

## **Firm-Level Strategy, Capabilities and Performance of Food and Beverage Manufacturing Companies in Kenya**

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*Manufacturing companies operate in a dynamic environment and require to continuously cultivate firm-level strategies for performance improvement. Currently, the main discussion in social sciences has centred on the links between firm-level strategy, capabilities and performance with varied result. To investigate this connections, we gathered and analysed data from 125 Large-Scale Food and Beverage Manufacturing Companies (FBMC) in Kenya. The study covered a two year period. The paper tested the hypothesis that firm capabilities have a significant effect on the relationship between firm-level strategy and performance using regression analysis. The results supported the hypothesis with human capital and research exhibiting the highest moderation. These findings will contribute to government policy development for the sector's expansion and competitiveness and management practises on resource utilization.*

**Key Words:** Firm-Level Strategy, Capabilities and Firm Performance

### **1. Introduction**

Scholarly explorations in strategic management over the recent two decades has demonstrated that success in firm performance does not depend upon a single indicator but upon several factors (Aosa, Bagire & Awino 2012). It is argued that firms with clear and competitive strategy will outdo those without such a strategy (Porter 1996). Firm-level strategy is a process of ensuring firm sustainable competitive edge through development of key capabilities that gears long-term performance (Lin, Tsai & Wu 2014). Organizational performance is directly affected by strategies that are implemented by the business in order to produce supernormal profits (Bowman & Toms 2010).

Firm capabilities is organization's power to reconfigure, integrate, and build company and industry competencies that meet and adapt to the fast shifting surroundings (Teece, Piano & Shuen 1997). Capabilities are core competencies of a factory and are essential to the company. In instances where these capabilities are deficient, firm-level strategy will not attain desired outcomes (Hamel & Prahalad 1990). Firm capabilities are generally grouped as physical and intellectual assets. Tangible assets are human, financial or infrastructure while intangible assets include reputation, know-how or patents (Aosa, Bagire & Awino 2012). Grant (2003) classified capabilities as financial resources, physical resources, human capital, technological resources, marketing, automation and research and development. This paper applied this indicators in evaluating the impact of capabilities on firm-level strategy and performance relationships.

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Firm capabilities stem from resource-based perspective which emphasizes on firm having specific capabilities, assets and presence of differentiating mechanism as the chief influencer of performance (Wernerfelt 1984). Therefore, capabilities are simply organization abilities to combine resources for superior performance (Pearce, Robinson & Mital 2012). Occasionally, resources are reconfigured, coevolved, coordinated and reorganized for proper exploitation in strategy implementation (Teece, Piano & Shuen 1997). Firm capabilities are naturally limited and their prudential application is usually a goal focus of every company. Firm's possession of strong capabilities enables it to readjust and adapt to volatile markets and environmental uncertainties and changes (Teece, Piano & Shuen 1997). Organizational performance variations are a function of capabilities and strategy (Eisenhardt & Martin 2000). The focal task for firms is on how to guarantee active regulation of their current capabilities while concurrently developing new ones.

The research problem for exploration was the existing empirical contradictions on the constructs that determine firm performance within theorists and researchers (Pearce & Robinson 2010; Murgor 2014). According to Awino (2011), the autonomous effect of core competencies, capabilities, and strategy execution on organizational performance was weaker when contrasted to the collective stimulus of the same variables. Other studies focused on developed economies (Pearce & Robinson 2010; Karlsson & Tavassoli 2015) which were done in different contexts and their results and suggestions cannot be replicated to operations in developing markets like Kenya without modifications. Hence, the artifact attempts to ease the knowledge gap in the inadequate empirical studies on corporate strategy, capabilities and performance of FBMC in Kenya.

Dynamic capabilities theory (DCT) will immensely benefit from the arguments on firm-level strategy, capabilities and performance. The results will assist the Kenyan government in formulating policies for the sector meant to multiply its performance and competitiveness. This will increase revenue and generate occupations that reduces national unemployment index and aid in the fulfillment of Vision 2030 goal of transforming Kenya into an industrialized second world status. This paper is organized into five divisions. Section two highlights empirical studies which formed the conceptualization and contextualization of the research. The third subdivision illustrates the research methodology adopted in the study; the design, population, respondents and analytical tools. Section four focuses on the outcomes of the inquiry and interpretations. Section five covers conclusion, recommendations, limitations and areas for further studies.

