

Competitive Advantage to Mediate the Influence of Entrepreneurial Orientation, Product Innovation on SMEs Business Performance

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Abstract

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Advantage

Previous research on entrepreneurial orientation and the impact of innovation with the moderating role of competitive advantage of Micro, Small and Medium Enterprises (SMEs) is still within the scope of limited studies. Therefore, many other studies are needed to analyze the impact of these variables on the performance of SMEs. This study was conducted to analyze the moderating role of competitive advantage on the effect of entrepreneurial orientation, product innovation, on business performance. The sampling method was purposive sampling, with a total of 306 respondents from SMEs in Magelang Regency. The analytical tool in this research is multiple regression analysis with SPSS 25.0. The results of this study indicate that competitive advantage can mediate the effect of entrepreneurial orientation, product innovation on business performance. In addition, this study also confirmed that there is a positive effect of product innovation and entrepreneurial orientation on SMEs business performance. The findings of this study contribute to expanding relevant knowledge about the impact of product innovation, entrepreneurial orientation on business performance with moderation of SMEs' competitive advantage. Regarding practical implications, policy makers should realize that adopting entrepreneurial orientation and product innovation will improve business performance if they pay attention to the competitive advantages of SMEs.

Abstrak

Kata kunci:
Orientasi
Kewirausahaan;
Inovasi Produk;
Kinerja Bisnis;
Keunggulan
Bersaing

Penelitian sebelumnya tentang orientasi kewirausahaan dan dampak inovasi dengan peran moderasi keunggulan bersaing Usaha Mikro, Kecil, dan Menengah (UMKM) masih dalam lingkup studi terbatas. Oleh karenanya, perlu banyak penelitian lain untuk menganalisis dampak variabel tersebut terhadap kinerja UMKM. Penelitian ini dilakukan untuk menganalisis peran moderasi keunggulan bersaing pada pengaruh orientasi kewirausahaan, inovasi produk, terhadap kinerja usaha. Metode pengambilan sampel melalui purposive sampling, dengan jumlah responden 306 pelaku UMKM di Kabupaten Magelang. Alat analisis dalam penelitian ini adalah analisis regresi berganda dengan SPSS 25.0. Hasil penelitian ini menunjukkan bahwa keunggulan bersaing dapat memediasi pengaruh orientasi kewirausahaan, inovasi produk terhadap kinerja usaha. Selain itu, penelitian ini juga mengkonfirmasi bahwa ada pengaruh positif inovasi produk dan orientasi kewirausahaan terhadap kinerja usaha UMKM. Temuan penelitian ini berkontribusi untuk memperluas pengetahuan yang relevan tentang dampak inovasi produk, orientasi kewirausahaan terhadap kinerja UMKM dengan moderasi keunggulan bersaing. Terkait implikasi praktis, pengambil kebijakan harus menyadari bahwa mengadopsi orientasi kewirausahaan dan inovasi produk akan meningkatkan kinerja bisnis jika memperhatikan keunggulan bersaing UMKM.

1. Introduction

SMEs majorly contribute to economic development and account for more than 90% of the world's enterprises (Ferreira et al., 2020). SMEs are essential for reducing unemployment rates by creating jobs, reducing poverty, and creating wealth for developing

countries' economic systems, including Indonesia. Therefore, developing SMEs is very important for the improvement of the nation's economy. According to existing literature, entrepreneurial orientation is a key factor contributing to business success during and after the crisis by enabling SMEs to take risks for new products, improve their performance, achieve competitive advantage, and sustain growth (Choi & Williams, 2016). However, despite this major role - SMEs suffer from a lack of financial, technical, and managerial resources, which can negatively impact performance (V.-H. Lee et al., 2016).

The development of SMEs has become one of the key points for governments around the world (Gherghina et al., 2020). Likewise, the limited resources available require all SMEs to use innovation to improve organizational performance. This product innovation can occur due to several factors, including the economic level of consumers which affects their needs, fashion demands and needs, and affordable prices (Shah & Ahmad, 2019). This innovation process must be carried out continuously so that the product continues to develop, improve, and achieve perfection, which can be done by utilizing science and technology. Product innovation should be able to meet the needs of current consumer behavior (Hunter & Lean, 2014). Product innovation is also carried out, because products that get innovation are given additional product modes, product quality, product improvements and product functions can improve business performance. Goods with new features or capabilities will increase the superiority of previous goods. So, in other words, goods that are given innovation will increase their superiority. Product innovation can sustain business and improve business performance.

