



Effect of Innovation on The Performance of SMEs in Karu Local Government Area, Nasarawa State.

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ABSTRACT

Most Small and Medium Enterprises (SMEs) in Nigeria have engaged in various innovation strategies, including market and process innovations, while organizations like SMEDAN provide support through training and resources. Despite these initiatives, many SMEs continue to face performance challenges. This study examined the effect of market innovation and process innovation on the performance of SMEs in Karu Local Government Area, Nasarawa State. A survey research design was employed, with structured questionnaires administered to a total of 346 SME owners and managers. The data were analyzed using Partial Least Squares Structural Equation Modelling (PLS-SEM) to test the formulated hypotheses. The study found a positive and significant effect of market innovation on SME performance, while process innovation showed a negative and insignificant effect. The study recommends that SMEs prioritize adopting innovative marketing strategies to enhance customer engagement and market positioning. Additionally, SMEs should carefully implement process innovations in alignment with their operational goals to avoid inefficiencies. Collaborating with industry experts could further optimize their innovation strategies, leading to improved overall performance.

Keywords: Innovation, Market Innovation, Process Innovation, SMEs Performance, Small and Medium Enterprises, Karu LGA, Nasarawa State.

INTRODUCTION

Small and Medium Enterprises (SMEs) are widely recognized as vital contributors to economic development and job creation. According to the World Bank, SMEs constitute approximately 90% of businesses and account for more than 50% of employment worldwide. Their significance extends beyond mere employment; they are instrumental in fostering innovation, driving competition, and enhancing economic resilience. In developed economies, SMEs contribute to a significant portion of Gross Domestic Product (GDP), while in developing economies, they play a crucial role in informal employment and poverty alleviation.

In the context of Africa, SMEs represent a substantial share of the economy, contributing roughly 80% of total employment and 30% of GDP in many countries. Despite their importance, African SMEs often grapple with unique challenges, including inadequate infrastructure, limited access to finance, and regulatory hurdles. For instance, the African Development Bank highlights that SMEs are significantly underfunded, with many unable to secure loans due to a lack of collateral and credit history. Additionally, the rapid urbanization and shifting consumer preferences in the region necessitate that SMEs innovate to remain competitive. The emphasis on innovation has become critical for SMEs to navigate these challenges and enhance their performance.

Small and Medium Enterprises (SMEs) are widely recognized as the backbone of economic development, particularly in developing economies such as Nigeria. They play a crucial role in generating employment, alleviating poverty, and contributing to Gross Domestic Product (GDP) growth (Small and Medium Enterprises Development Agency of Nigeria (SMEDAN), 2020). In Nasarawa State, SMEs are instrumental in driving local economic activities, especially within Karu Local Government Area (LGA), which serves as a bustling commercial hub due to its proximity to Abuja, the Federal Capital Territory.

Market Innovation involves developing new marketing strategies or significantly improving existing ones to better meet customer needs and enhance market presence (OECD, 2018). This type of innovation is crucial for SMEs seeking to differentiate themselves in competitive environments. In Karu LGA, effective market innovation can lead to increased customer engagement and loyalty. For instance, SMEs that adopt targeted marketing campaigns or utilize data analytics to understand consumer behavior can create tailored offerings that resonate with their audience. A study by Nwankwo and Oguji (2020) highlighted that Nigerian SMEs employing innovative marketing strategies experienced higher customer satisfaction and retention rates. However, challenges such as limited marketing budgets and insufficient understanding of digital marketing tools often hinder the ability of SMEs to implement effective market innovation.

Process Innovation, on the other hand, involves implementing new or significantly improved production or delivery methods (Organisation for Economic Co-operation and Development (OECD), 2018). This innovation type enhances operational efficiency, reduces costs, and improves product quality, contributing to better SME performance. In the highly competitive markets of Karu LGA, process innovation can be transformative. For example, adopting lean manufacturing techniques or automating repetitive tasks can lead to significant cost savings and faster turnaround times. Okonkwo and Wogu (2021) found that Nigerian SMEs embracing process innovation reported increased profitability and scalability. However, the adoption of process innovation is often hampered by limited access to modern technology and inadequate employee training, particularly in rural and semi-urban areas like Karu LGA (SMEDAN, 2020).

