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Understanding Firm Performance in Microfinance Banks: Does Adaptive Capability Matter?

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Abstract:

The microfinance banking sector plays a pivotal role by complementing the services of commercial banks by enhancing access to financial services. The complementary role played by the microfinance banking sector aids in mitigating the negative impact of escalating incidences of poverty and unemployment and spurs economic development among the unbanked segment of society. However, evidence drawn from annual supervision reports of the Central Bank of Kenya demonstrates that the performance of this sector has been gloomy, with losses registered in the last five years reviewed in this study. This unpleasant trend has been observed in a period that is marked by sustained growth in customer deposits in the sector. In the same period, the aggregate branch network for the sector has, on average, been observed to stagnate. Other notable concerns relating to the sector include the absence of customized customer solutions, delays in credit processing, and high cost of credit. In light of this, the study examined the effect of adaptive capability on firm performance. The resource-based view of the firm provided the theoretical foundation of the study and was complemented by dynamic capabilities theory. Explanatory research design served as a basis for guiding the research strategy for resolving the research questions. A structured questionnaire was used to gather data from management employees deployed at the headquarters of Microfinance Banks. Descriptive statistics was used to aid in providing insights about the characteristics of the observed subjects in terms of percentages, frequency count, mean and standard deviation. Inferential analysis was also undertaken using a linear regression model, where the research objective was tested at ninety-five percent level of confidence. The presentation of findings was done in terms of figures and tables. The study confirmed that adaptive capability affected firm performance. Management teams should enact policies that would ensure that chosen strategic actions are sustainably synchronized in direction and magnitude with the ever-changing environment.

Keywords: Adaptability, adaptive capability and firm performance

1. Introduction

The potential success of any business in both the short and long term depends upon its ability to effectively conceive and implement value-creating strategies (Barney, 1991; Randeree & Al Youha, 2009; Johns, 2017; Kamandi & Kinyua, 2021). Over the years, scholars in strategic management and other related fields have predominantly focused their research efforts on providing an explanation for the question of performance heterogeneity (Barney, 1991; Hamel & Prahalad, 1996; Miller, 2003; Kinyua, 2015; Ouma, Kinyua & Muchemi, 2022). Primarily, researchers have underpinned their explanation of the economic puzzle of the existence and persistence of competitive and performance differential on the phenomenon of resource heterogeneity for firms operating in the same industry with a fairly homogeneous environment (Barney, 1997; Foss & Knudsen, 2003; Panos, Zaralis & Lioukas, 2004; Ocharo & Kinyua, 2021).

Accordingly, the resource-based view contends that the stock of resources and capabilities, which a firm owns and controls, are essential components for generating competitive advantage and improved performance (Barney, 1991; Teece, 2007). Particularly, the mix of human and non-human resources contributes differently to achieving a competitive advantage depending on how those resources are set up (Hughes, 2009; Barney, Ketchen & Wright, 2011). According to Grant (1996), capabilities can be thought of as intricate, integrative processes that combine resources that are tangible and intangible in nature to provide useful inputs that improve a company's ability to service customers. Capabilities provide a firm with the ability to develop a complex set of knowledge and skills for the deployment of an optimal mix of resources for generating customer value in tandem with the desired objective of an enterprise (Helfat & Peteraf, 2003; Carraresi, Aibisu, Mamaqi & Banterrie, 2012). Such capabilities are manifested through institutional processes and systems that facilitate the coordination of execution of value creation activities and optimization of firm resources (Day, 1994; Cao & Zang, 2011).

Although company capabilities are crucial for achieving short-term success, greater performance and the development of competitive advantage depend more on strategic capabilities (Hagoug & Abdalla, 2021). Essentially, strategic capabilities enable a firm to build and extend its contemporary skill set and knowledge to adapt to and cope with the dynamic environment (Kraaijenbrink, Spender & Groen, 2011). Firms operating in the financial sector are endowed with a stock of resources whose optimal contribution towards creating value and sustained realization of performance objectives can be leveraged through strategic capabilities.

As has been noted by Miller and Chatterji (2013), the financial services sector serves a fundamental role in channeling funds from savers to borrowers through the functions of intermediation and financial markets. Indeed, the financial sector and other economic sectors have a symbiotic relationship (Otto, Ekine & Ukpere, 2012). In accordance with the financial stability report of the International Monetary Fund (IMF), financial conditions at the global level have become more challenging and characterized by increased risks as an aftermath of the shockwaves of the Russo-Ukrainian war (IMF, 2022). However, as reported by the Deloitte Center for Financial Services (DCFS), the current inflation and price surges in industrial and consumer goods and services are likely to be temporary and are within the target range for most economies of the world (DCFS, 2022). At the macro level, developed economies with deeper and comparatively advanced financial systems enjoy higher economic growth as they are able to diversify risks and mobilize as well as allocate resources more efficiently relative to developing countries (Asli, Leora & Dorothe, 2017).

Although the development of the financial sector in Africa has been faced with myriad constraints, an increase in the diversity of financial service providers offers an enormous opportunity for innovative solutions for delivering financial services to the unbanked and underbanked (Raga & Tyson, 2021). A report drawn from the project by the Africa, Mediterranean, and Europe Network (AMENET) contends that a vast number of African countries have experienced considerable growth and intensification of their banking systems supported by increasing uptake of digital technologies (AMENET, 2021). Accordingly, the report of the European Investment Bank (EIB) attributed the performance of the banking industry in East Africa in recent years to favorable economic outlook and regulatory developments (EIB, 2020). Moreover, macroeconomic policies have been broadly sound and supportive of the solid performance of the sector. In light of the foregoing, it is anticipated that the performance of the banking sector in the Eastern part of Africa would significantly depend upon the extent to which the downside risks to the economic outlook would be addressed, alongside the challenges related to regulation and digitization.

