

STRATEGIC ADAPTATION IN TURBULENT ENVIRONMENTS: LEVERAGING DIFFERENTIATION STRATEGY FOR IMPROVING PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES

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Abstract

It is imperative that to achieve and sustain competitive advantage in the face of turbulent environments, businesses need to adopt a strategic posture that emphasises the path to be undertaken in order to achieve their goals. The study examines the impact of strategic adaptation through differentiation strategies in enhancing the performance of small and medium scale enterprises in Nigeria's turbulent business environment, with a specific focus on innovation and technological adaptations. The study adopted a multi-stage sampling method to select a sample of 2,175 SME owners as participants from various sectors, and across six States representing the six Nigeria's geopolitical zones. Data collected were analysed through descriptive statistics and structural equation modeling. The findings reveal statistically significant correlations between innovation, technology adaptations, brand identification, and continuous product development with improved firm performance. The findings display the critical role innovation and technology adaptations play in the strategic differentiation of SMEs, suggesting that businesses that invest in these areas are more likely to achieve superior performance in challenging economic climates. It is recommended that SME managers should cultivate a proactive innovation culture, strengthen their brand equity, and institutionalise continuous product development processes to remain competitive and resilient in the face of ongoing environmental disruptions.

Keywords: differentiation strategy, technology adaptations, innovative differentiation, SMEs, performance, structural equation modeling, turbulent environments,

1. Introduction

The topic of how businesses operating in the same industry can have different levels of success has been a lengthy discourse in the literature for a long time, and it still is. Experts in the field of strategic management over the course of years (Derfusetal., 2008) have been arguing about what organization practice makes a business perform better than its competitors. In order to attain enhanced performance, an enterprise must participate in competition, which, according to Porter (1980), is one of the most important elements of strategy. Competitiveness is one of the most

common phenomena in the operation of business activities ((Bocken&Geradts, 2020; Kristoffersen*etal.*, 2021;Wu, Lao, & Li., 2019), and no doubt it is taking a hard stance on SMEs because of their inability to possess the resources and strategic initiatives, as well as rising costs and price competition from the larger firms (Moris*etal.*, 2015; Kaliappen, &Hilman, 2013).

Zehire*etal.* (2015) contend that competition, which is exceedingly ferocious in the global marketplacetoday, has become a pull factor, making firms adopt a variety of strategic actions and responses in order to attain competitive advantage and maintain bottom line results. Small and medium-scale enterprises (SMEs), being pivotal to driving growth and fostering job creation (Akeke*etal.*, 2021), must take a proactive approach, not only by developing a plan that will enable them to operate but also by creating customer value that will help position their firms relative to competitors for performance improvement (Sirajuddin, *etal.*, 2017). However, these firms as a result of a host of challenges that stifled their ability, struggle to compete effectively within both local and international markets. This is why Rosario and Rainmudo (2024) posit thatcompetition is fierce, exacerbated by a lack of strategic direction; hence, firms are often forced to rely predominantly on price competition, that undermined their capacity for sustainable growth. Therefore, leveraging differentiation strategies has emerged as a crucial approach for performance improvement in order to carve out sustainable market segments within the competitive landscape.

A differentiation strategy enables businesses to stand out in the market by offering unique products and services that are perceived as superior by consumers. These strategies are concerned with how an enterprise will pursue its goals while allocating resources in a certain customer function in comparison to competitors. It is concerned with how commercial activities are carried out in a manner that differs from those of competitors. The differentiation strategy, with particular reference to its innovation efforts through technological adaptations, is concerned with attracting customers by providing them with distinctive products and service features that compel them to pay a higher price for the product or service. Widuri and Sutanto(2018) state that when an organisation adopts a differentiation strategy, it may be necessary to concentrate its efforts on supplying differentiated products or services to customers. In this regard, because the products or services are distinct in form, character, and perhaps performance, such a game plan will result in high customer loyalty and cross-selling opportunities (Hlavacka*etal.*, 2001). This indicates that differentiation strategy has the potential to appeal to customers with preferences for value, uniqueness, high quality, and innovative products and service characteristics, and as such, they are prepared to pay the best selling price that does not cause cognitive dissonance in the marketplace.