## **2. Literature Review**

Dynamic capabilities theory (Teece, Piano & Shuen 1997) anchored this paper. DCT is rooted in the Resource Based View (RBV) which postulates that capabilities are company's capacity and abilities to assign resources (Wernerfelt 1984). The exercise is usually in a fabrication of company's processes, procedures and demands. DCT viewpoint on performance often aims to comprehend firm development and survival abilities (Pearce & Robinson & Mital 2012). The value created pivots on how resources are combined within the company. Capabilities emerge due to firm's repeated practices and routines captured in venture models that go back decades and are hard to imitate (Rugami 2013). Teece, Piano & Shuen (1997) extended RBV to formulate dynamic capabilities viewpoint that emphasises on organizational processes which employ firm resources.

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DCT approach to strategy evolved from resource application in generation of firm's core competencies (Lopez 2005). Dynamic capabilities are intangible internal resources which are idiosyncratic: unique to every company, inimitable and grounded in the company history (Rothaermel 2008). Dynamic capabilities are strategic routines through which firms procure new resource arrangements as markets evolve, split, collide and die (Johnson & Scholes 2005). It is observed that repeated practices detonate to the gradual development of dynamic capabilities, the categorization of that experience into technology. In addition, formal procedures reduce the difficulties to apply and accelerate in building routines and systems of effective capabilities but dependent on market dynamism (Eisenhardt & Martin 2000).

The emphasis of DCT is on firm's ability to appropriately adapt, integrate and rearrange internal skills, resources and operational competences to equal the needs of a dynamic surrounding (Rothaermel, 2008; Rugami, 2013). Thus, company differentiation in performance is dependent on how it maximizes its critical capabilities and not mere ownership of resources. The bottom-line of DCT is that, output is enhanced when companies are keen to recombine, coevolve, reconfigure and reallocate resources as their wants change (Aosa, Bagire & Awino 2012). Critics of the theory contend that dynamic capabilities are crucial but not enough in themselves for performance improvement (Eisenhardt & Martin 2000). A side from recognizing the theory's contribution; the scholars argue that by combining resources on learned processes and activities; the theory has nothing different from RBV preposition. Nevertheless, the theory guided the conceptualization of the moderation role of firm capabilities.

Hamel and Prahalad (1990) argued that, the critical task of the executive is to grow ventures capable of generating products needed for consumption. Firm's package of assets are reconfigured to become the company's core and distinctive competences. For a business to last and flourish in a competitive environment, requires to own definite levels of capabilities. The selection of firm-level strategy to be explored is directed by legitimizing pressures and threats/opportunities in the imminent enterprise environment (Johannesson & Palona 2010). For a company to maximize its production and competitiveness, it requires to align its strategy and competences to its exterior environs (Ansoff & Survillan 1993). In contrast, Murgor (2014) opined that the selection of a plan is not directly influenced by existing capabilities and there was lack of linkage between outer surroundings and strategic choices.

Organizations that select and afford to concoct a conglomeration of strategies are in a better standings for long-term performance when equated to those who elect not to or adopt only one strategy (Tavassoli & Karlison 2015). Conversely, Newbert (2008) argued that even if a company possesses resources that have the potential to create cutting edge performance, the full actualization will not be realized if the firm lacks capacity for capabilities exploitation. This process involves creation and execution of strategies for performance improvement. Nevertheless, Mintzberg, Ahlstrand & Lampel (2005) argued that it was really hard to get strategy right, since it is difficult to develop strategy in a speculative environment which emerge as intentions fusion with and accommodate to a changing reality. This explains why scholars have not settled on a collective ground on what constitutes key concepts for performance.