Even though the banking industry has remained largely resilient and stable, characterized by healthy capital and liquidity ratios, the Central Bank of Kenya (CBK) contends that the industry performance experienced a marked decline in base assets from 12.4 percent attributed to 2020 to 11 percent realized in 2021 (CBK, 2021). In absolute terms, there has been a decline in the asset base of the banking sector from Ksh 6.0 trillion to Kshs 5.4 trillion in the years 2020 and 2021, respectively. Players in the banking sector have continued to face challenges of non-repayment of financial obligations by customers occasioned by reduced income, business turnover, and deterioration of asset quality (CBK, 2020). The National Bureau of Statistics (KNBS) Economic Survey of 2022 shows that within the same time frame, the Producer Price Index, which is used to assess overall inflation, increased by 7.32 percent from 102.08 in 2020 to 109.55 in 2021 (KNBS, 2022). This bleak scenario portends an overall rise in the cost of goods and services across all economic sectors.

1.1. Firm Performance

The performance of a firm can be considered as the capacity of an enterprise to accomplish its mission through sound governance and management, as well as continued dedication to the realization of specified objectives and goals in a timely manner (Stafford & Miles, 2013). Notably, firm performance is a multifaceted concept whose central concern is the ability of an enterprise to accomplish its activities and tasks with efficiency and effectiveness and, hence, realize its corporate objective (Jones & Hill, 2009; Mihaela, 2017). Despite the fact that there are various perspectives that can be used to conceptualize the construct of firm performance, it has been suggested that firm performance should be decomposed within the limits of the firm objectives, environment, and relevant and recognizable attributes or indicators (Folan, 2007; Demeke & Tao, 2020). The conceptual perspectives of firm performance include strategic management perspective (Crook, Bratton & Street, 2006; Richard, Devinney, Yip & Johnson, 2009), balanced scorecard (Kaplan & Norton, 2005), entrepreneurial perspective (Chandler & Jansen, 1992; Slevin & Covin, 1995), and accounting perspective ((Beaver, 1968; Lev, 1989).

The strategic management perspective proposes product-market performance, shareholders value, financial performance and long-term survival as dimensions that are critical for conceptualizing firm performance (Drucker, 1954; Crook et al., 2006; Richard et al., 2009). These dimensions, as proposed by the strategic management perspective, are fairly comparable with the financial measures and operational measures that are underscored by the balanced scorecard (Kaplan & Norton, 2005). While highlighting the necessity of using firm performance indicators that take into account the current and future operational conditions of business entities, management scholars have questioned the feasibility of integrating financial measures that are historical in nature and reflective of actions that have already been taken by management and may thus have little or no potential implication to both present and future firm performance (Zhang & Li, 2009; Demeke & Tao, 2020). This criticism is manifested in the rationale provided by Norton and Kaplan (2007) that typified the integration of non-financial indicators.

There is abundant evidence of a wide range of firm performance metrics in the extant body of empirical literature (Kinyua, Muathe & Kilika, 2015; Kimaru & Kinyua, 2018; Kyengo et al., 2019; King'oo et al., 2020; Kitur & Kinyua, 2020). Some researchers have adopted return on investment, market share, profitability and sales turnover, employee satisfaction, customer satisfaction, customer retention, lead time, return on assets, employee retention, turn-around time,

defect rate, Competitiveness and the success of new product launches as measures of firm performance (Fauzul, Hirobumi, & Tanaka, 2010, Lithaa, Ngugi & Njagi, 2014; Muthoni & Kinyua, 2020). Notably, these measures were chosen to operationalize firm performance in the context of manufacturing firms.

In the financial services sector, empirical literature depicts a rather mixed approach pertaining to choices of measures of firm performance. One segment of researchers has operationalized firm performance using financial metrics, including return on equity, return on assets and net interest margin (Ongore & Kusa, 2013; Kamande, Zablon & Ariemba, 2016; Otieno, 2020). Another segment of researchers has inclined the choice of measures to non-financial indicators such as stakeholder satisfaction, new product, customer retention, speed of response to the market crisis, product improvement, process improvement, turn-around time, new product, market share (Kinyua et al., 2015; Gabow & Kinyua, 2018; Ontita & Kinyua, 2020; Muthaura & Kinyua, 2021). On the basis of the foregoing case, non-financial measures of firm performance, market share, process improvement, and turn-around time were chosen to facilitate analysis of firm performance of Microfinance Banks.

1.2. Adaptive Capability

In the views of Schilke (2014), a strategic capability is essentially the ability that a firm possesses and controls that facilitates the optimal integration of resources and alignment of firm operations with the environment. In accordance with Kraaijenbrink et al. (2011), a firm's ability to build and extend its contemporary skill set and knowledge to adapt to and manage the changes in a dynamic environment draws upon its stock of strategic capability. Strong arguments have been raised suggesting that a firm is not likely to enjoy a competitive advantage and superior performance by merely possessing a good stock of resources, with an observation made to the effect that it is the firm's capabilities that facilitate optimal mix and exploitation of resources of business entities (Barney, 1991; Teece, 1997; Helfat & Peteraf, 2003; Hagoug & Abdalla, 2021). Furthermore, given the fundamental concerns of enterprises to embed practices that can support the productive and sustainable functioning of a firm in a volatile environment, significant scholarly and management attention has been drawn to the phenomenon of strategic capability (Hamel & Prahalad, 1996; King'oo, Kimencu & Kinyua, 2020). The existing body of relevant literature presents strategic capability as a multidimensional concept. Accordingly, Hagoug and Abdalla (2021) have identified human and physical resources as components for developing strategic capability. Similarly, Chepkole and Deya (2019) conceptualized human resource capability, cost efficiency capability, knowledge management capability and financial resource capability as dimensions of strategic capability in the context of information technology firms. Equally, strategic capability has also been considered to consist of capabilities related to information technology, marketing, human capital, operations, networking, intellect, adaptability, market-linking, and management (Seyhan, Ayas, Sönmez & Uğurlu, 2017; Kyengo, Muathe & Kinyua, 2019; King'oo, 2020).