The relationship between innovation and SME performance is well-documented in the literature; however, most studies have focused on developed economies, with limited attention to the unique challenges and opportunities faced by SMEs in developing countries like Nigeria (Oyelaran-Oyeyinka, 2020). Moreover, few studies have examined the specific context of Karu LGA, where SMEs operate in a dynamic yet resource-constrained environment. By focusing on product, process, technological, open, and market innovation, this study aims to fill this gap and provide actionable insights for policymakers, SME owners, and other stakeholders.

In summary, innovation is a critical determinant of SME performance, particularly in competitive and rapidly evolving markets like Karu LGA. Product innovation enables SMEs to meet changing customer needs, while process innovation enhances operational efficiency and cost-effectiveness. Technological innovation presents new growth opportunities and improves customer engagement, market innovation fosters deeper connections with consumers, and open innovation promotes collaboration and knowledge-sharing.

Statement of the Problem

Despite the support provided by both government initiatives and private-sector programs, Small and Medium Enterprises (SMEs) in Nigeria continue to exhibit underperformance, reflected in their diminishing contributions to the national GDP and erratic growth trends. In Karu Local Government Area (LGA), many SMEs face significant challenges in maintaining competitiveness, primarily due to their insufficient adoption of innovative practices. Although the role of innovation in enhancing business performance has been extensively documented in developed countries, there is a noticeable lack of empirical research focusing specifically on the context of SMEs in this region.

This gap is particularly concerning given that SMEs are crucial to economic development and job creation in Nigeria. Current statistics indicate a decline in the contribution of SMEs to GDP, falling from 50% in 2021 to 39.8% in 2023 (Clement et al., 2024). Furthermore, many SMEs remain stagnant despite the availability of credit facilities aimed at supporting expansion. Existing literature has primarily addressed training and performance in other regions, leaving a void in understanding how market and process innovations specifically impact SMEs in Karu LGA.

Consequently, this study aims to investigate the effects of market innovation and process innovation on the performance of SMEs in Karu LGA, Nasarawa State, to provide actionable insights for policymakers and business owners. By addressing this research gap, the study seeks to enhance the understanding of innovation's role in driving sustainable performance among SMEs in this locality.



Objectives of the Study

- i. To examine the effect of market innovation on the performance of SMEs in Karu LGA, Nasarawa State.
- ii. To assess the effect of process innovation on the performance of SMEs in Karu LGA, Nasarawa State.

Research Questions

- i. What is the effect of market innovation on the performance of SMEs in Karu LGA, Nasarawa State?
- ii. What is the effect of process innovation on the performance of SMEs in Karu LGA, Nasarawa State?

1.4 Research Hypotheses

H₀₁: Market innovation has no significant effect on the performance of SMEs in Karu LGA, Nasarawa State.

H₀₂: Process innovation has no significant effect on the performance of SMEs in Karu LGA, Nasarawa State.

LITERATURE REVIEW

Conceptual Review

Market Innovation

Johnson and Smith (2025) define market innovation as the process of reshaping market offerings and distribution methods to create new value propositions for customers, enabling companies to enter new markets or revitalize their presence in existing ones. They highlight that market innovation often involves leveraging technology and data analytics to personalize customer experiences and optimize market penetration strategies. Martinez and Lee (2025) describe market innovation as the introduction of novel marketing strategies, customer engagement techniques, and sales models aimed at transforming how businesses reach and serve their target markets. Their definition emphasizes the importance of agility and adaptability in developing innovative approaches to meet changing customer expectations and competitive pressures.

According to Chen and Wilson (2025) market innovation is a transformative approach that focuses on redefining customer interactions, distribution channels, and market positioning to stay ahead of competitors. They suggest that successful market innovation requires continuous monitoring of industry trends, customer feedback, and emerging technologies to create impactful, long-term value. Brown and Lee (2023) argue that market innovation is the process of rethinking and restructuring how organizations interact with their customers, through innovative marketing strategies, digital transformation, and new market-entry techniques. They emphasize the importance of integrating technology and data analytics to optimize customer experience and market performance.

Patel and Garcia (2025) characterize market innovation as the strategic exploration of new market opportunities through innovative approaches to pricing, branding, and customer relationships. They point out that market innovation is crucial for organizations to adapt to evolving consumer preferences and to differentiate themselves in increasingly competitive markets. Martinez and Roberts (2023) characterize market innovation as the strategic reconfiguration of market positioning and customer interactions, leveraging creative marketing approaches and modernized sales techniques to respond to evolving consumer preferences and market demands. They highlight the role of market innovation in driving business growth and maintaining a competitive edge in dynamic environments.