Consequently, an enterprise pursuing a differentiation strategy will place a strong emphasis on acquiring knowledge and understanding about the market it serves as well as its competitors from sources outside the organisation, rather than within it. Not only does it concern itself with commanding a firm's reputation, but it also engages in costly and comprehensive promotion campaigns, product design and performance evaluations, among other things, in order to achieve customer satisfaction and repeat purchases (Widuri&Sutanto, 2018; Miller, 1986). Such a firm is capable of channeling the preferences, requirements, and choices of its customers into the value that is being created. This is why it is widely assumed in the literature that differentiation strategies will lead to long-term success for businesses (Banker*etal.*, 2014). A differentiation strategy can be implemented through several key measures, such as developing innovative products, making significant investments in technology and digital platforms, fostering strong brand identification, continuously developing new products, and offering a diverse range of

products. Each component is essential for enhancing the perceived value of offerings, contributes significantly to differentiating SMEs from competitors, and can result in improved market performance. For instance, innovative products that meet local consumer needs can substantially improve brand loyalty and increase market share, while high expenditures on technology and digital platforms can similarly result in operational efficiencies that lower costs, improve resource management and overall service delivery (Wibowo, 2023; Craig et al., 2012; Kumar & Patel, 2020). Robust brand identification enhances consumer trust, a vital factor in a saturated marketplace, while ongoing product development enables SMEs to adapt effectively to consumer needs (Onalaja & Otokiti, 2021; Fritz et al., 2017). A diverse product range can reduce risks linked to market fluctuations by catering to various consumer segments and preferences.

Understanding the effects of differentiation strategies on performance indicators, including market share, revenue growth, profitability, and customer satisfaction, is crucial for SMEs aiming to navigate existing market challenges. Thus, the reliance on price competition to differentiate has been shown to be unsustainable (Rosario & Rainmudo, 2024), as numerous SMEs encounter substantial obstacles to market entry and expansion. Focusing on differentiation enables SMEs to tackle challenges such as limited product innovation and insufficient brand visibility, which have hindered their competitiveness (Schlegelmilch, 2022). As well as continuous new product development that enables businesses to respond to evolving consumer preferences which are critical aspects in a dynamic market such as Nigeria.

The growing debate on differentiation strategy and SMEs' performance has attracted several important findings, yet it shows significant gaps because different studies present conflicting findings about differentiation strategy effectiveness. For instance, a study conducted by Akingbade in 2020 discovered that service differentiation enhances SME performance through better customer satisfaction and market expansion. The study by Casimir (2025) also demonstrated that differentiation strategy leads to better market share and service quality outcomes. However, while using employee engagement as mediator variable in the study of Isichei et al. (2024), yet they found no statistically significant relationship exists between differentiation strategy and SME competitiveness, thereby suggesting that there is a missing link in the findings from previous research, because differentiation strategy effectiveness seems to be dependent on certain conditions in the environment, such as turbulence, resource availability, and innovation intensity.

More importantly, resource based view (RBT) and strategic balanced model have been largely utilised in many past studies (Musa & Waziri, 2022; Anekwe et al., 2021), either individually or in combination, but ignored Schumpeter's (1934) innovation theory which has its focus on creative destruction, technological advancement, and innovation for sustainable differentiation. Moreover, although certain studies (Okwaro et al., 2025) utilised innovation theory, their implementation does not specifically address the volatility and institutional challenges, inherent in Nigerian markets, such as weak regulatory frameworks, bureaucratic inefficiencies, laws, etc., that are necessary for the proper functioning of the economy because they can create uncertainty, ambiguity, and obstacles for businesses. Therefore, the limitation brought about by past studies in providing knowledge on how innovation-based differentiation helps small businesses to transform their operational capabilities under turbulent environmental conditions calls for a study of this nature.

Furthermore, Gorondutse and Hilman (2017) study in the hotel sector shows environmental munificence affects differentiation and performance relationships, but how environmental turbulence affects strategic adaptation processes has not been explored. The Nigerian economy

faces lots of challenges including foreign exchange instability, technological disruptions, and infrastructural decay which make it essential to study differentiation as a strategic adaptation tool. The majority of existing research views the external environment as an unchanging context instead of recognizing its active role in strategic development and execution.

