to use such capability, should be ascertained.

The result from the correlation analysis of hypothesis two confirmed a significant positive relationship between absorptive capability and competitive advantage. The regression analysis also reported that absorptive capability made a unique statistical contribution to the predictive variable. This finding is supported by Owoseni and Twinomurinzi (2018) who found that absorptive capability help SMEs to address trends in the business environment. This implies that appropriate use of new or external knowledge from the business environment can sustain competitive advantage.

Furthermore, the correlation analysis of the third hypothesis showed a significant relationship between innovative capability and competitive advantage. This is also in line with that of the regression analysis. This finding is also confirmed by Kaur and Mehta (2017). In their case, innovative capability made the highest contribution to competitive advantage.

Finally, the primary objective of this study is to find out if any significant relationship exists between dynamic capability and competitive advantage. The results from the analysis found that most of the dimensions of adaptive capability have significant relationship with competitive advantage. The analysis further revealed that each of the dimensions made significant statistical contribution to competitive advantage of SMEs in Lagos. Based on these, the study infer that dynamic capability significantly impacts competitive advantage. This finding is in line with Li and Liu (2014) who also found that dynamic capabilities significantly impact competitive advantage.

**Conclusion**

The dynamic nature of business environment affects the survival, performance, strategies, and sustainability of SMEs in Lagos, Nigeria. To address the threats and opportunities pose by this environment at the industry-level, firms can adopt adaptive, absorptive, and innovative dimension of dynamic capability. The impacts of these predictors on competitive advantage among SMEs in Lagos were examined. The regression results showed that adaptive,
absorptive and innovative capability all made statistical significant contribution to competitive advantage. However, in other economies or contexts, existing studies have shown that the relevance of each dimension vary from firm to firm, sector to sector, and industry to industry. The practical implication of this is that firms should endeavour to identify which dimension(s) enhances and sustains their competitive advantage before committing their scarce resources to its development and adoption.

**Recommendation**

The study recommends that aside C.E.Os, other levels of management in the organisation should be involved in the identification, development and adoption of dynamic capability. The systemic view of a firm recognises the contribution of the various subsystems, units or departments that are headed by other managers who have found unique ways to getting things done effectively and efficiently. Imputing these technical know-how, skills, and internal capability to the development of organisational dynamic capability will make it unique, valuable, and difficult to imitate.

**Suggestion for Further Study**

All the dimensions of dynamic capability cannot be treated in this study. It is therefore suggested that macro-level dimensions of dynamic capability be considered in future studies. Also, this study is limited to SMEs in Lagos. A larger population like SMEs in Nigeria or another developing economy may be considered for future direction.

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