The premise of RBV is that companies must base their strategic choices on a solid set of assets that can produce complicated capabilities that give superior performance (Amit & Schoemaker 1993). Firm's competitive edge is acquired with a sustainable and consistent

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exploitation of core capabilities not just product and market portions (Grant & Jordan 2012). Organizational structure, whose edifice are the people, as a design of communication and relations among a group of talents, including the practice of formulating and effecting decisions as a major contributors of firm sustainable competitive advantage in Kenya (Mutunga, Minji & Gachanja 2014). Though, the study failed to conceptualize firm-level strategy, capabilities and organizational performance.

Firm capabilities assure sustainable competitive edge and long-term performance because new competences are always assured as markets collide, emerge, merge, separate, and liquidate (Eisenhardt & Martin, 2000). Resources can only generate superior performance if coupled with proper collocations, reconfigurations, mixture, gradual development, production and synergy (Newbert 2008; Aosa, Bagire & Awino 2012). Capabilities allow activation and redirection of a complex framework of economic and organizational factors. Hence, capabilities are key in optimizing strategic course of the firm's future (Lopez 2005). However, irrespective of how good capabilities might be, they cannot stir economic progress if the firm does not excel in acquiring resources and expanding them through strategic course (Makadok 2001). It follows that, differences in performance may resonate from how differently organizations mix capabilities in strategy formulation. Conversely, the studies did not demonstrate independent capabilities moderation on firm-level strategy and performance in FBMC.

Empirical proof shows that possession of treasured, exceptional and inimitable resources leads to superior performance (Zollo & Winter 2003). Hence, creating a strategy constructed on unique capabilities provides a sophisticated competitive edge and high performance. Firm capabilities unlike ordinary resources are idiosyncratic to every organization and are deep-rooted in its history. Resource possession could only lead to performance improvements if they are converted into productive use, although in other firms they are a cause of poor performance due to costs associated in preserving them (Tokuda 2005). Intangible resources contributes more prominently to firm performance when paralleled to tangible resources. (Kamasak 2017). In contrast, the researchers argue that it is hard to separate the software and hardware of capabilities as they are intertwined. The paper therefore, focuses on the combined effect of distinct capabilities on corporate strategy and organizational performance connections.

Kamasak (2017) concentrated on the general category of tangible and intangible resources and firm performance. To address this limitation the paper investigates capabilities using sub-categories of human resources, marketing capabilities, automation, capabilities, research and development and information technology. Additionally to engagement of highly qualified human capital is the need to have training programmes that sustain these talents (Kale 2010). Firm's talent development to support strategy necessitates attitude transformation so that workers share similar dream and mission of the venture (Ulrich & Lake 1990). Kidombo (2007) expounded that soft and hard talent management have a strong bearing on firm output. Subsequently, Lopez (2005) posit that capabilities are dire in escalating the accomplishments of a given organization. Conversely, this previous study observed the direct rapport of employees' asset management and productivity but ignored the indirect control of employee capital on firm-level strategy and performance.

To grow market share, enterprises have to introduce modern products with certain marketing capabilities. Advertisement is important to the realization of a firm's market share and a massive monetary success (Kanibir, Saydan & Nart 2014; Nalcacia & Yagci 2014). Firm's

product generation capabilities, stimulates the launch of strategy for a long-lasting product that is consecutively improved over time (Kor & Mahoney 2005). Advertising capacity also promotes international growth of new ventures by impacting firm's decision to select penetration modes including higher capital outlets in worldwide markets (Ripolles 2011). Grounded on these arguments, the study advises for exploration and exploitation of international markets as they positively arbitrate marketing and product development. Marketing competences are also functioned under appropriate managerial expert.

Bharadwaj (2000) posit that technological capabilities is the ability of a company to rally and deploy IT based resources together with other capabilities. Moreover, there is proof that installation of technology in project designs and industrial systems, forms a fundamental fragment of the innovation cycle and accelerated product innovation (Chrowman, Pries & Sara 2017). IT grounded assets consists of technical and managerial know-how, intangible IT- programmed resources such as expertise, assets, client orientation and cooperation. Subsequently, firm capabilities detonate to the capacity of the organization to pool resources and stimulate higher performance (Amit & Schoemaker 1993). Thus, the joint effect of core competencies, capabilities, strategy, and strategy operationalization is comparatively stronger than their separate effect (Murgor 2014). Nonetheless, the study did not evaluate the individual effect of capabilities on firm-level strategy and performance.