Noting that strategic capability is primarily concerned with the functions of deployment and coordination of resources in the value-creation endeavors of an enterprise (Prahalad & Hamel, 2001), dimensions that have mere institutional resource orientation may not present a sound conceptualization of the construct of strategic capability. This form of dynamic capability requires that the expertise of members of a business enterprise is leveraged for effective integration with capital equipment, technology, and other resources of the firm. To a greater extent, strategic capability has its central concerns geared towards effective resource allocation, utilization and management (Huang, Wu & Rahman, 2012). Considering the context of the survey, operational capability, adaptive capability, knowledge management capability and market capability were adopted as critical dimensions for operationalizing strategic capability among Microfinance Banks in Kenya.

The success of a firm in implementing its chosen strategic actions is contingent upon its ability to establish a fit with its ever-changing environment (Porter, 1980; Teece, 2012). In particular, an adaptive capability is a variant of dynamic capability that is strongly associated with strategic actions that facilitate the re-configuration of a firm's resources, routines, and competencies to match the demands and harness the opportunities that evolve with the changing business environment (Barney, 1991; Ambrosini & Bowman, 2009). As argued by Wang and Ahmed (2007), the ability to align internal resources with the demands of the business environment is critical and is embedded in adaptive capability. In essence, the ability to adapt for any given firm is not necessarily a function of its size but is rather reinforced by the degree of conception and acceptance of change by primary stakeholders (Adriana, 2014).

1.3. Statement of the Problem

In Kenya, the microfinance banking sector plays a pivotal role by complementing the services of commercial banks through enhancing access to financial services intent on lessening the adverse effect of escalating incidences of poverty and unemployment besides spurring economic development among the unbanked segment of the society (Ali, 2015; Ahmed & Khan, 2016; MFI, 2019). As indicated by the CBK annual bank supervision reports, the microfinance banking sector has been characterized by losses in the last five consecutive years, ranging from Ksh 662 million in 2017 to Ksh 877 million in 2021 (CBK, 2018; CBK 2021). This unpleasant trend has been observed at a time when the sector has enjoyed growth in customer deposits from Ksh 38.9 billion to Ksh 50.4 billion in 2017 and 2021, respectively, with the highest growth of 12 percent experienced in 2020. Further, the aggregate branch network for the Microfinance Banking Sector has been observed to stagnate on average in the last five years (CBK, 2021). Other notable concerns relating to the sector include the absence of customized customer solutions, delays in credit processing, and high cost of credit and physical barriers (Mugo & Kilonzo, 2017).

A vast body of literature considers adaptive capability as an imperative for the effective functioning of a firm and in building and sustaining competitive advantage and superior performance (Barney, Ketchen & Wright, 2011; Hagoug &

Abdalla, 2021). The empirical literature is replete with evidence of adaptive capability as an antecedent of performance (Carraresi et al., 2012; Seyhan et al., 2017; Hagoug & Abdalla, 2021; Murugi & Kariuki, 2021). The study conducted by Carraresi et al. (2012) revealed that firm performance in the case of small and medium Italian food enterprises is positively affected by aspects of strategic capability adaptive capability. In this study, conclusions were based on a response rate of 16.3 percent, which does not meet the benchmark of 50 percent for making inferences, as advised by Mugenda and Mugenda (2003). Chryssochoidis, Dousios and Tzokas (2016) conducted a study on adaptive capability, competitive strategy and performance outcomes among small firms in Greece. Firms that had been in operation for at least five years were surveyed in this study in line with the perspective by Zahra *et al.* (2006) that capabilities take time to materialize and also given that the strategy-performance link in a firm becomes more stable and noticeable with time (Wiklund & Shepherd, 2005). Field data for this survey was gathered from chief executive officers and owners of the small firms. Among the 710 sampled subjects, only 143 returned valid responses in the survey, translating to a response rate of 20 percent. The study presented empirical evidence that adaptive capability influences the performance of small firms. The current study seeks to bridge the methodological gap of low response rate by making scheduled follow-ups with target respondents to validate the making of conclusions.

2. Literature Review

2.1. Resource-Based View of the Firm

The resource-based view is considered to have evolved from Edith Penrose's theory of the firm (Penrose, 1959), which placed the firm's resources at the center of value creation and contest for survival in the market (Kor, Mahoney, Siemsen & Tan, 2016). Accordingly, a firm is viewed as an aggregation of productive human and non-human resources under administrative coordination that generates goods and services for satisfying market needs at a rent (Penrose, 1996). Human and non-human resources possessed and controlled by a firm have varying influences on the achievement of competitive advantage, which is contingent upon how such resources are organized (Hughes, 2009; Barney, Ketchen & Wright, 2011).

The resource-based perspective presents an internal focus, contending that firm-specific resources and capabilities are ingredients for conceiving and executing a value-creating strategy with potential bolster performance outcomes of a firm (Barney, 1991; Peteraf, 1993). In accordance with Barney (1991), a firm relies on its collection of resources to conceive its strategy and efficiently and effectively implement the strategy. The diversity of resources and competencies that these organizations own and control is what underpins performance variation for businesses operating in the same industry (Newbert, 2007), in the absence of which firms would experience performance parity. Furthermore, building a competitive advantage would require that the resources and capabilities owned by the firm have inelastic supply and are immobile in nature (Grunert & Hildebrandt, 2004). In light of this, Barney (1986) notes that any assets that are homogeneous or can be freely acquired in the factor market cannot be all that strategic.

Resources of a firm that have characteristics of evaluability, rarity, inimitability and non-substitutability give a business the capacity to create and preserve competitive advantages, use these resources, and perform better (Collis & Montgomery, 1995; Madhani, 2010). Sund, Bogers, Villarroel, and Foss (2016) assert that a firm's capacity to create and maintain a competitive edge and enhance performance is driven by the identification, possession, and control of key internal resources. As Gimenez, van der Vaart, and van Donk (2012) observe, the concept of strategy, competitive advantage and superior performance are rooted in strategic resources and capabilities, which underlies the execution of sustainable economic activities in an enterprise. Accordingly, Teece and Pisano (1994) contend that a capability that is strategic must be unique, honed to users' needs, and difficult to replicate.

