



ROAD TO SUCCESS: HOW DOES ENTREPRENEURIAL ORIENTATION AND MARKET ORIENTATION IMPROVE SME PERFORMANCE?

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Abstract: SMEs are one of the pillars of the economy that continues to move daily in carrying out its business activities. Each business field has different characteristics, but striving to develop a business and earn income is one of the main capitals to continue to advance. There are so many obstacles faced by MSME players to compete in the market so the management of business breakthroughs is important to support business development. Maintaining a business existence requires a strong entrepreneurial spirit so that it can achieve the desired business goals. Also, market orientation and entrepreneurship could positively impact SMEs' performance. In this study, it is explained that innovation also plays an important role in improving the performance of SMEs. A conceptual structural model that includes aspects of Market Orientation (MO), entrepreneurial orientation (EO), Innovation (I), and SME Performance (SMEP) is developed based on the concept and relationship results from the literature. This study examines the influence of entrepreneurial and market orientation on whether it has a direct or indirect impact on SME performance. This study investigates whether entrepreneurial orientation and market orientation affect the performance of SMEs using innovation mediation. The population of this study is small and Medium Enterprises (SMEs) in the city of Pacitan, East Java engaged in food and beverages, services, and production, with a sample of 100 SMEs. In research using Structural Equation Modeling (SEM) analysis tools and it is expected that this

research will have an impact on SMEs in the city of Pacitan, which focuses on how entrepreneurial orientation and market orientation have an impact on SME performance, both directly and indirectly, and how Innovation as a mediating variable can have a direct or indirect impact on entrepreneurial orientation and market orientation on SME performance.

Keywords: Entrepreneurship Orientation, Market Orientation, Innovation, SME Performance

INTRODUCTION

Small and medium enterprises (SMEs) contribute significantly to a country's economic growth by providing various job opportunities, using resources efficiently, increasing national income, and reducing poverty (Al Mamun et al., 2022). SMEs, considered the backbone of the Asia Pacific economy, employ a significant amount of the workforce, making nearly more than 96 percent of all jobs (Yoshino & Taghizadeh-Hesary, 2018). Therefore, Asian economies must have fully functional support measures for SMEs. According to data from the Ministry of Finance, Small and Medium Enterprises (SMEs) accounted for 64.2 million of the total number of business actors in Indonesia in 2018 (Sasongko, 2020). A total of 117 million SME workers, or 97% of the company's total workforce, were absorbed. Although they make up only 5,550, or 0.1% of all business users, large companies account for 38.9% of GDP in the country, while SMEs contribute 61.1% (Kementerian Koordinator Bidang Perekonomian, 2023). However, entrepreneurial and innovation orientation is a prerequisite for accelerating SME performance (Rezaei & Ortt, 2018),

and market orientation also affects company performance (Schulze, Townsend, & Talay, 2022).

The company cannot be studied in isolation from the internal and external environment for which it is responsible (Gomes, Seman, Berndt, & Bogoni, 2022). This is a clear relationship between corporate strategy, market uncertainty, and competition intensity. In such market conditions, turbulence decreases and stability becomes stronger, but corporate risk-taking impulses increase (Lukas, Tan, & Hult, 2001). (Moorman & Day, 2016) create an outline for future research methodologies by showing how the shift from product structure to customer structure impacts organizational success. For these authors, it is important to present an overview of effective strategies for transitioning from conventional systems to structures based on the argument that this can only succeed if the company already has a market-oriented culture. We responded (Schulze et al., 2022) to explore SME market orientation, incubate innovation, and improve SME performance. As a result, in addition to significant market orientation, innovation strategies, and value-based pricing, the study identified the level of profitability and variation of sales projections between constructs and market performance (De Toni, Reche, & Milan, 2022).