In another vein, while most previous research conceptualised differentiation as product and service uniqueness (Mark & Akpan, 2024; Eboh et al., 2024), other studies have treated it as service quality (Musa & Waziri, 2022), or packaging (Mark & Akpan, 2024), and (Msinga *et al.*, 2018; Kaliappen & Hilman, 2014), on the dimensions of marketing and support services. The current research lacks a complete understanding of differentiation because it not only fails to study its multiple components which include innovation and technological adaptation and branding and continuous product development for enduring firm success in unstable markets, but also how they are strategically integrated to create synergy for competitive advantage. Empirical studies examining technological adaptations that cause customer engagement, promote products, information sharing, and continuous new product development are essential for a thorough understanding of the impact of differentiation strategies on the performance of SMEs in Nigeria. Therefore, this research project expands the definition of differentiation strategy to include multiple innovation dimensions which creates a complete and active framework based on Schumpeterian innovation perspective.

2 Theoretical Background and Hypothesis Development

2.1 Innovation Theory

The lens through which this study is anchored is the Schumpeter's (1934) theory of innovation. The theory provides the foundation to study how SMEs adapt their differentiation strategies within the dynamics of strategic adaptation. Schumpeter's innovation theory demonstrates that economic and organisational development emerges from firm innovation because firms engages in creative destruction to eliminate current patterns while acquiring new competitive advantages and creating innovative value propositions. Schumpeter (1934) explains that innovation is the complete process through which new products are developed, new production methods introduced, new markets exist, new sources of supply introduced, which match the components of differentiation strategy form the mechanism that enables SMEs to operate in a volatile environment for sustainable performance.

According to Schumpeter, the entrepreneur operates as the main driver of change who searches for new business opportunities through resource and knowledge reconfiguration in unstable economic environments marked with high competition. Thus, the theoretical framework helps understand how Nigerian SMEs with acute resource constraints, unstable markets, and economic instability can adopt innovation-based differentiation approaches for strategic adaptation. Through product innovation and redesign, brand identity resilience, SMEs can overcome environmental constraints and create unique market positions. The main argument of this study is in line with innovation theory which maintains that innovation is a strategic and adaptive process which helps businesses survive and succeed in unstable business environments, rather than merely technological issue.

The unstable Nigerian business environment which is characterised by economic instability, inflationary conditions, regulatory unpredictability, and rapid technological advancements requires SMEs to navigate in the face of strategic adaptation, because firm that use traditional strategies will be vulnerable to shocks in the market. Thus, differentiation by innovation remains the fundamental business model for strategic adaptation, hence this study concludes that

differentiation strategy is not only a static choice among alternatives, but also an adaptive technique that will enable firms to respond to turbulence business environment through their creativity. For instance, innovation dimension of differentiation will enable firms to create new products and services which meet and exceed customer needs and expectation, and this fits into major thrust of innovation theory, while technological adaptation element enables SMEs to enhance their operational efficiency and market responsiveness in today's digital business environment.

Furthermore, the psychological and emotional connection arising from brand identification enables firms to build brand strong value and reputation which makes it possible to distinguish their products from competitors for competitive advantage, which aligns with the non-price completion of Schumpeter innovation theory. The continuous product development element enables businesses to update their offerings, which as Schumpeter theory posits matches market requirements, and acting as a fundamental driver of business expansion and market transformation. This integration of innovation dimension of differentiation strategy aligns with Schumpeter operational manifestation of innovation thrust within the strategic posture of SME for strategic adaptation. Therefore, we hypothesise that:

Firms that leverage differentiation strategy through the dimensions of innovation, technological adaptation, brand identification, and continuous product development will achieve improved performance in turbulent environments.