Hills and Jones (2012) recognize strategic capability as an organizational competence that resides in procedures, routines, rules, routines, and processes and is actualized through interactions, collaboration, and decision-making. Scholarly work in the field of strategic management has provided strong evidence that firm performance is among some of the anticipated outcomes of strategic capability (Seyhan et al., 2017; Hagoug & Abdalla, 2021; Murugi & Kariuki, 2021). In this study, the resource-based view was considered the theoretical basis for strategic capability and firm performance as research variables.

2.2. Dynamic Capabilities Theory

The notion that firm capabilities have a bearing on strategy draws upon the scholarly work of Schumpeter (1934), Penrose (1959), Barney (1986), and Teece and Pisano (1994). The theoretical framework of dynamic capabilities was developed by Teece, Pisano and Shuen (1997) in an attempt to provide a response to the basic concern in the field of management on how firms in environment with flux can develop and sustain competitive advantage. The theory contends that mere possession and control of resources and capabilities may not guarantee sustainable competitive advantage even as much as it may be used to propel a firm to a position of superior performance in the short term (Teece, 2007).

In a dynamic business environment, success has been associated with firms with management capability to effectively coordinate, integrate, and redeploy their competencies and thus demonstrate timely adaptation to shifts in the marketplace (Teece *et al.*, 1997). Accordingly, dynamic capabilities are the capacity that enables a firm to attain an optimal mix as it builds and reconfigures its internal and external competencies to address the rapidly changing environment. According to Helfat *et al.* (2007), dynamic capability is a corporation's ability to consciously build, extend and adjust its resource base. The dynamic capabilities framework proposes an explanation of firm-level differences in terms of asset position, firm processes, and the path-dependence nature of capabilities (Pisano, 2015).

The thrust of the dynamic capabilities model is not short-term efficiency, as in classic management, but the ability of a firm to maintain its 'evolutionary fitness' over a period of time (Teece, 2007). The Dynamic capabilities framework has integrated theoretical perspectives of behavioral theory and evolutionary economics and, therefore, has considered sensing-related capabilities, opportunity recognition-related capabilities, learning-related capabilities, re-configuration-related capabilities, and replication-related capabilities as variants of dynamic capabilities (Rick & Wolfgang, 2013). The viewpoint expressed by Rick and Wolfgang forms a sound conceptual basis for anchoring operational capability, adaptive capability, and marketing capability as critical capabilities that aid the endeavors of an enterprise to successfully navigate shifts in its environment. The success of a firm in maintaining a dynamic fit with its environment can be leveraged for superior performance in both the short and long terms.

2.3. Adaptive Capability and Firm Performance

Adaptive capability is a form of dynamic capability that is strongly associated with strategic actions that facilitate re-configuration of a firm's resources, routines and competencies in order to meet the demands and exploit opportunities in a dynamic business environment (Ambrosini & Bowman, 2009). As observed by Wang and Ahmed (2007), the ability to align internal resources with the demands of the business environment is critical and is embedded in adaptive capability. Adaptable enterprises are able to efficiently manage the present performance and effectively prepare for the future, both individually and collectively.

Chrysochoidis, Dousios and Tzokas (2016) conducted a study on adaptive capability, competitive strategy and performance outcomes among small firms in Greece. Firms that had been in operation for at least five years were surveyed in this study in line with the perspective by Zahra et al. (2006) that capabilities take time to materialize and also given that the strategy-performance link in a firm becomes more stable and noticeable with time (Wiklund & Shepherd, 2005). Field data for this survey was gathered from chief executive officers and owners of the small firms. Among the 710 sampled subjects, only 143 returned valid responses in the survey, translating to a response rate of 20 percent. The study presented empirical evidence that adaptive capability influences the performance of small firms. The current study seeks to bridge the methodological gap of low response rate by making a scheduled follow-up with target respondents to validate the making of conclusions.

Cristiano, Franciele, Grace, Hansen and Santos (2014) conducted an empirical enquiry into the effect of adaptive capability on strategic orientation in Brazilian agencies for maritime services. A structured questionnaire with 5 points was used as the research instrument. The study showed that adaptive capability and strategic orientation had a positive linear correlation. The study suffered from other contextual and methodological gaps that were addressed through the use of linear regression analysis and gathering data from Microfinance Banks in Kenya.

Mweu and Mung'ara (2021) carried out an empirical evaluation of adaptive capability as an input variable for the organizational performance of tier-two Commercial Banks in Kenya. The survey used a descriptive research design for executing the research methodology. A census survey of 64 heads of information technology, marketing, finance and operations functional areas was undertaken in 16 tier-two commercial banks. The response rate that was attained in this study was 94 percent, which strongly supported further statistical analysis. The study revealed a positive effect of adaptive capability on organizational performance. The methodological gap that drew from the use of descriptive research design was addressed using explanatory research design, which has a higher predictive power for causal links between organizational phenomena.

2.4. Conceptual Framework

A careful review of the pertinent body of literature facilitated the formulation of a conceptual model in figure 1, reflecting the proposed relationship linking adaptive capability and firm performance.

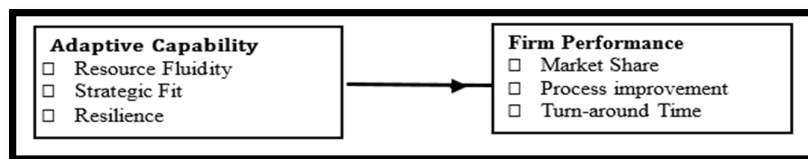


Figure 1: Conceptual Framework
Source: Author (2023)

2.5. Research Hypotheses

The research hypotheses of this study were:

- H₀: Adaptive capability has no significant effect on firm performance in Microfinance Banks in Kenya
- H₁: Adaptive capability has a significant effect on firm performance in Microfinance Banks in Kenya

3 Research Methodology

3.1. Research Design

A research design, according to Ahuja (2010), is a blueprint or strategy for carrying out a study in a way that balances economy and procedure with relevance to the research purpose. It provides a scheme for responding to the

research questions by combining the various components of the study in a logical way (Mishra & Alok, 2011). Explanatory research design was chosen as the blueprint for conducting the proposed study. This research design was suitable for testing the cause-effect behaviour of chosen phenomena as opposed to whether the phenomena are related (Edmonds & Kennedy, 2016). In particular, explanatory research design facilitated testing the effect of adaptive capability on firm performance on the basis of field data gathered from Microfinance Banks in Kenya.