Governments are establishing policies that take into account SMEs' potential for innovation, nevertheless innovation action remains an involved issue, specifically for SMEs in nations that are developing. In Indonesia, SMEs are dominated by micro-enterprises, amounting to 98.68% with employment of around 89%. However, the contribution of micro-enterprises to GDP is only around 37.8%. For this reason, the

government encourages SMEs by taking policies to increase the capacity of micro and small enterprises so that they can be upgraded to medium enterprises (Sasongko, 2020). The program is strengthening SME capital through the People's Business Credit (KUR). Therefore, this concept of the wide range of performance displayed by manufacturing SMEs and their intimate connection to innovation and strategic focus. Consequently, we study how innovation in products and processes influences markets, consumers, entrepreneurial spirit, and business success in Indonesian small and medium-sized enterprises.

Entrepreneurial Orientation: Entrepreneurial Orientation (EO) is one of the most studied issues in the strategy and Literature of entrepreneurship (Kraus et al., 2012). EO is defined according to the literature definition, which states that EO is a firm's willingness to adopt innovative practices and take risks to introduce new products, services, and markets, and proactively move ahead of its competitors to take advantage of new opportunities in the market (Soininen et al., 2012). Meanwhile, according to Naman & Slevin (1993), the definition of entrepreneurial orientation is values related to the aim of finding new market opportunities and expanding the current area of activity. The majority of studies argue that the three main components of EO are; innovative, proactive, and risk-taking (Kraus et al., 2012; Li, Huang, & Tsai, 2009). However, research (Gomes et al., 2022; Li et al., 2009) defines different dimensions of EO, namely innovation and autonomy. However, the existing literature creates considerable debate regarding the dimensions of EO.

In (Miller, 1983) literature EO is "a three-dimensional concept: innovativeness, risk-taking, and proactivity". Lumpkin & Dess (2001) added dimensions of competitive aggression and autonomy. In this study, researchers will focus on innovativeness, risk-taking, and proactivity as EO dimensions to characterize and test entrepreneurship. The existing literature has long observed that EO improves performance, both implicitly and explicitly (Li et al., 2009). Rauch et al. (2009) found that financial performance and corporate MO and EO are positively related. Using a qualitative framework, Li et al., (2009) argue that EO orientation triggers long-term growth for SMEs while proposing that OM can also enable firms to achieve short-term competitive advantage. Recently, Nuvriasari et al., (2020) reported that the entrepreneurial orientation dimension improves the performance of Batik SME companies in Indonesia. Other studies have shown that entrepreneurial orientation has no significant effect on performance (Ahmatang & Sari, 2022).

According to several studies, innovation is the most important component of EO, and the results show a significant relationship between innovation and high performance (Li et al., 2009; Lumpkin & Dess, 2001). Innovation means a firm's ability to support new ideas, experiment, introduce new products, and use creative processes (Rauch et al., 2009; Soinenen et al., 2012). In today's business environment, SMEs force themselves to be more innovative than ever before as they have developed first-mover advantages with new products and services offered, resulting in high sales revenue, high market share, and better company performance (Ejdys, 2016; Kraus et al., 2012).

Proactive is the readiness to take actions that will encourage competitors' reactions. A proactive approach reflects an organization's participation in the market for emerging industries, the constant search and use of weak market signals, and rapid response to changing trends in the organizational environment (Miller, 1983). Proactive is a business's willingness to allocate resources to introduce new products and services before competitors (Rauch et al., 2009). According to research, business activity is highly correlated with how much a company continues to develop new products, improve existing products, and expand into new markets.

Risk-taking involves creating bold actions using large resources (Lumpkin & Dess, 2001). Organizational risk is an area of increasing concern that can support SMEs and their owner-managers in some capacity. In the case of innovative initiatives, it provides direction for decision-making regarding other options, increases confidence in project success, and reduces the risk of unforeseen events that can lead to delays and unnecessary expenses. Organizational risk is an ever-evolving area that can support SME owners and managers in some capacity (Brettel, Chomik, & Flatten, 2015). Accepting risk is an important component in the decision-making process for entrepreneurs trying to enter a new company, market, or product (Ejdys, 2016).