Davis and Zhang (2025) view market innovation as the redesign of market strategies and business models to better align with shifting consumer demands, technological advancements, and global market trends. They argue that organizations that invest in market innovation can gain a competitive edge by anticipating market changes and quickly adapting their strategies to meet new challenges. Roberts and Singh (2024) define market innovation as the development of new marketing strategies, channels, or business models aimed at entering new markets or significantly improving customer engagement in existing markets. They emphasize that market innovation often



involves identifying emerging customer needs and using innovative approaches to reach new audiences or create new value propositions for existing ones.

Process Innovation

Process innovation refers to the introduction of new or significantly improved production or delivery methods within an organization. It involves the development and implementation of novel processes, technologies, or workflows that enhance efficiency, reduce costs, or improve product or service quality. Process innovation may involve automating manual tasks, streamlining operations, adopting new technologies, or reconfiguring supply chain management practices. The primary goal of process innovation is to optimize organizational performance by increasing productivity, reducing waste, minimizing errors, and improving customer satisfaction. It can also lead to more sustainable business practices by reducing resource consumption and environmental impact. By continuously improving internal processes, organizations can maintain a competitive edge, respond more effectively to market changes, and drive long-term growth and innovation (Brown & Garcia, 2025).

Johnson and Lee (2025) define process innovation as the strategic re-engineering of organizational workflows, where new technologies and methods are applied to production and service delivery processes to increase operational efficiency and reduce costs. They emphasize that process innovation is vital for maintaining competitiveness by streamlining operations and improving productivity. Martinez and Patel (2025) describe process innovation as the introduction of novel approaches to the internal workings of a company, aimed at enhancing the efficiency, quality, and sustainability of its processes. Their definition highlights the importance of leveraging technological advancements and data-driven insights to optimize workflow and improve overall performance.

SMEs Performance

SMEs performance refers to the ability of small and medium-sized enterprises (SMEs) to effectively achieve their business objectives and goals, as measured by a variety of financial and non-financial indicators. It encompasses a range of outcomes, such as profitability, revenue growth, market share, productivity, and operational efficiency, that collectively reflect the overall health and success of an SME. Performance is not only determined by financial results but also by qualitative factors such as innovation, customer satisfaction, employee engagement, and organizational adaptability (Adeyemi, 2022). Successful SME performance is often driven by the company's ability to navigate market challenges, leverage available resources, and implement strategies that improve competitiveness, sustainability, and long-term growth. In addition, factors like leadership quality, strategic vision, access to funding, and the ability to innovate play critical roles in influencing how SMEs perform in both local and international markets. Therefore, measuring SME performance involves a holistic approach that considers both the tangible and intangible assets that contribute to the business's overall achievements.

Martinez and Lopez (2025) define SMEs' performance as the ability of small and medium-sized enterprises to achieve both financial and non-financial objectives through efficient resource management, innovation, and customer satisfaction. They argue that SMEs' performance is a multidimensional concept that includes profitability, market share, operational efficiency, and the capacity to innovate, all of which are crucial to sustaining long-term competitive advantage (Johnson & McCarthy, 2025).

Empirical Review

Market Innovation and SMEs Performance

Adebayo and Oluwaseun (2025) examined the impact of market innovation on the performance of small and medium enterprises (SMEs) in Nigeria's agricultural sector. Using a sample of 200 SMEs, the study employed regression analysis to assess the relationship between market innovation strategies, such as new distribution channels and pricing models, and performance indicators like sales growth and market share. The results indicated that SMEs that adopted innovative marketing strategies experienced significant improvements in their market performance. However, the study also identified challenges related to market access and competition.



The authors recommended developing supportive policies to enhance market access for innovative SMEs. The findings cannot be replicated in the current study due to differences in the method of analysis.

Sakura and Chen (2025) explored the role of market innovation in enhancing customer satisfaction among small and medium enterprises in the Asian retail sector. Utilizing a sample of 200 SMEs, the study applied structural equation modeling (SEM) to analyze how market innovation practices, including personalized marketing and loyalty programs, affected customer satisfaction. The findings revealed that SMEs that focused on innovative customer engagement strategies reported higher levels of customer loyalty and retention. However, the study highlighted that many SMEs faced difficulties in implementing these strategies effectively. The study was carried out in Asia; therefore, its findings cannot be replicated elsewhere. This current study is limited due to geographical differences.