3. Material and Methods

The study design was based on quantitative research. The study includes all owners of small and medium enterprises across six States representing each of six Nigeria's geopolitical zones. The selection of these SMEs was justified by the need to capture regional diversity, sectorial representation, and the varying impact of environmental turbulence across the country. The owners were chosen because they were thought to have a clear understanding of their company's operations and so be in a position to provide accurate responses. The overall number of SMEs owners in the research was 620,447, including 53,189 medium businesses and 617,249 small businesses (NMSMEs, 2021). Using multi-stage sampling method, 201,311 SMEs were selected across six States from the six geopolitical zones, including Abia, Bauchi, Benue, Kano, Lagos, Plateau, and Rivers with the inclusion of the FCT. A total of 2,175 owners were chosen as participants. Multi-stage sampling was employed to ensure a representative selection of SMEs from diverse sectors, reflecting the geographical and economic variance within the country. To obtain data for the latent constructs, the study instrument was created utilising a 7-point Likert scale measurement. Porter's (1985) differentiation strategy measurement was adapted which now has fourteen components. The dependent variable's questionnaire items include several aspects of company performance that are compared to prominent competitors in the industry of operation (Lopez-Nicholas & Merons-Cerdan, 2011; Choi & Lee, 2003). Firm performance was based on balanced score-card measured by profitability, customer satisfaction, sales growth, and market growth; process performance was measured by quality and efficiency; and internal performance was measured by individual capabilities such as employee satisfaction, and creativity. Data collected was analysed through descriptive statistics and structural equation modeling which is capable of providing robust insights into the relationships among variables.

4 Results and Discussion

4.1 Results

Influence of Differentiation Strategy on Performance of SMEs

The outcomes of data collected and analysed from differentiation strategy used by SMEs on its performance is presented in Tables 1 and 2 and Figure 1. Results in Table 1 show that nearly all the strategies used by SMEs are significantly ($P < 0.05$) related to its performance outcomes, implying that the strategies implemented by SMEs have a meaningful relationship with their performance outcomes. Among these, innovative product development (DS5) recorded the highest regression weight of 0.799, reflecting that innovation remains the most powerful determinant of improved performance across indicators such as sales growth, profitability, market share, customer satisfaction, product quality, and efficiency.

Other differentiation strategies such as strong brand identification (DS7) had a regression weight of 0.748 and continuous development of new products (DS4) recording a regression weight of 0.714. This implies that SMEs that continuously improve and diversify their products, while also exhibiting distinctive brand identities are experiencing superior performance. The ability of firms to offer a wide range of products (DS3) with a regression weight 0.672, and maintain technological dynamism (DS6) with a regression weight of 0.614 further reinforces the importance of differentiation strategies in turbulent environments.

However, high expenditure on technology (DS8) which recorded the lowest regression weight of 0.388, suggests that while technology adoption enhances competitiveness, excessive or misaligned spending without strategic integration may not bring about commensurate firm performance outcomes. The overall path coefficient of 0.697 (69.7%) from Figure 1 shows that differentiation strategy explains a substantial portion of the variation in SMEs' performance, emphasising its central role in fostering resilience and competitiveness. These results collectively affirm that innovation, technological adaptation, and brand distinctiveness are vital strategies which SME can leverage for improved performance in Nigeria's turbulent business landscape. The high regression weight shows that differentiation strategy is more crucial as a competitive strategy to ensure a good performance of SMEs is attained.

Table 1: Unstandardised Regression Weights for Differentiation Strategy Performance of SME

Path			Estimate	S.E.	C.R.	P-value
DS1	<---	Differentiation strategy	1.000			
DS2	<---	Differentiation strategy	1.069	.106	10.058	***
DS3	<---	Differentiation strategy	1.752	.114	15.409	***
DS4	<---	Differentiation strategy	1.929	.117	16.417	***
DS5	<---	Differentiation strategy	2.059	.112	18.405	***
DS6	<---	Differentiation strategy	1.583	.113	14.034	***
DS7	<---	Differentiation strategy	1.939	.113	17.203	***
DS8	<---	Differentiation strategy	.915	.104	8.794	***
DS9	<---	Differentiation strategy	1.174	.103	11.368	***
DS10	<---	Differentiation strategy	1.495	.114	13.113	***
DS11	<---	Differentiation strategy	-.111	.114	-.975	.330
PERFORM	<---	Differentiation strategy	1.000			