Market Orientation: Market orientation (MO) defines how much an organization values, supports, and promotes behaviors that conform to the marketing concept (Jaworski & Kohli, 1993). The organization's goals and culture, which focus on providing value to its clients in order to maintain its competitiveness, are reflected in its market orientation. (Siti, Surachman, Rofiaty, & Sabil, 2017). MO began to be researched

by pioneers such as (Morgan & Strong, 1998; and Narver & Slater, 1990). Based on (Narver & Slater, 1990) MO, there is a concentration on customers and competitors as well as the integration of corporate functions to create superior value for customers. Delivering more value to customers is seen as the key to long-term profit and competitive advantage.

Many research studies indicate that over the past few years, market orientation has been receiving a lot of discussion in the literature. This research adopts (Narver & Slater, 1990) the conceptualization of MO, which has been applied in the SME industry, according to emerging markets (De Toni et al., 2022; Nuvriasari et al., 2020). Such concepts include (1) orientation to competitors; (2) customer orientation; and (3) coordination between functions. These three elements, based on some previous research, offer a comprehensive picture of collecting, distributing, and utilizing market information in business (Narver & Slater, 1990).

Innovation: Entrepreneurial orientation is a key factor in the development and implementation of innovation. Entrepreneurial orientation about innovation is the object of research in the context of three main components of entrepreneurial orientation: innovativeness, risk-taking, and proactive (Miller, 1983) and types of innovation ((Li et al., 2009), innovation processes (Pérez-Luño, Wiklund, & Valle, 2011), and product innovation (Al Mamun et al., 2022; Nasir, Al Mamun, & Breen, 2017). Small and medium-sized enterprises (SMEs) need to create innovative performance (I) that guides them in developing new products and services, improving the quality of their

products and services, and building organizational structures that match the demands of the competitive environment.

Product innovation is the process when a company introduces new goods and services one after the other in order to satisfy customers in a market that is highly competitive. (Murmura, Bravi, & Santos, 2021). Product innovation is the process of providing a product with new features and improving its quality while continuing to meet growing market demand (Liu, Ding, Guo, & Luo, 2014). Process innovation is the application of technology to transform production processes or innovative methods of service delivery. Some researchers argue that process innovation can affect firm performance (Chen & Tsou, 2012; Mursid, Suliyanto, & Rahab, 2019; Tsou & Cheng, 2018) and entrepreneurial orientation (Liu et al., 2014; Pérez-Luño et al., 2011). Product and process innovations increase companies' capacity to solve them and allow them to do so sustainably (Arboretti, Ceccato, Pegoraro, & Salmaso, 2022)

SME Performance (SMEP): Performance is the capacity of a business to produce output. In the 1980s, Michael Porter defined a company's performance as dependent on its ability to create value for its clients (Rezaei & Ortt, 2018). Today, company performance has become a relevant concept in strategic management research and is often used as a dependent variable. Measurement of a company's return on investment, growth, volume, profit, and labor is generally done to determine the company's performance (Kaplan & Norton, 1993). Based on existing literature and empirical studies, there are several indicators used in this study to measure company performance, namely sales growth, asset growth, and profit growth.

METHODS

The exogenous variables within this study have market orientation and entrepreneurial orientation. The performance of SMEs is the endogenous variable, and innovation is the mediating variable. The following is the operational definition of the variable, namely:

1. Entrepreneurial orientation is an aspect of SMEs that encourages them to make various innovative efforts for the sustainability and progress of the business.
2. Market orientation is an effort to have competitiveness to survive and develop the market
3. Innovation is a form or result that indicates something new and a change in the development of efforts
4. SME performance is an effort result that shows an increase in business

In taking data from the responses, is carried out through filling in the questionnaire the measurement of the variables is determined according to the expected purpose, and then data analysis using the PLS-SEM program to see the influence of the three variables.