Process Innovation and SMEs Performance

Martinez and Liu (2025) examined the impact of process innovation on operational efficiency in small and medium enterprises (SMEs) in the European manufacturing sector. Their objective was to assess how practices such as lean manufacturing and automation influenced performance indicators like production output and cost reduction. The study involved a sample of 300 SMEs and employed regression analysis to analyze the data. The findings revealed that SMEs implementing process innovations experienced significant improvements in operational efficiency, with production output increasing by up to 30% and operational costs decreasing by 20%. However, the study faced criticism for overlooking the complexities involved in implementing innovations across diverse manufacturing environments.

Nguyen and Patel (2025) explored the role of process innovation in enhancing service delivery among small and medium enterprises in the Asian hospitality sector. The researchers aimed to determine how process innovations, including workflow optimization and technology integration, affected service quality and customer satisfaction. They surveyed a sample of 150 SMEs and applied structural equation modeling (SEM) for their analysis. The study found a positive correlation between process innovation and improved service quality, with a reported 25% increase in customer satisfaction among SMEs that adopted innovative practices. Nonetheless, the study lacked a longitudinal perspective, making it difficult to assess the long-term effects of process changes on customer loyalty.

Theoretical Framework

Schumpeter's Theory of Innovation

Schumpeter's Theory of Innovation, first advanced in his seminal works (Schumpeter, 1934; 1942), emphasizes that innovation is the fundamental driving force of economic development and business performance. Schumpeter identified five forms of innovation: the introduction of new products, the development of new methods of production, the opening of new markets, the discovery of new sources of supply, and the creation of new organizational structures. According to this theory, entrepreneurs and firms that embrace innovation create a process of "creative destruction," whereby old processes, products, and markets are displaced by newer, more efficient, and competitive ones. This continuous renewal is what sustains growth and ensures long-term survival in dynamic environments.

The theory is particularly relevant to small and medium enterprises (SMEs), as they often operate in competitive and resource-constrained environments where innovation becomes a necessity rather than an option. For instance, product innovation allows SMEs to differentiate their offerings, meet consumer demands, and improve customer retention. Process innovation enhances efficiency, reduces costs, and improves quality, thereby strengthening performance. Market innovation helps SMEs penetrate new customer segments and geographical regions, while technological innovation enables them to leverage digital platforms, automation, and advanced tools to compete with larger firms. Furthermore, in today's knowledge-driven economy, open innovation—although not originally emphasized by Schumpeter—aligns with his notion of recombining resources and ideas, as SMEs increasingly rely on external networks, collaborations, and partnerships to innovate and grow.

Applied to this study, Schumpeter's theory provides a theoretical justification for examining how different forms of innovation (market, process, product, technological, and open innovation) influence the performance of SMEs. It suggests that the ability of SMEs in Karu LGA and beyond to remain competitive, grow market share, and achieve profitability depends largely on their innovative capacities. In essence, the theory underscores the argument that SMEs which continuously innovate are more likely to experience improved performance, while those that fail to do so risk stagnation or decline in the face of competition and changing market conditions.

METHODOLOGY

A survey research design was adopted. The population for this study comprises all 346 registered SME owners in Karu Local Government Area of Nasarawa State, as documented by the Nasarawa State Chamber of Commerce and Industry (2023). Structured questionnaires were administered to SME owners and managers in Karu LGA. Given the manageable size of the population (346 SMEs), the study adopted the census technique, which involves collecting data from the entire population without selecting a subset. This approach ensures comprehensive coverage and enhances the generalizability of the findings within the study area. Data were analyzed using Partial Least Squares Structural Equation Modelling (PLS-SEM).