Note: ***p<0.001. DS1 was fixed to 1.000 to set the measurement scale

Table 2 Standardized Regression Weights for Differentiation Strategy and Performance of SME

Path			Standardised Estimate
DS1	<---	Differentiation strategy	.429
DS2	<---	Differentiation strategy	.443
DS3	<---	Differentiation strategy	.672
DS4	<---	Differentiation strategy	.714
DS5	<---	Differentiation strategy	.799
DS6	<---	Differentiation strategy	.614
DS7	<---	Differentiation strategy	.748
DS8	<---	Differentiation strategy	.388
DS9	<---	Differentiation strategy	.500
DS10	<---	Differentiation strategy	.574
DS11	<---	Differentiation strategy	-.043
PERFORM	<---	Differentiation strategy	.697

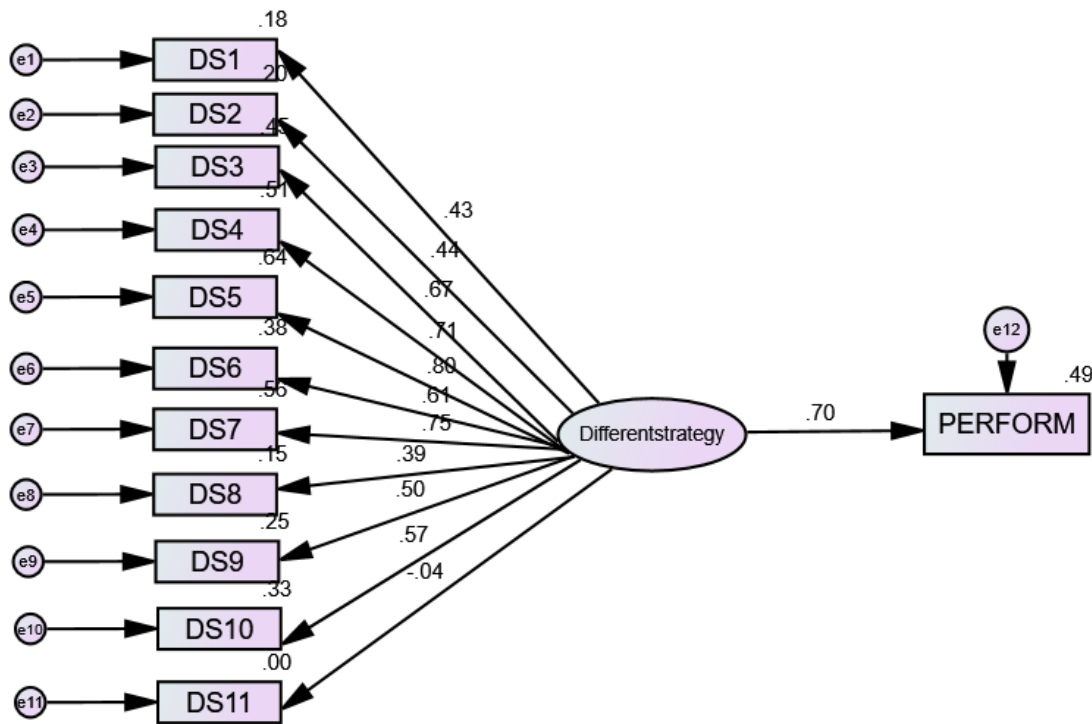


Figure 1: Path Analysis of the Influence of Differentiation Strategy on Performance of SMEs

4.2 Discussion

With the use of the maximum likelihood approach and structural equation modeling, the study findings illustrate that differentiation strategy is a crucial mechanism for navigating turbulent business environment. The study contributes to the literature by demonstrating that differentiation strategy measured through innovation and technological adaptation strategies were significant business models to be adopted in order to improve the performance of SMEs sector. The high regression weight of innovative products confirms that economic progress is fueled by firms' ability to innovate and create new combinations of products and processes, which aligns with Schumpeter's (1934) innovation theory. Thus, Nigerian SMEs that embrace continuous innovation are, therefore in a better position not only to anticipate change, meet evolving customer needs and expectations, but also are able to outperform their competitors.