Instrument Development

First, with the help of an extensive literature review, there were seven potential sources used to create the questionnaire. Researchers used an 18-item measurement scale to measure the underlying structure contained in the questionnaire (attached). Scale of entrepreneurial orientation adapted from Li, Huang, & Tsai, 2009; Sadiku-Dushi, Dana, & Ramadani, 2019 includes 4 items. Market orientation includes 5 scale items adapted from Morgan & Strong, 1998; Narver & Slater, 1990, the innovation performance scale includes 4 items in a form

adapted from Liu, Ding, Guo,& Luo, 2014; Miller, 1983. SME Performance is measured by 5 item scale adopted from (Kaplan & Norton, 1996; Sadiku-Dushi, Dana, & Ramadani, 2019)

(1) Sample and Data Collection: This investigation aims to find out how the sample elements are SME owners in Pacitan, East Java. We selected SMEs that were established within 3 to 5 years. A questionnaire survey was created to collect comments from new entrepreneurs about their perspectives on various topics. A total of 100 questionnaires were distributed. A preliminary analysis was conducted to provide information on the characteristics of the sample in Table 1. The data obtained from the questionnaires were analyzed with the PLS SEM program. All constructs have been operationalized using a 5-point Likert scale, ranging from (1) Strongly Disagree; (2) Disagree; (3) Disagree and Disagree; (4) Agree; and (5) Strongly Agree.

(2) Conceptual Structural Model and Hypothesis Development

A conceptual structural model covering aspects of Entrepreneurial Orientation, Market Orientation, Innovation, and SME Performance is developed based on concepts and relationship results from the literature as shown in Figure 1

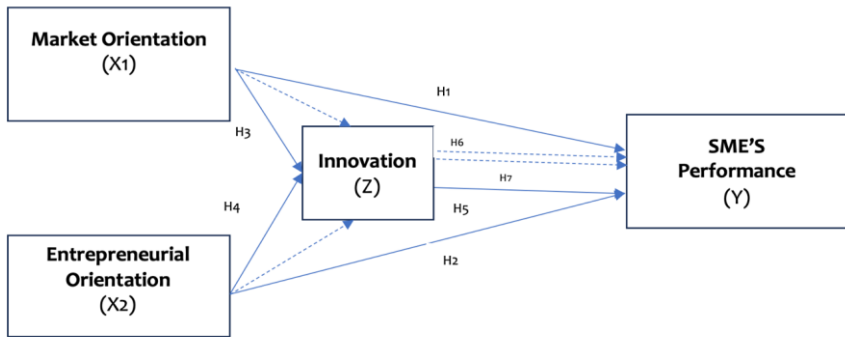


Figure 1. Conceptual Structural Model

A hypothesis is a provisional conjecture that has not been proven true and is used to explain a fact. The hypothesis development of this study is explained as follows:

RESULT AND DISCUSSION

The relationship between entrepreneurial orientation and SME performance

One of the relevant studies is the one conducted by Ahmatang, Ahmatang, & Sari, N. (2022). The results showed that entrepreneurial characteristics had a significant positive influence on entrepreneurial competence, but did not have a significant influence on SME performance. On the other hand, entrepreneurial competence has a significant positive influence on the performance of SMEs. The study also found that entrepreneurial competence mediates the relationship between entrepreneurial characteristics and SME performance. These findings demonstrate that SMEs must strengthen their entrepreneurial competencies to increase their performance. Drawing from prior research findings, the following conjectures can be made:

H1: It is suspected that there is a positive and significant influence between Entrepreneurial Orientation on SME Performance.

The relationship between market orientation and SMEs' performance.

Amalia et al.'s (2018) study looks at how market orientation and entrepreneurial orientation affect small- and medium-sized businesses' (SMEs') success in the retail industry. The findings demonstrated that while market orientation has a positive and significant impact on SME performance, entrepreneurial orientation also has a positive and significant impact. This study highlights how crucial it is to have sound entrepreneurship. To enhance the performance of SMEs in the retail industry, this research highlights the need to embrace a strong entrepreneurial and market orientation. Furthermore, Nuvriasari et al. (2020) clarified that market orientation has a big impact on SMEs' performance. The performance of SMEs is significantly impacted by entrepreneurial orientation as well. Human capital can also have an impact on MSMEs' performance and market orientation. Drawing from prior research findings, the following conjectures can be made:

H2: It is suspected to be a positive and significant correlation between market orientation and SMEs' performance. The relationship between innovation and SME performance

The relationship between market orientation to innovation

Schulze et al. (2022) found that market orientation and innovation have a positive and significant influence on the performance of SMEs. Innovation is also identified as the process of turning opportunities into ideas that can improve the performance of

SMEs. Based on the results of previous research, the following hypotheses can be drawn:

H3: It is alleged that there is a positive and significant influence between Market Orientation on innovation

The relationship between entrepreneurial orientation toward innovation

Entrepreneurial orientation refers to processes, practices, and decision-making that push toward new inputs and has three entrepreneurial aspects, namely always innovative, acting proactively, and daring to take risks (Rahmadi et al., 2020). Research has shown that entrepreneurial orientation has a positive and significant influence on innovation (Rahmadi et al., 2020). Based on the results of previous research, the following hypotheses can be drawn:

H4: It is thought that there is a positive and significant influence between entrepreneurial orientations against innovation

The relationship between innovation and SMEs' performance.

Innovation has a significant relationship with SME performance. Research by Amilia et al (2018) found that market orientation, entrepreneurial orientation, and innovation have a positive and significant influence on the performance of SMEs in the convection sector in West Jakarta. The results of this study show that entrepreneurial orientation paves the way for the strategic direction of SMEs to achieve better business performance. In addition, innovation is also identified as a process to turn opportunities into ideas that can improve the performance of SMEs. In addition, the research of Al Mamun et al (2022) also produced a positive influence. Based on the results of previous research, the following hypotheses can be drawn:

H5: It is suspected that there is a positive and significant influence between Innovation on SME Performance

The Relationship of Market Orientation to SME Performance Through Innovation

Product innovation also has an important role in mediating the influence between market orientation and SME performance. Research by Rachmasari and Suprpti (2022) shows that product innovation can be a mediator between market orientation and SME performance. In this study, product innovation is measured through new product development, product improvement, and product diversification. The results of this study show that product innovation has a positive and significant influence on the performance of SMEs. Based on the results of previous research, the following hypotheses can be drawn:

H6: It is suspected that there is a positive and significant influence between Market Orientation on SME Performance through Innovation

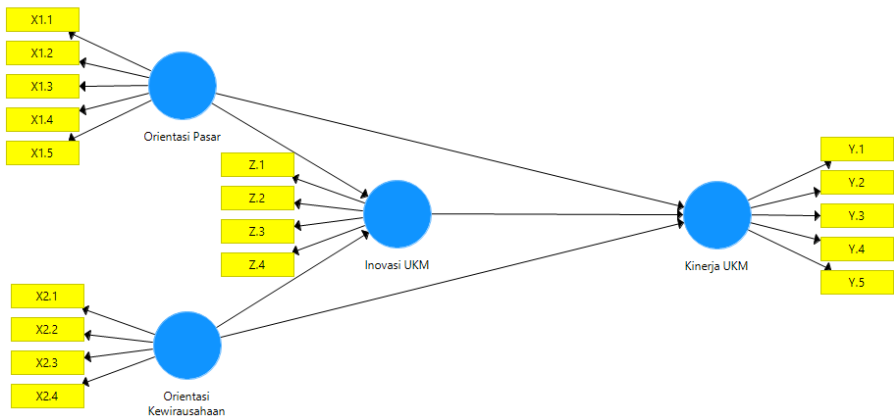
The Relationship of Market Orientation and Entrepreneurial Orientation to SME Performance Through Innovation

According to Putra & Setiawan (2019) their research found that innovation mediates the relationship between entrepreneurial orientation, company resources, small and medium enterprises Branding on company performance, this research was conducted on small and medium enterprises. In addition, Sulaeman (2018) found that entrepreneurial orientation toward company performance in the creative industry can be mediated by innovation. Based on the results of previous research, the following hypotheses can be drawn:

H7: It is suspected that there is a positive and significant influence between Entrepreneurial Orientation towards SME Performance through Innovation

DISCUSSION

Data is processed using Smart PLS 3.0. The initial model of correlation between variables as shown in the figure below.