Meanwhile, *Entrepreneurial Orientation* (EO) describes new ways of entrepreneurial activities related to business performance. Entrepreneurship experts state that EO is an important factor that determines the performance of SMEs (George et al., 2001; Graham, 2022). EO is suggested to be a key capability that enables SMEs to build their competitive advantage (Brouthers et al., 2009). In particular, EO increases the willingness to innovate and take risks, as well as the tendency to act faster than their competitors and anticipate future customer demands. Therefore, EO makes it possible to better utilize internal resources and acquire and exploit external resources more efficiently (Wiklund & Shepherd, 2003).

All those statements translate into better performance. The direct relationship between EO and performance is complex (Anderson & Kimball, 2019). Empirical evidence shows mixed results, some studies show a positive relationship (Covin et al., 2006; Covin & Slevin, 1991; Ireland et al., 2009; Lumpkin & Dess, 1996; Wiklund & Shepherd, 2003), while some studies show a negative relationship (T. Lee & Chu, 2017) and also no relationship. To explain such mixed results, EO scholars (Lumpkin & Dess, 1996; Wiklund & Shepherd, 2003) argue for examining other factors that influence this relationship. One approach is to examine the indirect effects of EO on performance through mediating factors (Cossío-Silva et al., 2016). Assessment of indirect effects enables an understanding of the mechanisms underlying the indirect impact on business performance (Wales et al., 2013). Therefore, it is necessary to explore new mediators to contribute to the EO literature. In relation to competitive advantage, previous research has focused on differentiation strategies rather than the mediating role of these variables. The mediating role of competitive advantage is novel

in this study. Competitive advantage is stated as a factor that leads to performance sustainability (Budiati et al., 2022; Shah & Ahmad, 2019). Entrepreneurial-oriented approaches and product innovation are more likely to improve business performance through its competitive advantage.

The critical issues that drive this research are formulated in the following basic questions: (a) how do *EO* and product innovation affect SMEs business performance? (b) how do EO and product innovation affect SMEs competitive advantage? and (3) how can *competitive advantage* mediate the effect of *entrepreneurial orientation* and product innovation on SMEs business performance? The conceptual framework to answer the critical research problems is illustrated as follow **Figure 1**.

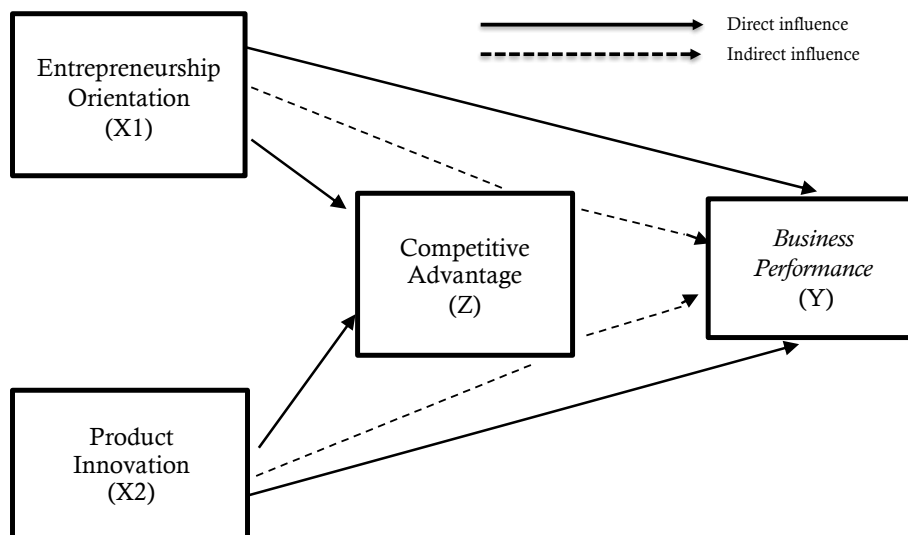


Figure 1. Research conceptual framework

2. Literature Review

The relationship between *Entrepreneurial Orientation* (EO) and performance as well as product innovation and performance can be explained using the *Resoucers Based View* (RBV). This view states that when organizations successfully combine their resources and/or capabilities together, they obtain superior performance (Barney, 1991). According to the resource-based view, EO and innovation can have an impact on performance. Barney (1991) explains how and why an organization's resources and competencies maintain its competitive advantage to gain superior performance. Therefore, organizational resources and capabilities are critical to improving organizational performance (Penrose, 1995). On the other hand, product innovation variable is one of the main keys in the success of a product in winning the competition, so that it can be accepted directly by consumers (Chen et al., 2020). Companies are required to prepare various innovative ideas for business ventures that are run so that they are superior to market competitors. The company's success in innovation can be said if the company is one step ahead of its competitors. Therefore, creativity and ingenuity are needed in innovating so as to enable the creation of competitive advantages in the company's performance (Wang et al., 2019). The RBV approach is used because there is