The implications from the findings is that the inventive, technologies, digital platforms, brand identity, more product lines, continuous new product development, and service components of differentiation strategy analysed in this study are all closely associated with quality and efficiency, sales growth, market share, customer satisfaction, and profitability as indicators of the performance of SMEs in Nigeria, while large expenditure and a broad choice of product offerings had a less substantial impact on business success than expected. This means that these components of differentiation strategy enable firms in the SME sector to respond flexibly to

environmental changes, enhance competitive advantage, and sustain long-term growth. The empirical evidence underscores the critical importance of strategic innovation and technology use as core drivers of performance in unstable environments.

The study implies that for Nigerian SMEs to thrive in the midst of volatility business landscape, they must prioritise innovation that drives differentiation and invest in appropriate technologies which is tailored to their operational realities. According to earlier studies in competitive strategy research, differentiation strategies have been found to have a positive and significant impact in boosting the performance of enterprises. The findings of this study support Aykan and Aksoylu (2013), Teeratansirikoo *et al.* (2013), and Parnell and Koseoglu (2010) studies in competitive strategy research. As previously stated, the high impact of innovative technologies and digital platforms, brand identity and continuous product improvement is not surprising in this study. After all, firms adopting a differentiation strategy should place an emphasis on brand image, proprietary technology for product development, utilise logistics and delivery services, acquire skills in online payment and procurements, and special features that will differentiate their products and services against their competitors, with overall result in a higher profit margin than their competitors (Porter, 1985). According to the findings of the study, doing something unusual and adequately valued by customers would no doubt result in a premium pricing, which Johnson *et al.* (2011) argue will result in high performance outcomes.

5. Conclusion and Recommendations

From the findings of this study, it is concluded that differentiation strategy positively and significantly enhances the performance of Nigerian SMEs through its dimensions of innovation, technological adaptation, and brand identity. This suggests that all innovation-led differentiation attributes contribute approximately 70% to overall performance outcomes, which highlights its strategic importance in turbulent environments. Therefore, firms in SMEs that consistently innovate, adapt to technological change, and cultivate strong brand identities will achieve superior sales growth, profitability, market share, and customer satisfaction.

The results confirm the innovation propositions of Schumpeter which posits that innovation is the engine of firm growth and transformation, especially in economies where volatility and competition are high. Hence, differentiation is not an occasional business tactic, but it is a sustained strategic posture which is essential for a long-term success and resilience.

From the above, it is therefore recommended that SMEs should create not only a culture of innovation that encourages creative thinking, research and development, and continuous improvement in products and processes, but also they should guide their technological investments by strategic needs and capacity for utilisation. Besides, they should prioritise technologies that directly improve productivity, product quality, and customer engagement, as well as build a strong, trustworthy brand. SMEs should also develop clear value propositions, consistent branding, and quality assurance systems that differentiate them in competitive markets.

The entrepreneurs who are owners of SMEs should foster learning capabilities in order to anticipate environmental changes and appropriately respond proactively. Training, networking, and collaboration with research institutions can be undertaken to enhance this adaptability.

Policymakers and SME support agencies such as SMEDAN and SMIESIS should create innovation enabled environments that support tax incentives, access to finance, and infrastructural support for technological adoption. These will not only strengthen SMEs strategic

adaptability, enhance competitiveness, but also enable them achieve sustainable performance despite environmental turbulence.

6. Future Research Direction

While this study provides a lever through which firms in SME sector can navigate turbulent environments, we suggest some paths for further research due to the dynamic nature of strategy.

- i. Since this study used cross-sectional, and because strategic adaptation is an evolving process, a longitudinal studies that track several years is suggested, because it will help in the assessment of whether the benefits of technological adaptation diminishes or shifts.
- ii. Since challenges faced by small firms are different across institutional contexts, it would be invaluable if cross country studies are undertaken particularly in emerging economies, because it may provide more insights on whether or not certain dimensions of differentiation in specific regulatory environments are more critical.
- iii. Although, the use of structural equation modeling for testing and analysing complex relationships looks excellent, further studies could employ mixed-methods strategy that integrate qualitative survey so that human elements that may drive continuous innovation such as leadership mindsets could be uncovered.

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