Model evaluation (*outer model*) was carried out by converging and discriminant validity tests by looking at the *loading factor value of ≥ 0.6* and *Average Variance Extracted (AVE) > 0.5* . The *loading factor* and AVE values are listed in the table below.

Table 2. Initial *Model Loading Factor* and AVE Value

Indicator	Loading Factor	AVE	Indicator	Loading Factor	AVE
X1.1	0.73	0,6	X2.1	0.707	0,521
X1.2	0.856		X2.2	0.534	
X1.3	0.613		X2.3	0.772	
X1.4	0.817		X2.4	0.84	
X1.5	0.832				
Z.1	0.623	0,538	Y.1	0.833	0,628
Z.2	0.835		Y.2	0.783	
Z.3	0.62		Y.3	0.74	
Z.4	0.826		Y.4	0.703	
			Y.5	0.889	

The results of the convergent validity test in Table 1 show that there are two indicators that have a *loading factor value* of less than 0.6, namely indicators X1.3 and X2.2 so that these indicators must be excluded from the model. After the indicator was issued, another analysis was carried out and a second model was obtained as shown below.

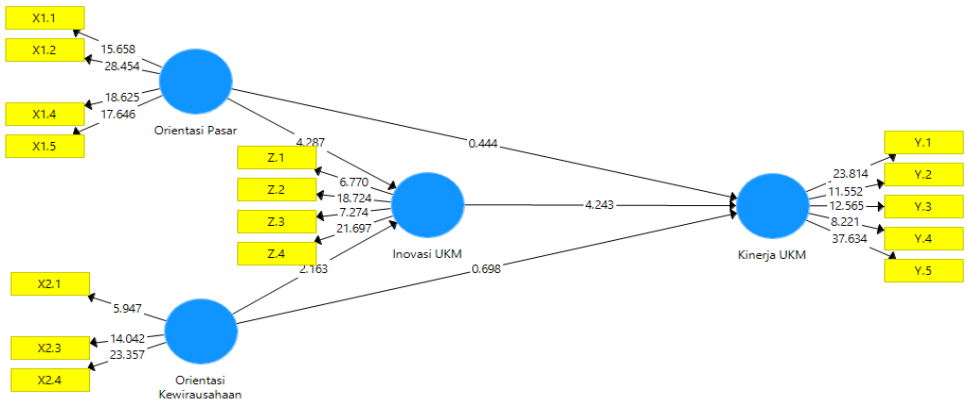


Table 3. Final Model Loading Factor and AVE Value

Indikator	Loading Factor	AVE	Indikator	Loading Factor	AVE
X1.1	0.771	0,676	X2.1	0.677	0,634
X1.2	0.853		X2.3	0.823	
X1.4	0.825		X2.4	0.876	
X1.5	0.838				
Z.1	0.626	0,538	Y.1	0.832	0,628
Z.2	0.833		Y.2	0.78	
Z.3	0.604		Y.3	0.741	
Z.4	0.837		Y.4	0.706	
			Y.5	0.889	

The results of the convergent validity test in Table 2 show that all indicators already have a *loading factor* value of more than 0.6 and an AVE value for each variable construct of more than 0.5 so that it can be said that in this final model the convergent validity has been met and further analysis can be carried out, namely the discriminant validity test. This test is performed using *the fornell-lacker criterion*. The results of the discriminant validity test are shown in the table below.

Table 4. Final Model Discriminant Validity Testing

	Z	Y	X2	X1
Z	0.733			
Y	0.512	0.792		
X2	0.614	0.276	0.796	
X1	0.68	0.358	0.688	0.822

Based on Table 3, it is obtained that the correlation between constructs is already smaller than the AVE root so all construct variables have met the validity of the discriminant. After the model has met the convergent validity and discriminant validity, it proceeds with composite reliability testing. The results of composite reliability testing are shown in the following table.