Performance improvement of FBMC in Kenya is vital to the fiscal growth of the country as this will ensure increased incomes and employment to the rural population (KIPPRA 2013). It is on this premise that their performance continues to be a key priority to the Government of Kenya, strategic management practitioners and researchers. Despite of previous inquiries on the liaison of capabilities, strategy and performance in FBMC (Murgor 2014; Mutunga, Manji & Gachanja 2014; Tavassoli & Karlison 2015; Kamasak 2017), the connections of firm-level strategy, capabilities and performance, still remains an area of interest as there is flimsy information on how this variables are connected.

The paper endeavours to offer solution on research question as to whether firm capabilities affect firm-level strategy and performance connections that still remains unclear in literature. Therefore, constructed on this limitations in scholarly works, the objective of this study was to determine the effect of capabilities on the link amongst firm-level strategy and performance of FBMC in Kenya.

*H<sub>1</sub>. Firm capabilities have a significant effect on the relationship between firm-level strategy and performance of food and beverage manufacturing companies in Kenya.*

### **3. Methodology**

The study applied cross-sectional survey design. Cross-sectional survey employs quantitative methods in their evaluation. The justification of the methodological approach was the objective of the study. The study goal was to expound capabilities, firm-level strategy and performance relationships. Before testing this connection, the researchers established the manifestations of the selected capabilities (using one sample t-tests). Study capabilities indicators were human capital, marketing, automation, research and development and information technology. The data was collected through a census of 178 large-scale firms that are active members of Kenya Association of Manufacturers (KAM) by 2016.

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A census sampling was justifiable owing to the decline in total population. The study was for a two year period running from January, 2016 - December, 2017. The key respondents were the Chief Executive Officers/ Managing Directors of sampled companies. These senior executives were chosen for the study because firm attributes to be tested are best known to them. In Kenya, FBMC are classified under the manufacturing sector which is a crucial industry of the economy contributing about 10% of Gross Domestic Product (GDP) with agro-processing accounting for 3% (KIPPRA, 2014). Manufacturing sector employ nearly 300,000 people which accounts for 13% of the Kenyan employment index. It has been ascertained that the industry's share to the GDP registered a decline trend of 13.9% in 2008, to 9.2 % in 2012. The sectors proportion to the wage employment has also gradually declined from 13.9% in 2008 to 12.8 % in 2012 (KIPPRA, 2014). The degeneration in growth of this sector is attributed to a fusion of many factors like, high rising costs of food, wage bills, increased establishment costs, competition from industry players of Common Market for Eastern and Southern Africa States (COMESA) and tightened bank loan requirements.

For data analysis the paper utilized hierarchical regression analysis and presented the results using inferential and descriptive statistics. The hypothesis of the study was framed as *H1. Firm capabilities have a significant effect on the relationship between firm-level strategy and performance of FBMC in Kenya.* To test this hypothesis, the individual effect of capabilities and firm-level strategy on each performance indicator was first determined. For the overall effect of capabilities, firm-level strategy composite index was regressed on financial performance. The relationship of Firm Performance (FP), firm-level strategy (FLS) and firm capabilities (FC) is as follows. Model:  $FP = \beta_0 + \beta_1 X_1 + \beta_2 X_1 * X_2 + \varepsilon_2$ . Where  $\beta_0$  is the constant and  $\beta_1$  and  $\beta_2$  are the coefficient slope or gradient for FLS and FC respectively and  $\varepsilon$  is the error term.

## 4. Findings

The results of independent effect of capabilities on firm-level strategy and performance relationships are depicted in Table 1.