Model specification

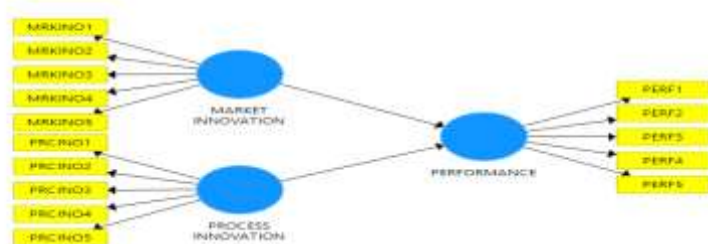


Figure 3.1 Structural model for direct relationship between marketing communication and performance

Data Presentation and Analysis

A total of 346 copies of questionnaires were distributed, of which (340) were retrieved, giving a response rate of 98%. 6(2%) were not properly filled but returned. All further analyses were carried out using 340 responses.

Indicator Reliability

When evaluating the measurement model, we initiate the process by examining the item outer loadings. Generally, it is recommended to consider loadings above 0.708, as they signify that the construct accounts for more than 50 percent of the variance in the indicator, ensuring acceptable item reliability (Hair et al., 2019). However, Hair et al. (2019) also suggest that low but statistically significant indicator loadings (below 0.50) may be included. Conversely, outer loadings below 0.4 should be eliminated, and in exploratory research, loadings between 0.4 and 0.7 may be retained if the average variance extracted is satisfactory (Hair et al., 2014). This justifies the decision not to exclude indicators with loadings below 0.70 and above 0.40 from the model.

Table 1: Factor Loadings of the Constructs

	MARKET INNOVATION	PERFORMANCE	PROCESS INNOVATION
MKTINO1	0.665		
MKTINO2	0.623		
MKTINO3	0.743		
MKTINO4	0.769		



MKTINO5	0.748		
PERF1		0.666	
PERF2		0.736	
PERF3		0.811	
PERF4		0.867	
PERF5		0.700	
PRCINO			0.695
PRCINO1			0.552
PRCINO2			0.612
PRCINO3			0.780
PRCINO4			0.810

Source: SmartPLS Output, 2025

Convergent Validity

Convergent validity assesses how well a construct explains the variance among its associated items. For convergent validity to be established, the average variance extracted (AVE) must be greater than 0.5. As shown in Table 2, all constructs have AVE values exceeding 0.5, confirming that they satisfy the requirement for convergent validity. This indicates that each construct captures at least 50 percent of the variance in its respective measurement items.

Table 2: Construct Reliability and Validity of the Indicators

Variables	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
MARKET INNOVATION	0.855	0.756	0.836	0.507
PERFORMANCE	0.814	0.826	0.871	0.577
PROCESS INNOVATION	0.827	0.736	0.822	0.585

Source: SmartPLS Output, 2025

Table 3: Heterotrait-Monotrait Ratio (HTMT)

	MARKET INNO	PERFORMANCE	PROCESS INNO
MARKET INNO	1.000		
PERFORMANCE	.729	1.000	
PROCESS INNO	.661	.605	1.000

Source: SmartPLS Output, 2025



Model Goodness of Fit (GoF)

To assess the validity of the PLS model, evaluating its goodness of fit is crucial, as suggested by Hair et al. (2017). In this research, the Standardized Root Mean Square Residual (SRMR) was used for this purpose. This metric was chosen because it offers an absolute measure of model fit, where a value of zero indicates a perfect fit. According to Hu and Bentler (1998), an SRMR value below 0.08 signifies an acceptable model fit. The result of this study showed an SRMR of 0.025, suggesting a strong model fit. In addition to the chi-square statistic, other indices also supported the model's overall goodness of fit.

Table 4: Model of Goodness of Fit Summary

	Saturated Model	Estimated Model
SRMR	0.025	0.025
d_ULS	6.651	6.651
d_G	2.151	2.151
Chi-Square	4872.500	4872.500
NFI	0.483	0.483

Source: SmartPLS Output, 2025

Test of Hypotheses

The table below showed the path coefficients, t-values and p-values used to test the first four null hypotheses of the study:

Table 5: Path Coefficient of the Model

Variables	Beta	T Statistics (O/STDEV)	P Value s	Decision	F2 Values
MARKET INNOVATION -> PERFORMANCE	0.116	2.974	0.003	Rejected	0.009
PROCESS INNOVATION -> PERFORMANCE	- 0.167	0.049	0.625	Accepted	0.041

Notes: (P<0.01), (P<0.05), (P<0.1)

Source: SmartPLS Output, 2025

Hypothesis One

H01: Market innovation has no significant effect on the performance of SMEs in Karu LGA, Nasarawa State.