3.2. Target Population

The proposed study was carried out in the 14 Microfinance Banks that have their operations in Kenya. The choice of Microfinance Banks is predicated upon the existence of concerns relating to their performance against a background where the microfinance banking sector is expected to aid in mitigating the negative impact of escalating incidences of poverty and unemployment and to spur economic development at family, community and national levels in Kenya (Ali, 2015). Microfinance Bank served as the analysis unit, whereas the observation unit was management staff accountable for the functional areas in the head offices of the 14 Microfinance Banks.

The focus on the head of functional areas drew upon the kind of information that was needed, which relates to capabilities that are predominantly in the custody of senior managers. Additionally, the functional heads were considered to bear the greatest responsibility regarding performance outcomes due to the critical and complementary roles that their functional areas play in ensuring the smooth functioning of Microfinance Banks. The functional areas of marketing and sales, operations, information technology, human resource management, products and finance were targeted in the study. This, therefore, implied that 84 functional heads among the 14 Microfinance Banks were observed in this study. The study was, therefore, a census survey of all the 14 Microfinance Banks in Kenya.

3.3. Census Survey

The researcher conducted a census survey of microfinance banks that have operations in Kenya. Accordingly, Johnie (2011) asserts that the decision to sample or carry out a census is predicated upon the size of the population, where when the cases in the population fall below 200, census survey becomes the preferred survey method. In the case of Microfinance Banks, 84 functional heads in the areas of marketing and sales, operations, information technology, human resource management, products and finance were observed in compliance with the recommendation made by Johnie.

3.4. Data Collection Instrument

A research instrument plays a crucial role in eliciting the required information in an empirical inquiry (Birmingham & Wilkinson, 2003). In the proposed study, a structured questionnaire was used to gather the needed data. The questionnaire provided a standardized set of items for each of the research variables, upon which participant responses fell within the 5-point rating scale that was provided in the instrument. The research instrument had a general information section and a specific information section. The section for general information focused on eliciting the biographical information of observed subjects. In the same respect, the section for specific information focused on eliciting information on the research variables. As such, the section for specific information had subsections for eliciting information on adaptive capability and firm performance.

3.5. Pilot Testing

A feasibility study was organized and carried out among 9 managers who are accountable to the heads of marketing and sales, operations, information technology, human resource management, products and finance in Microfinance Banks. The pilot study provided an opportunity for pre-testing the research instrument to verify the soundness of the set of test items on the basis of internal consistency. The pilot study involved approximately 10 percent of the 84 subjects involved in the final study. The choice of managers who report to the heads of functional areas was important as it ensured that these subjects were fairly familiar with the relevant practices relating to the research variables, and these managers were excluded in the final phase of gathering data. The pilot study facilitated the gathering of data for the reliability test.

3.5.1. Validity of the Research Instrument

In the views of Ghauri and Gronhaug (2005), it is necessary to assess the validity of a research instrument to ascertain how well the collected data covers the actual area of inquiry. Field (2005) avers that validity focuses on whether a set of test items measures what was intended. Face validity, content validity, and construct validity are considered important categories of validity (Taherdoost, 2016). Face validity is concerned with a subjective evaluation of the extent to which a test appears to measure what it was supposed to measure: the relevance of the test in terms of consistency, clarity, feasibility, and readability (Oluwatayo, 2012). Face validity was ensured by subjecting the research tool to the assessment by experts in the area of strategic management to identify and address any areas of concern.

Content validity is the degree to which a set of items in an instrument fairly represents the universe of the content to which the test would be generalized (Straub et al., 2004). The main concern is whether the test has all the essential items for a given construct domain. On the other hand, construct validity has its central concerns on test items that measure the concept/construct of interest to the researcher. A careful, extensive review of relevant theoretical and empirical literature on the constructs of adaptive capability and firm performance was carried out to inform the aspects and scope of aspects for formulating the set of questions for each of the variable.

3.5.2. Test of Reliability

The reliability of a research instrument is concerned with the extent to which a measurement of a phenomenon generates consistent and stable results (Huck, 2007). The particular concern in the test of reliability is whether the set of items representing a given construct has a fairly strong internal consistency as measured through Cronbach's Alpha coefficient (Robinson, 2009). Even though there is no consensus on the threshold of Cronbach's Alpha coefficient for making a decision, there is wide acceptance and use of Cronbach's Alpha coefficient of at least 0.70 while determining whether a research instrument is reliable (Field, 2009; Taherdoost, 2016). As such, Cronbach's Alpha coefficient of at least 0.70 was used as the threshold for decision-making for the test of reliability in the proposed study. The Cronbach Alpha coefficients for the items considered under each research construct in this study are portrayed in table 1.

Research Construct	Number of Test Items	Cronbach's Alpha Coefficients	Decision
Adaptive Capability	14	0.769	Acceptable Level
Firm Performance	7	0.748	Acceptable Level
Overall Score	21	0.762	Acceptable Level

Table 1: Cronbach's Alpha Coefficients Statistics
Source: Observations in the Pilot Study (2023)

The reliability statistics that drew from the analysis demonstrated that the test items for adaptive capability had the highest level of internal consistency with a Cronbach Alpha coefficient of 0.769. On the other extreme, the test items for firm performance revealed a relatively lower level of internal consistency with Cronbach's Alpha coefficient of 0.748. Therefore, the overall reliability statistics for the research constructs was 0.762. It can be observed that the Cronbach Alpha coefficients for the research constructs exceeded the recommended benchmark of 0.70 (Field, 2009; Taherdoost, 2016), which informs decisions on the reliability of the research instrument. As such, the questionnaire was determined to be within the acceptable threshold for reliability and was, therefore, suitable for measuring the respective research constructs.