an understanding of the relationship between resources, capabilities, competitive advantage and profitability. Especially in understanding the mechanism of maintaining competitive advantage over time. The success of a company is determined by its resources and capabilities. Both tangible and intangible data sources. However, to find performance implications, these resources and capabilities must be valuable and rare. In addition, these resources and capabilities must be difficult for competitors to imitate in order to be more competitive. Finally, organizations must manage these resources and capabilities well to sustain their competitive advantage, and in turn, sustain the firm's business performance.

In general, entrepreneurship is related to introducing new products/services, while some corporate practices and behaviors are considered as entrepreneurial attitudes capable of supporting becoming an entrepreneur. From a historical aspect, EO investigations have mainly concentrated on entrepreneurship at the firm level. EO theory originated from the strategy creation process literature and has become important in entrepreneurship and strategic management literature. Currently, theoretical and empirical attention to EO is increasing to determine its impact on firm performance.

One of the important factors of business success is an organization's ability to create innovation. Many management researchers pay attention to the phenomenon of innovation. Innovation is defined as the application of new ideas to structure activities, unique tactics to divide responsibilities, and new ways to organize relationships with other companies or stakeholders. Companies must remain innovative to maintain competitiveness; otherwise, they will not survive in a dynamic environment.

From this point of view, performance is the company's ability to handle all organizational processes to achieve relevant goals and effectively perform organizational maintenance & adoption activities. Firm performance consists of several dimensions; its indicators are related to non-financial performance and financial performance related to production and marketing. Previous studies consider growth and profit as indicators of firm performance. Therefore, profit, revenue, growth, productivity, efficiency, and new markets determine organizational performance. Although some studies suggest that innovation is significantly related to firm performance, some studies suggest a negative relationship. For example, innovation negatively affects firm growth, which is consistent with the claim that ignoring the potential negative impact of innovation can lead to uncontrolled business growth. Despite doubts about possible negative impacts, most previous studies support a positive correlation between product innovation and SMEs business performance.

Competitive advantage is a strategic process that can create opportunities for companies to get higher profits than their competitors (Ngo, 2023). Porter defines competitive advantage as a benefit strategy of companies that cooperate to compete more effectively. The new strategy is designed to realize *sustainable competitive advantages*. To achieve the success of this strategy, companies must identify both *tangible* and *intangible* assets and resources that make the organization unique.

3. Method

The sampling method in this study used *purposive* and *quota sampling* techniques. The samples are MSMEs in the Borobudur National Tourism Strategic Area (KSPN) of Magelang Regency. Determination of this location by judgment that SMEs in tourist destination areas experience a more dynamic level of competition. SMEs are required to identify their competitive advantages so that their business sustainability is guaranteed. The sample criteria used are SMEs that have been established for 2 years or more. This criterion is based on the assumption that SMEs have experienced the process of maintaining their business sustainability. The number of samples in this study used the Slovin formula, (1960). The number of SMEs actors is 1312 and the percentage of standard error used is 5%. The sample results in this study were 306.5 which were rounded up to 306 samples. This study uses multiple linear regression analysis to test the hypothesis.

There are four variables developed in this study, the operational definition of each variable is as follow [Table 1](#).