Tabel 5. Pengujian Relibilitas Model Akhir

Variabel	Composite Reliability
Z	0.82
Y	0.893
X2	0.837
X1	0.893

Based on the results of reliability testing in Table 4, it is obtained that all variables are reliable because they have a *composite reliability* value greater than 0.7. The structural model or *inner model* describes the correlation between latent variables in research evaluated with several test criteria, namely coefficient of determination, and parameter coefficient with t-statistical tests obtained by the bootstrapping process. The results of the bootstrapping analysis are summarized in the table below.

Table 6. Direct Effect, Indirect Effect, and Total Effect

Hypothesis	Relationship	Direct effects	Indirects effects	Direct and Indirect effects
		P-value	P-value	P-value
H1, H6	OK-K	0,487	0.048	0.572
H2, H7	OP-K	0,658	0.011	0.002
H3	I-K	0,00	0	0,00
H4	OK-I	0,033		0,033
H5	OP-I	0,00		0,00

Based on the results of the above tests it was obtained that

1. The relationship between entrepreneurial orientation and SME performance

The direct influence of entrepreneurial orientation on SME performance shows a p-value of 0.487 which does not support H1, so it can be said that there is no influence of entrepreneurial orientation on SME performance.

2. The relationship between market orientation and SME performance

The test results show a p-value for the direct influence of market orientation on performance of 0.658 which does not support H2 so there is no influence between market orientation on SME performance. While the indirect influence between market orientation on SME performance through SME innovation has a p-value of 0.011 which is smaller than 0.05, so it can be said that market orientation has an influence on SME performance through SME innovation

3. The relationship between innovation and SME performance

SME innovation has an influence on SME performance with a p-value on the influence or direct effect of 0.00. This supports H3 which says that SME innovation affects SME performance

4. The relationship between entrepreneurial orientation toward innovation

Furthermore, the direct influence between entrepreneurial orientation and SME innovation has a p-value of 0.033 which is smaller than 0.05 in favor of H4. So it can be said that entrepreneurial orientation affects SME innovation

5. The relationship between market orientation to innovation

The latest test results show that the direct influence of market orientation on innovation with a p-value of 0.000 is less than 0.05 in favor of H5. So it can be said that market orientation affects SME innovation

6. The Relationship of Entrepreneurial Orientation to SME Performance Through Innovation

Based on the indirect influence of entrepreneurial orientation on SME performance through SME innovation, a p-value of 0.048 is obtained where the value is less than 0.05 which supports H6 that there is an influence of entrepreneurial orientation through SME innovation on SME performance. then the results of the direct and indirect influence of entrepreneurial orientation on SME performance through SME innovation obtained a total influence p-value of 0.572

7. The Relationship of Market Orientation to SME Performance Through Innovation

By the indirect influence of market orientation on SME performance through SME innovation, a p-value of 0.658 is obtained where the value supports H7 that there is an influence of market orientation through SME innovation on SME performance. Meanwhile, the influence of total market orientation on the performance of SMEs through innovation obtained a p-value of 0.002.

Tabel 7. Koefisien Determinasi

	R Square	Adjusted R Square
SME Innovation	0.503	0.494
SME Performance	0.266	0.245

The structural model is then assessed through coefficient determination to see the goodness of the model that has been made. Based on the test results, a coefficient of determination for SME innovation of 50.3% was obtained which entered the criteria is strong enough where entrepreneurial orientation and market orientation can explain the variability of SME innovation, and the rest is explained by other variables that are not studied. Likewise, the performance of SMEs with

a coefficient of determination value of 26.6% which is included in the category is quite strongly explained by the latent variables of market orientation, entrepreneurial orientation, and SME innovation, and the rest is explained by other variables.

CONCLUSION

Based on the results of the study, it shows that market orientation and entrepreneurship have a significant influence on the performance of SMEs through SME innovation because with innovation, it will provide a breakthrough for market development and foster entrepreneurial spirit by striving to continue to create more quality products so that they can be accepted by consumers

The improvement of SME performance is also influenced by other factors that have not been included in the variables in this study so that it can be the focus of future research.

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