3.6. Data Collection Procedure

The process of data collection was facilitated by letters of authority and an introduction that was issued by Kenyatta University. These letters were used to process the research permit from the relevant division of the National Council of Science, Technology and Innovation (NACOSTI). Consent to collect data from the head of functional areas in the respective Microfinance Banks was sought through the respective human resource divisions. Additionally, informed consent was sought from the relevant heads of functional areas, setting the stage for the actual collection of the required data. Print copies of the questionnaire were shared with all the participants identified in the proposed study. Upon dropping the questionnaires, participants were granted an agreeable period of time to provide respective responses. Contact persons were established in all the Microfinance Banks for ease of follow-up and tracking of progress. Subsequently, the questionnaires were picked to facilitate the actualization of analysis and development of the project report.

3.7. Data Analysis and Presentation

Data analysis is an essential aspect of research methodology that is concerned with deriving meaning for practical application in resolving the research problem. The research instrument gathered quantitative data through closed-ended questions on a scale of 1 to 5. The investigator carefully checked through each of the questionnaires received from the field for consistency and completeness. The respective items of the questionnaire were systematically coded and actual participant responses were carefully entered into the computer in preparation for actual analysis. The researcher performed a final audit of the keyed-in data set for accuracy, completeness, and consistency.

Descriptive characteristics of the observed subjects were analyzed using frequency count, percentages, mean and standard deviation. This elementary analysis formed the basis for further statistical analysis, the central focus of which was making inferences and conclusions. As such linear regression analysis was undertaken as shown in equation 1.

$$\text{Firm Performance} = \beta_0 + \beta_1 \text{Adaptive Capability} + \varepsilon \dots\dots\dots 1$$

A conclusion on the results of the regression analysis was made at a level of confidence and significance of 95 percent and 5 percent, respectively. The results of the data analysis were displayed in figures as well as in tabular form.

4. Research Findings and Discussion

4.1. Response Rate

The print copy of the questionnaire was administered to 84 functional heads in the areas serving at the head offices of the 14 Microfinance Banks in Kenya. However, 63 duly completed questionnaires were returned. The results of the participation rate by the targeted heads of functional areas are portrayed in figure 2.

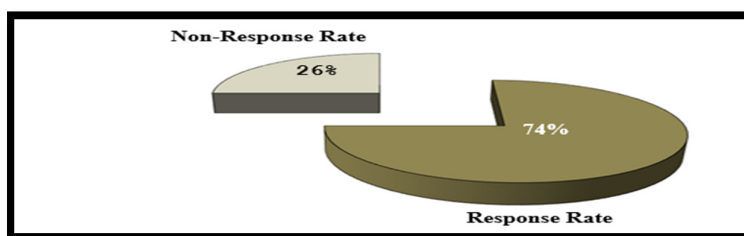


Figure 2: Analysis of Response
Source: Survey Data (2023)

The completed questionnaires formed a proportion of 74 percent of the total number that had been administered amongst the target heads of functional areas. This has an implication of 26 percent as the proportion of non-response rate. As has been underscored by Fincham (2008), the response rate has a bearing on the degree of representativeness of the sample and has an inverse relationship with non-response bias. Fincham further recommends a response rate exceeding 60 percent as suitable for studies focusing on making analyses to infer and generalize the behavior of the population from the measured sample. It is, thus, notable that a participation rate of 74 percent reported in this study was acceptable for generalizing findings to the entire context of microfinance banks in Kenya.

4.2. Characteristics of the Participants

4.2.1. Demographic Information

Observations were made to enrich the researcher's understanding of the gender, organizational position, and duration of service in the organizational position of the participant. The descriptive statistics for these attributes are analyzed in table 2.

Characteristic	Categories	Frequency Count	Percentage Frequency
Gender	Male	38	60
	Female	25	40
	Total	63	100
Organizational Position	Marketing and Sales	5	7.9
	Operations	7	11.1
	Information Technology	9	14.3
	Human Resource & Administration	10	15.9
	Products Development	8	12.7
	Finance & Strategy	7	11.1
	Credit	9	14.3
	Audit, Risk and Compliance	8	12.7
	Total	63	100
	Duration of Service	At most 4 years	22
4 - 8 years		28	44.4
8-12 years		9	14.3
Above 12 years		4	6.3
Total		63	100

Table 2: Respondents' Demographic Information
Source: Survey Data (2023)

Observations collected on the gender of the research participants revealed that there was a good representation of both male and female gender in the survey. Precisely, there was a 60 percent proportion of male participants relative to the 40 percent associated with the female participants. These proportions were a fair reflection of the numerical representation of the two genders in the top management of the functional areas observed in the study. The participation of the two genders in the study was critical in ensuring balanced observations in regard to the phenomena of adaptive capability and firm performance.

Descriptive statistics derived from observations on functional areas of the respondents manifested audit, risk and compliance, and credit as some of the key functional areas that characterize microfinance banks in Kenya. In terms of distribution, the analysis showed that all functional areas were represented in the survey, with human resources and administration enjoying marginal dominance at 15.9 percent while marketing and sales had the least showing at 7.9 percent. The proportion of representation of the eight functional areas depicted in the microfinance banks surveyed fell within a cross range, as can be seen in table 2. It is clear that all the functional areas were fairly represented in the data gathered on the variants of adaptive capability as input variables and firm performance as an outcome variable.

Duration of service in the management of functional areas was analyzed into four exhaustive categories. Precisely, functional heads who had served for a period between 4 and 8 years comprised the majority at 44.4 percent, while those with a service duration exceeding 12 years were the minority at 6.3 percent. The spread depicted by the analysis demonstrated that the research participants were familiar with the pertinent aspects of adaptive capability and firm performance. As a matter of fact, the research participants possessed the knowledge and skills that aid in bundling, reconfiguring, exploitation, and coordination of firm resources as construed by the variants of adaptive capability chosen in this survey. Further, the observed functional heads were well versed with envisaged performance outcomes as they are involved in conceiving, communicating, and measuring the level of achievement of adaptive objectives such as firm performance and others.