Table 1. Variable names and indicators

Variable Name	Definition	Indicator
<i>Entrepreneurial Orientation</i> Covin & Slevin (1991), Lumpkin & Dess (1996)	It is the orientation of the entrepreneur's mind in realizing his ambitions, relating to the processes, practices and decision-making that lead to new ventures.	- Ability to innovate - Dare to take risks - Proactive
<i>Product Innovation</i> Falahat et al. (2020); Kristinae et al. (2023).	Is a process or activity to develop new ideas into profitable products.	- Product modification - Use of modern technology - New product creation - Product culture innovation
<i>Business Performance</i> Wiklund J and Shephend, (2003)	Is the company's ability to benefit from its resources and achieve its goals.	- Sales Growth - Capital Growth - Market Growth - Profit Growth
<i>Competitive Advantage</i> Bharadwaj et al. (1993)	Is the ability obtained through the characteristics and resources of a company to have higher performance and capabilities than other companies in the same industry or market.	- Price - Product quality - Market time - Product uniqueness

4. Results and Discussion

With a total of 306 respondents in accordance with the sampling criteria, the results of distributing questionnaires can be described as following [Table 2](#). The validity test with a total of 306 respondents found that all variable statements submitted to respondents were valid (r value > r table 0.112). Meanwhile, the reliability test provides an explanation that all research variables have a *Cronbach's Alpha* value > 0.7. (Hair et al., 2019). So that entrepreneurial orientation, product innovation, *business performance* and competitive advantage are reliable. The results of multiple linear regression analysis using statistical aids obtained regression coefficient values presented in the [Table 3](#).

Table 2. Frequency distribution

Conditions	Criteria	Amount	%
Gender	Male	139	45%
	Female	167	55%
Age	< 20	5	2%
	20-30	58	19%
	31-40	92	30%
	41-50	87	28%
	>50	64	21%
Level of Education	Elementary School	21	7%
	Junior High School	93	30%
	Senior High Scholl	168	55%
	Diploma	8	3%
	Scholar	16	5%

Table 3. Multiple linear regression test results

Model	Business Performance				Competition Advantage			
	B	Std. Error	t	sig	B	Std. Error	t	sig
(constant)	2.088	1.091	1.914	0.050	7.792	1.360	5.728	0.000
Entrepreneurial Orientation	0.647	0.043	14.985	0.000	0.413	0.051	8.033	0.000
Product Innovation	0.132	0.041	3.201	0.002	0.182	0.053	3.438	0.001
Competitive Advantage	0.132	0.044	3.018	0.003	-	-	-	-
F		127.561		0.000		44.828		0.000
Adjusted R-square		0.555				0.223		

Regression Equation 1:

$$Z = 7.792 + 0.413X1 + 0.182X2 + e \quad (1)$$

Regression Equation 2:

$$Y = 2.088 + 0.647 X1 + 0.132X2 + 0.132Z + e \quad (1)$$

The Adjusted R-Square value is 0.555, indicating that the variables of *Entrepreneurial Orientation*, product innovation, and competitive advantage in influencing *business performance* and have a positive and significant effect of 55.5% on *business performance*, and the remaining 44.5% is influenced by variables other than the variables in this study. In addition, based on the Adjusted R-Square value, a value of 0.223 is obtained, showing that the contribution of the *Entrepreneurial Orientation* variable and product innovation in influencing competitive advantage has a positive and significant effect of 22.3% and the remaining 77.7% is influenced by variables other than variable i in this research. Based on the F test that has been carried out, the value of F count > Ftable. Because F count > Ftable, Ho is not accepted or Ha is accepted. This shows that the research model used in this study is good (fit) to be tested.

4.1. The Effect of Entrepreneurial Orientation on Business Performance

This study shows that the hypothesis is supported for the effect of *Entrepreneurial Orientation* has a positive effect on *business performance*. EO shows how important entrepreneurial dimensions (risk-taking, proactivity, autonomy, innovativeness, and competitive aggressiveness), which of course have an impact on company performance.

These components collectively influence how SMEs respond to market opportunities and challenges. [Fatikha et al. \(2021\)](#) noted that a proactive approach allows firms to identify and exploit new market opportunities, thereby enhancing their competitive advantage and overall performance. In addition, EO is a strategy creation process that distinguishes entrepreneurship in business. Furthermore, in the existing literature, EO is one of the company's strategies to improve company performance. [Al-Momani et al., \(2023\)](#) said that the role of entrepreneurs is said to be quite high in running a business, especially in terms of entrepreneurial orientation, so it can be assessed that the business is running smoothly. [Kottika et al., \(2020\)](#) said that the role of entrepreneurs is said to be quite high in running a business, especially in terms of entrepreneurial orientation, so it can be assessed that the business is running smoothly. [Siregar \(2020\)](#) indicating that firms with strong EO are more likely to achieve better outcomes. This aligns with the findings of [\(Nti & Osei, 2022\)](#) who emphasized that entrepreneurial management practices are critical for enhancing the performance of SMEs.