The result from Table 5 shows that market innovation has a positive and significant effect on the performance of SMEs in Karu LGA, Nasarawa State, with $\beta = 0.116$, $t = 2.974$, and $p = 0.048$. Thus, hypothesis one was not supported and therefore rejected at the 5% level of significance. There is sufficient evidence to reject the null hypothesis, and the study concludes that market innovation has a positive and significant effect on the performance of SMEs in Karu LGA, Nasarawa State.

Hypothesis Two

H02: Process innovation has no significant effect on the performance of SMEs in Karu LGA, Nasarawa State.



The result from Table 5 shows that process innovation has a negative and insignificant effect on the performance of SMEs in Karu LGA, Nasarawa State, with $\beta = -0.167$, $t = 0.049$, and $p = 0.625$. These values support the null hypothesis at the 5% level of significance. Therefore, the null hypothesis was accepted, and the study concludes that process innovation does not have a significant effect on the performance of SMEs in Karu LGA, Nasarawa State.

Table 6: R square Statistics

Variable	R Square	R Square Adjusted
Performance	0.524	0.523

Source: Researcher's computation in SmartPLS 2025

The r-square statistics shows the level of determinism of the dependent variable by the independent variables of the study. Table 6 show that the study has an r-square value of 0.524 which indicates that the variables (market and process innovation) used for the study account for about 52.4% of the variability in the dependent variable.

DISCUSSION OF FINDINGS

The study examined the effect of innovation on the performance of SMEs in Karu LGA, Nasarawa State. The findings from the analysis above indicate that the model is adequately fit to measure the relationship between innovation and SMEs' performance. The study tested two hypotheses and evidence provided by the results revealed that innovation affects SMEs' performance moderately, as indicated by the coefficient of determination (R^2). The findings on the specific independent variables and how they affect SMEs' performance are discussed below:

The first finding revealed that market innovation has a positive and significant effect on the performance of SMEs in Karu LGA, Nasarawa State, with $\beta = 0.116$, $t = 2.974$, and $p = 0.048$. This implies that SMEs that adopt strategies to expand into new markets or reposition themselves in existing ones are likely to experience improved performance. This finding is consistent with the study of Adebayo and Oluwaseun (2025), who reported that market innovation significantly improves SMEs' market performance in agricultural sector in Nigeria. However, it contrasts with the findings of Ibrahim and Nwankwo (2023), who found that market innovation, resource constrain limit the effect of market innovation. This result aligns with the Resource-Based View (RBV) theory, which emphasizes that firms can leverage innovative approaches to markets to strengthen competitiveness and enhance performance.

The second finding revealed that process innovation has a negative and insignificant effect on the performance of SMEs in Karu LGA, Nasarawa State, with $\beta = -0.167$, $t = 0.049$, and $p = 0.625$. This suggests that process changes among SMEs in the study area do not significantly contribute to performance and may even create disruptions in efficiency. This finding contrasts with the study of Eze and Tobi (2024), who found that process innovation positively influenced SMEs' productivity in Enugu State. However, it agrees with the findings of Muktar and Bello (2023), who reported that process innovation had no significant impact on the growth of small businesses in Kano. The result suggests that SMEs in Karu LGA may not yet have the structural or financial capacity to implement process innovations that positively affect performance.

CONCLUSIONS AND RECOMMENDATIONS

Conclusions

- Based on the findings, it can be concluded that market innovation has a positive and significant effect on the performance of SMEs in Karu LGA, Nasarawa State. This implies that SMEs that adopt new market strategies, customer-focused approaches, and market positioning achieve better performance outcomes.



- ii. The study finds that process innovation has a negative and insignificant effect on SME performance in Karu LGA, Nasarawa State. This indicates that changes in production processes or internal workflow improvements alone do not contribute significantly to overall performance in this context

Recommendations

- i. SME owners should prioritize market innovation by adopting customer-focused strategies, exploring new market niches, and enhancing their market positioning. By tailoring products and services to meet changing customer preferences, SMEs can strengthen competitiveness and achieve better performance outcomes.
- ii. While process innovation showed a negative and insignificant effect in this study, SME owners are encouraged to adopt it cautiously. Instead of focusing solely on internal workflow improvements, they should align process changes with customer needs, technology adoption, and strategic goals to derive meaningful performance benefits.

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