**Table1: Regression of Firm Capabilities on Financial Performance**

Model	Unstandardized		Standardized		Sig.	Tolerance	V.I.F.
	B	Std Error	Beta	T			
1 (Constant)	.24			3.06	.00		
Human Capital	-.21	.05	-.31	-4.05	.00	.38	2.66
Marketing capabilities	-.222	.06	-.31	-4.06	.00	.38	2.67
Manufacturing automation	-.14	0.05	-.13	-2.49	.01	.87	1.16
Research and development capabilities	.19	.06	.17	3.14	.00	.80	1.25
Information technology capabilities	-.19	.05	-.29	-3.97	.00	.38	2.66

a. Dependent variable financial performance

The results in Table 1 with  $p\text{-value} \leq 0.05$ , reveals that all the indicators that tested capabilities on performance were statistically significant. The overall regression model for this study was:  $Y = 0.24 - 0.21HC - .22MC - .14MA + .19RD - .19IT$ . Founded on the statistical significant beta coefficient values ( $p < 0.05$ ) for the moderation consequence of firm capabilities on the

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relationship between the independent and dependent variables; the alternate hypothesis that firm capabilities have a significant effect on the linkages amid firm-level strategy and performance of FBMC in Kenya was supported.

The results indicated that firm capabilities have a significant influence on the correlation between firm-level strategy and performance. The findings of interaction influence of capabilities on firm-level strategy and financial performance are offered in Table 2.

**Table 2: Effect of Capabilities on Firm-Level Strategy and Performance**

Model Summary					
Model	R	R <sup>2</sup>	Adjusted R <sup>2</sup>	Std. Error of the estimate	
1	.78 <sup>a</sup>	.65	.48	.25	
ANOVA <sup>a</sup>					
Model	Sum of Squares	df	Mean Square	F	Sig.
<b>Regression</b>	10.01	6	.33	5.13	.02 <sup>b</sup>
<b>Residual</b>	5.12	35	.32		
<b>Total</b>	15.13	41			
Coefficients					
	Standard coefficients		df	F	Sig.
	Beta	Std. Error			
<b>Firm-Level Strategy and FC</b>	.54	.45	1	5.61	.004 <sup>4</sup>

a) Predictor: (Constant) Firm-level strategy

b) Predictors: Human capital, marketing, manufacturing automation, research and development and information technology

c) Dependent Variable - Financial Performance

Table 2 demonstrates the product of the model that verified the combined influence of firm-level strategy and capabilities on financial performance ( $F = 5.10$ ;  $R^2 = 0.65$ ;  $P < 0.05$ ). This shows they were statistically significant. The independent  $R^2 = 0.05$ ; interactive  $R^2 = 0.65$ . This implies that firm capabilities accounted for 60% change in performance. The results similarly implies that capabilities influence on firm-level strategy and performance was marginal. Human capital capabilities whose interaction term recorded a 64% increment, had the premier input to the variation in performance. Research and development which posted a 53% change in performance was the second highest contributor. The results supports the proposition that firm capabilities significantly affects the relationship between firm-level strategy and organizational performance. Table 3 presents the results on the combined effect of firm-level strategy-capabilities-performance.

**Table 3: Joint Effects of Firm Capabilities on Firm-Level Strategy – Performance**

Model	R	R <sup>2</sup>	Adjusted R <sup>2</sup>	R <sup>2</sup> Change	F Change	df 1	df 2	Sig. F Change	Durbin Watson
1	.30 <sup>a</sup>	.09	.08	.09	10.38	4	410	.00	
2	.44 <sup>b</sup>	.21	.20	.21	60.69	1	409	.00	1.521

a) Predictors: (Constant) Firm-Level Strategy

b) Firm-Level Strategy and Firm Capabilities

c) Dependent variable: (Firm Performance)

Centred on model 2 in summary in Table 3 where the predictors: Human capital, marketing capabilities, manufacturing automation, information technology, and research and development capabilities was added ( $F = 60.69$ ;  $R^2 = 0.21$ ;  $P < .05$ ). The results demonstrate that these predictors contributed to the overall relationship with financial performance. The overall model was significant and that the joint independent variable was significant in

clarifying the changes in financial performance. The increase in  $R^2$  after including the moderating variable (firm capabilities) in the analysis was ( $\Delta R^2 = 0.21$ ) explaining a 21% positive variation in performance. The findings confirmed the alternative hypothesis that firm capabilities have a significant effect to the connection of firm-level strategy and performance of FBMC in Kenya.