4.2. The Effect of Product Innovation on Business Performance

From this study, the results of product innovation have a positive effect on business performance, so that the hypothesis is supported. Product innovation is an effort made by businesses that produce products to improve, perfect and develop products produced so far into superior products. Products developed in the form of goods, with innovation is a series of developments by applying science and technology to a product. This product innovation is caused by several things, including the economy of customers who influence needs, the combination of fashion and needs and affordable prices ([Falahat et al., 2020; Kristinae et al., 2023](#)). This innovation process must be carried out continuously so that the product continues to develop, improve, and achieve perfection by utilizing science and technology. Relationship product innovation capability in business is the ability to form and various organizational capabilities to improve activities to improve the business performance of new products. Along with the changing times and needs, the goods created will increasingly become obsolete because they cannot meet the needs of the present, it is necessary to innovate in order to meet the needs of current consumer behavior ([Montiel, 2013](#)). Product innovation is also carried out, because products that get innovation are given additional product modes, product quality, product upgrades and product functions that can improve business performance. Goods with new features or capabilities will increase the superiority of previous goods. So, goods that are given innovation will increase their superiority. Product innovation is an idea carried out by business actors in creating a product, improving product quality, improving and developing products that have been produced as long as the company is running, with the creation of innovative products, it will increase competitive advantage.

4.3. The Effect of Entrepreneurial Orientation on Competitive Advantage

These results conclude that entrepreneurial orientation has a positive effect on competitive advantage, so the hypothesis is supported. Entrepreneurial orientation is identified as one of the many factors that can affect performance, because it can determine

the direction of motion of a business that has been run / pioneered. Choi & Williams, (2016) said entrepreneurial orientation has 3 dimensions, namely: innovation, risk taking, and proactivity. (Pratono et al., 2019) emphasize that firms with high EO are more likely to achieve sustainable competitive advantages through increased inter-organizational learning and adaptability. This adaptability allows firms to respond effectively to market changes and capitalize on new opportunities. This is in accordance with research conducted Feriyansyah & Febriansyah, (2023), Budiati et al., (2021) and Farhan et al., (2022) suggest that there is a positive influence between entrepreneurial orientation and *business performance*. Based on research conducted by Rahmadi et al., (2020) shows that entrepreneurial orientation has a positive influence on competitive advantage. This is also supported by Asad et al., (2021) who stated in their research that entrepreneurial orientation has a positive and significant relationship with competitive advantage.

4.4. The Effect of Product Innovation on Competitive Advantage

This study found that product innovation has a positive effect on competitive advantage, so the hypothesis is supported. Existing literature shows that innovation directly affects business performance and can lead to competitive advantage (Udriyah et al., 2019). Similarly, previous research shows a significant correlation between innovation and the company's competitive advantage (Saunila et al., 2014). Different types of innovative developments are related to several performance factors. Moreover, the design and implementation of a strong innovation strategy results in better financial performance, process performance, customer performance, and growth performance. In addition, previous research shows that technology improves business stability, growth, and success. This is in accordance with the results of the research Hasnatika & Nurnida, (2019) which states that there is a positive and significant influence between product innovation and competitive advantage.

This research is also supported by Wang et al., (2019) stated that there is a positive and significant influence between product innovation and competitive advantage. This is in line with research conducted by Uyun & Rulirianto, (2023) suggests that there is a positive and significant influence between product innovation and competitive advantage. The success of the company in carrying out product innovation makes it easier for the company to achieve the expected sales targets. Innovation is also important in SMEs, where competition is currently getting tighter. With the implementation of innovation, business actors need to conduct research regarding changes or improvements that can be applied to their products. SMEs must also be able to find alternatives to the production process of goods with the aim of improving product quality. In product innovation, SMEs actors are directed to be able to apply new methods or alternative production strategies. All efforts made are aimed at improving the performance of the SMEs.

4.5. The Effect of Competitive Advantage on Business Performance

This study found that competitive advantage has a positive effect on business performance, so the hypothesis is supported. This innovation process must be carried out continuously so that the product continues to develop, improve, and achieve perfection,

which can be done by utilizing science and technology. Product innovation should be able to meet the needs of current consumer behavior (Montiel, 2013). This is in accordance with research Hoiron et al., (2019) that there is a positive and significant influence between competitive advantage and business performance. This research is also supported by research Sukmamedian, (2021) which states that there is a positive and significant influence between competitive advantage and business performance. This is also in line with research Ahmatang & Sari, (2022) which states that there is a positive and significant influence between competitive advantage and business performance.