4.2.2. Descriptive Analysis for Adaptive Capability

In this empirical enquiry, the adaptive capability was conceptualized as the skill set and knowledge leveraged to facilitate the re-configuration of the firm's resources, routines and competences to meet the demands and exploit opportunities in a dynamic business environment. In the case of Microfinance Banks observed, the adaptive capability was signified by resource fluidity, strategic alignment and resilience. The observations made on the adopted aspects of adaptive capability have been summarized in table 3.

Statement	Frequency	Mean	Std Dev
The bank is able to redeploy commensurate resources on the basis of fluctuating demand	63	3.52	0.77
The bank undertakes timely redeployment of resources	63	3.46	1.19
There is seamless redeployment of resources across the various subsystems of the bank	63	3.60	1.01
Changes in the environment determine the resource needs of the banks' subsystems	63	3.82	0.78
Opportunities in the environment are a major basis for restructuring resources	63	4.26	0.84
The mix of resources for facilitating the creation of value in the bank subsystems is dynamic	63	3.79	0.92
Retooling is done on a need basis as triggered by cues from the business environment	63	3.87	1.12
The resource needs of the bank subsystems are hinged on opportunities and threats identified in the external environment	63	4.17	0.98
The activities of the different units of the bank interact with each other to optimise the synergistic benefits	63	4.38	0.76
The activities of the different units of the bank reinforce each other in the process of creating customer value.	63	4.13	0.71
Shifting of assignments amongst employees is undertaken to facilitate integration of efforts for creating and delivering customer value	63	3.55	1.09
The bank has committed sufficient resources to monitor market crises	63	3.68	1.22
The banks use coordinated efforts to respond to disruptive occurrences in the market	63	3.87	0.75
The banks enhance the capacity of employees to changes in the business environment	63	4.05	0.97
Adaptive Capability	63	3.87	0.94

Table 3: Descriptive Statistics for Adaptive Capability

Source: Research Data (2023)

The observations obtained on the measured activities and aspects of adaptive capability, as signified in the tabulated statements, have been used as a basis for formulating the summary measures that are necessary for carrying out further statistical analysis. It is apparent from the resulting values of mean response that participants were, to a large extent, in agreement that adaptive capability was determined as an important value chain activity in the surveyed Microfinance Banks. This behavior is signified by the mean response of 3.87 registered for the fourteen aspects of adaptive capability and its associated relatively low standard deviation. A characteristic low standard deviation signifies a low coefficient of variation, which is a desirable attribute in the estimation of population characteristics.

In the analyzed mean response, it has been noted that interaction among different units in the execution of activities with the consequent effect of generating synergistic benefits has the highest mean of 4.38 and a relatively small value of standard deviation of 0.76. In contrast, the aspect that banks undertake timely redeployment of resources has the lowest mean response of 3.46 with an accompanying relatively high standard deviation of 1.19. The rest of the measured aspects of adaptive capability lie between these two extreme values of the mean response. It can be observed that there is

a shared evaluation amongst the participants that the observed activities and practices are considerably manifested in the fourteen Microfinance Banks and are imperative for generating customer value. As contended by Wang and Ahmed (2007), adaptive capability enables an enterprise to align internal resources with the demands of its environment and, as posited by Adriana (2014), is not necessarily a function of its size but is rather reinforced by the degree of conception and acceptance of change by primary stakeholders.

4.2.3. Descriptive Statistics for Firm Performance

Firm performance is a multifaceted concept whose central concern is the ability of an enterprise to accomplish its activities and tasks with efficiency and effectiveness and, hence, realize its corporate objective. This multifaceted construct should be decomposed within the limits of the firm objectives, environment, and relevant and recognizable attributes or indicators. In this study, outcomes that relate to market share, process improvement, and turn-around time were adopted to aid in measuring the performance of Microfinance Banks. The observations gathered on the set of aspects contextualized as firm performance have been summarized in table 4.

Statement	Frequency	Mean	Std Dev
The bank sales are characterised by repeat purchases	63	3.91	1.08
There are customer-friendly provisions for switching from one bank product to another	63	4.21	0.74
Alternative products are available to meet customer's needs	63	3.96	0.59
There is an improvement in existing institutional processes	63	4.14	0.87
There is a notable reduction in the time taken to execute customers' requests	63	4.05	0.72
Feedback to customers' queries takes a relatively short time	63	4.31	0.83
There are new innovative processes for the delivery of services	63	3.85	0.54
Firm Performance	63	4.06	0.77

Table 4: Descriptive Statistics for Firm Performance
Source: Research Data (2023)

The operational aspects of firm performance capability, as manifested in the tabulated statements, were analyzed into summary measures of mean and standard deviation to form the basis for further statistical analysis. The behavior of the values of mean response provides clear evidence that, to a large extent, the heads of functional areas agreed that the envisaged performance outcomes were manifested in the surveyed Microfinance Banks. It can be observed that there is wide variability in responses on the aspect that bank sales are characterized by repeat purchases. This implies that there are mixed assessments and evaluations concerning the behavior of this crucial performance outcome amongst the observed Microfinance Banks.

It is apparent that there is a favorable evaluation of the aspects relating to the short time span for responding to customers' queries, with a mean response of 4.31 and a standard deviation of 0.83. This is an outcome that is highly valued by customers and is important in enhancing the value proposition of a Microfinance Bank. Other outcomes that have high mean response are on existence of customer friendly provisions for switching from one bank product to another, improvement of existing institutional processes, and reduction in the time taken to execute customers' requests. The mean response and corresponding standard deviation at 4.06 and 0.77, respectively, for firm performance confirm that, to a large extent, the participants agreed that the measured performance outcomes were manifested in the context of microfinance banks. In the inside-out perspective of explicating performance heterogeneity, adaptive capability has been presented as a key ingredient in informing strategic choices, achieving competitive advantage and delivering desirable firm performance (Hagoug & Abdalla, 2021).

