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ASSESSING SMALL AND MEDIUM ENTERPRISES' INNOVATION CAPABILITIES WITHIN A RAPID ECONOMIC TRANSFORMATION: AN EMPIRICAL STUDY IN SAUDI ARABIA

by

Mohanad Jabreel Aboudayah

Faculty Advisor

Dr. Omar Hujran, Department of Statistics and Business Analytics

College of Business and Economics

Date & Venue

08:00 am to 09:00 am

Friday, 17 November 2023

H3-2021

Abstract

The theory of dynamic capability posits that environmental uncertainty and organizational flexibility drive the growth of innovation capability at the firm level. Environmental uncertainty is the inability of the firm to quickly and accurately forecast changes in economic conditions. Building innovation capability can mitigate environmental uncertainty and enable the firm to gain a competitive advantage by innovating continually in response to evolving circumstances. Organizational flexibility, a key element of the firm's managerial capabilities, is necessary but not sufficient to attenuate environmental uncertainty. Organizational flexibility enables the firm to identify and assess emerging opportunities, but pursuing those opportunities requires innovation capability. In Saudi Arabia, several studies have noted that despite their positive macroeconomic impact, the government's ambitious interventions under Vision 2030 have had ambiguous effects on the private sector, implying that the country's rapid economic transformation may be increasing environmental uncertainty, especially among small and medium enterprises.

This study empirically tested the relationship between environmental uncertainty, organizational flexibility, and firm-level innovation capability by collecting surveys from 211 small and medium enterprises in the Saudi service sector and analyzing the results through partial least squares structural equation modeling. The findings showed that environmental uncertainty and each of its dimensions (munificence, dynamism, and complexity) positively affect firm-level innovation capability, and that organizational flexibility moderates the relationships between innovation capability and environmental uncertainty and between innovation capability and munificence. This study contributes to the literature on innovation management, and it has important implications for policymakers in developing countries striving to observe and mitigate the effects of environmental uncertainty.

Keywords: Dynamic Capability, Innovation Capability, Environmental Uncertainty, Organizational Flexibility, Small and Medium Enterprises, Saudi Arabia.