4.6. Mediating Role of Competitive Advantage on the Effect of Entrepreneurial Orientation and Product Innovation on SMEs Business Performance

Based on the results of the sobel test calculation, the t_{count} is greater than the t_{table} ($2.842 > 1.650$). This test shows that competitive advantage can mediate entrepreneurial orientation on business performance, so the hypothesis is supported. EO is suggested to be a key capability that enables SMEs to build their own competitive advantage (Brouthers et al., 2009). In particular, EO increases the willingness to innovate and take risks, as well as the tendency to act faster than their competitors and anticipate future customer demands. Therefore, EO makes it possible to better utilize internal resources and acquire and exploit external resources more efficiently (Wiklund & Shepherd, 2003). This is consistent with research from Ahmatang & Sari, (2022) where there is a positive and significant effect on *Entrepreneurial Orientation on business performance* and competitive advantage significantly mediates the relationship between *Entrepreneurial Orientation on business performance*.

The mediating role of competitive advantage on the effect of EO on business performance will be realized if the company implements value creation strategies not simultaneously with the strategies implemented by existing or potential competitors. Companies must have the ability to differentiate the products produced in competition to gain competitive advantage. EO triggers the creation of products that have key characteristics in capturing consumers so that they become special products.

4.7. The Mediating Role of Competitive Advantage on the Effect of Product Innovation on SMEs Business Performance

Based on the results of the sobel test calculation, the t_{count} is greater than the t_{table} ($2.402 > 1.650$), so there are results that show that competitive advantage can mediate product innovation on business performance, so the hypothesis (H7) is supported. Product innovation is one of the main keys to the success of a product in winning the competition, so that it can be accepted directly by consumers (Chen et al., 2020). The company is required to prepare various innovative ideas for the business it runs so that it is superior to market competitors. The company's success in innovation can be said if the company is one step ahead of its competitors, therefore it requires creativity and ingenuity in innovating so that it is possible to be said to be able to create a competitive advantage in the company's performance (Wang et al., 2019). Competitive advantage is a strategic process that can create opportunities for companies to get higher profits compared to their competitors (4) (Ngo, 2023). New strategies are designed to realize *sustainable competitive advantages*.

The results of this study are in accordance with research Kurniawan & Nuringsih, (2022) and Wang et al. (2019) there is a positive and significant influence between product innovation on *business performance* through the mediation of competitive advantage. Product innovation makes the products offered more unique and different compared to competitors, production process updates can also be carried out in order to reduce production costs or also improve product quality, marketing innovations are also applied in order to expand the market so that they can excel in competition. The application of these innovations encourages SMEs actors to always excel in competition. Therefore, competitive advantage will further increase the influence of innovations applied by SMEs actors to improve business performance. This business performance can be in the form of a more efficient production process, faster revenue growth, and increased profit growth.

5. Conclusion

The complexity of the problems faced by SMEs has been identified in relation to manufacturing, distribution, management, and marketing. At the same time, SMEs face problems related to the development of their products, processes and management. These problems require innovative solutions, which can be motivated by *entrepreneurial orientation* and product innovation. This study proves that there is a moderating role of SMEs competitive advantage on the effect of entrepreneurial orientation and product innovation on performance. This result has closed the gap between the theoretical framework and the practice of SMEs in Magelang district. By empirically confirming the relationship among these three variables, it can be concluded that entrepreneurial orientation and product innovation can improve SMEs business performance by building competitive advantage. The creation of product uniqueness, delivery of greater customer value, lower pricing or by providing more benefits that match the pricing - should be the main concern of every SMEs actor. The researcher recommends that MSMEs adopt new entrepreneurial activities and orientations, spurring product innovation. Likewise, the importance of this study lies in its managerial implications for entrepreneurial strategies in Magelang district SMEs. The research findings should provide critical awareness of the development of SMEs' competitive advantage. The implications of this research have the potential to be developed in several other regions in Indonesia due to the similarity of SMEs characteristics.

Authors' Declaration

Authors' contributions and responsibilities

The authors made substantial contributions to the conception and design of the study. The authors took responsibility for data analysis, interpretation and discussion of results. The authors read and approved the final manuscript.

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The authors declare no competing interest.

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