## **5. Conclusion**

The objective of the investigation was to determine the effect of firm capabilities on the connections amid firm-level strategy and performance of FBMC in Kenya. The results on the influence of firm capabilities was positive and statistically significant to firm-level strategy and performance relationships ( $R^2= 0.65$ ; Std. Beta = .54;  $p\text{-value}\leq 0.05$ ). These directed the acceptance of the research hypothesis. The results also agrees with DCT proposition that high firm performance is a result of an efficient and effective engagement of critical intangible resources (Rothaermel 2008; Kamasak 2017).

The results on the impact of human capital on firm-level strategy and financial performance had the uppermost contribution of ( $R^2= 0.64$ ; Std. Beta = 0.26;  $p\text{-value}\leq 0.05$ ). This denotes that 60% variations in organizational performance was caused by changes in human resources capabilities. Employees would be more likely to settle with a company if the management invested in their employee asset management systems, learning and development, positive industrial associations and working environment. These results were consistent with Mutunga, Minja and Gachanja (2014) who argued that human capital structures, communication practices and sustainable competitive advantage had a positive relationship. Nevertheless, the results are in sharp contrast to Nalcaci & Yagci (2014) who established that marketing capabilities, use of informational and economic resource syndicates with administration and consumer relations capabilities had the uppermost bearing on business performance.

Research and development had the second highest effect of capabilities on firm-level strategy and performance ( $R^2= 0.56$ ; Std. Beta = .35;  $p\text{-value}\leq 0.05$ ). This shows that 51% changes in firm-level strategy and performance are influenced by research and development. The results confirmed the significant effect of research and development on firm-level strategy and performance connections. This process has a tie on enactment of competitive strategies. Consequently, the levels of research will significantly affect firm-level strategy accomplishment. In support of this view, Hitt, Hoskisson and Kim (1997) argued that firm's research and development capabilities is related to international diversification. However, the results are in sharp contrast to Krasnikov and Jayachandran (2008) who advocate that marketing capabilities have a robust influence on firm performance when compared to research and development.

The study supports the arguments of Awino (2011) who argued that the separate effect of core competencies, capabilities and strategy was relatively weaker when contrasted to the combined effect. The results supports the altercations of (Lopez, Peon & Ordas 2004) regarding internal capabilities worth on company financial performance. Studies with contrast results did not address the joint effect of these variables but only the independent effect of capabilities on firm performance (Johnson & Scholes 2005). Therefore, the study argues that the effect of firm capabilities on the linkages amongst firm-level strategy and performance was significant.

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The study has advanced frontiers of knowledge in firm-level strategy, capabilities and performance of FBMC. It advances support to the arguments of (Barney 2001a & 2001b) on existence of relationships amongst firm-level strategy, competences and performance. These results lend support to DCT in regard to firms' uniqueness in possession of idiosyncratic characteristics and core competences. The study will benefit Kenyan government in policy making and carrying out schemes for long-term financing of FBMC, knowledge and skill growth and support for research and development. The study further established that the effect of combined capabilities on firm-level strategy and performance connections is greater than their individual influences. To achieve stellar performance, key decision makers should judiciously incorporate numerous capabilities in firm-level strategy development.

The first constraint of the inquiry was in the research method. Cross sectional design lacks the rigor to test causality among concepts. The moderation of capabilities on firm-level strategy and performance, demands a longitudinal design as the evaluation of the concepts is more appropriate if tested for a 6-12 year term. Even though, hierarchical regression analysis is a powerful analysis tool; the method is sensitive to the order in which the concepts are entered in the programmer. Future studies should consider using other analytical tools such as Tobin Q or multivariate analysis. The second limitation of the study was the choice of senior executives as the only respondents. Consequently, the element of bias could not be entirely overruled. The perspective of other stakeholders like board members or executive team might have been ignored.

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