4.3. Linear Regression Analyses

The observations made on adaptive capability and firm performance were analyzed through a simple linear regression model to ascertain and quantify how adaptive capability affected firm performance. The summary output of this analysis is tabulated and discussed accordingly.

Model	R	R Squared	Adjusted R Squared	Std. Error of the Estimate	Durbin-Watson
1	0.815 ^a	0.664	0.616	0.739	1.936

Table 5: Model Summary
Source: Survey Data (2023)

The output determined from the regression analysis for model summary reveals that the correlation coefficient for the model is 0.815, which demonstrates a strong positive relationship of linear nature between adaptive capability and firm performance. Further examination of the output reveals that the value of R square for the estimated model is 0.664. It can thus be observed that adaptive capability is associated with a variation of 66.4 percent of firm performance. Additional statistics that provide crucial information on whether the model is significant are tabulated and discussed.

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	15.483	4	7.208	18.020	0.001 ^b
	Residual	11.044	58	0.371		
	Total	26.527	62			

a. Dependent Variable: Firm Performance
 b. Predictors: (Constant), Adaptive Capability

Table 6: Output of Analysis of Variance
 Source: Survey Data (2023)

The output manifested from the F-test indicates that the estimated equation has a p-value of 0.001, which is precisely less than 0.05 and an F statistic of 18.020. These statistics demonstrate that the model deriving from the regressed data has a good fit and is, therefore, appropriate for predicting firm performance on the basis of adaptive capability.

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	β	Std. Error	Beta		
(Constant)	1.702	.461		2.271	.018
Adaptive Capability	.583	.078	.518	3.582	.001

Table 7: Coefficients of Regression Analysis
 Source: Survey Data (2023)

a. Dependent Variable: Firm Performance
 b. Predictors: (Constant), Adaptive Capability and Marketing Capability

As can be seen from the statistical values of the regression analysis, the parameters derived from unstandardized coefficient values generate the estimated model thus presented.

$$Firm\ Performance = 1.702 + 0.583 Adaptive\ Capability \dots\dots\dots 2$$

It can be clearly noted from the statistics of regression analysis that when adaptive capability is maintained at a level of zero, the level of firm performance would be at 1.702. This value represents the y-intercept for this linear relationship, for which the p-value of .018 serves as a confirmation of its statistical significance. The rest of the statics for respective adaptive capability are useful for responding to the objective of the survey.

The survey sought to analyze the effect of adaptive capability on firm performance. In table 7, the beta coefficient for adaptive capability is .583 and its p-value is 0.001, which is less than .05. This confirms that a variation of 1 unit in the level of adaptive capability would cause firm performance to vary by .583 in the same direction. It is thus reasonable to infer that firm performance amongst Microfinance Banks in Kenya is affected by adaptive capability.

The conclusion made in this study agrees with the findings of other enquiries that have been carried out in diverse contexts. For instance, adaptive capability and competitive strategy were determined to influence performance outcomes among small firms in Greece (Chrysochoidis, Dousios & Tzokas, 2016). Similarly, the implications of the findings of the current study agree with the observations made by Wang and Ahmed (2007) that adaptive capability is imperative for aligning internal resources with the demands of the business environment. Additionally, the findings of this study confirm the postulates of dynamic capabilities theory that in an environment that is characterized by flux, strategic fit can only be guaranteed if a firm has the capacity to adapt and thus respond favorably to the changing outfit of its environment (Helfat *et al.*, 2007).

5. Conclusion

In this study, adaptive capability was adopted as the input variable, while firm performance was the output variable. Microfinance Banks in Kenya were chosen as the context for the study due to the complementary role that they play in the financial services sector, which fosters access to financial services and financial inclusion and also aids in mitigating the negative impact of escalating incidences of poverty, unemployment and spur economic development among the unbanked segment of the society. However, evidence drawing from annual supervision reports of the Central Bank of Kenya has demonstrated that there are a couple of concerns regarding such parameters of firm performance as characterized by annual losses amidst growth in customer deposit in the sub-sector, stagnation in aggregate branch network, absence of customized customer solutions, delay in credit processing, and high cost of credit.

The resource-based view was reviewed as a basis for the theoretical foundation of the study and complemented by the theoretical perspectives of dynamic capabilities theory. Explanatory research design served as the methodological basis for guiding the observation and analysis of the cause-effect adaptive capability on the phenomenon of firm

performance. Observations made through crossed-ended questions on management staff responsible for functional areas at the head offices of Microfinance Banks were analyzed to understand the basic characteristics of the subjects, descriptive attributes of the research variables and making inferences in terms of the research questions.

The descriptive analysis demonstrated that the response rate was within an acceptable range for the estimation of population characteristics. In terms of demographic attributes, there was a fairly good distribution of participants in the categories that were deemed crucial for this survey. Observations made in relation to the research question demonstrated that relevant aspects of adaptive capability and firm performance were present to a large extent in the surveyed Microfinance Banks. Statistical analysis revealed that the resulting model for adaptive capability and firm performance has a good fit and thus can be used for planning purposes in the observed Microfinance Banks. It was further determined that adaptive capability is a predictor of firm performance. The investigator, therefore, concluded that the phenomenon of firm performance is affected by adaptive capability.

6. Recommendations of the Study

The conclusions of this study have a bearing on policies and practices within the microfinance banks in Kenya. The top management team should enact policies that would ensure that chosen strategic actions are sustainably synchronized in direction and magnitude with the ever-changing environment. Such policy guidelines would foster resource fluidity and ensure strategic alignment in the internal firm's productive factors, which would essentially confer the firm with the ability to withstand and cope with environment-related threats and crises. With such a policy framework, Microfinance Banks would undertake re-configuration and timely redeployment of resources across the complementary subsystems. Sufficient resources should be made available to aid in the accurate and timely monitoring of the environment and thus inform the bank's retooling initiative.

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