

Entrepreneurship Orientation and Innovation as Strategies to Improve Financial Performance through Competitive Advantages (Empirical Study of SMEs in the Cultivation Sector in Jember Regency)

Abstract

This study aimed to examine the direct effect of entrepreneurial orientation and innovation on competitive advantage, and of competitive advantage on financial performance. This study also examined the indirect effect of entrepreneurial orientation and innovation on financial performance through competitive advantage. This was a quantitative research using a survey method. The number of respondents was 74 SMEs owners in the field of cultivation industry in Jember regency. The analysis technique used in this research was the Structural Equation Model (SEM) which is operated through the Warp PLS Version 7.0 program.

The results indicated that there was a direct influence of entrepreneurial orientation and innovation on competitive advantage. The results of this study also proved that competitive advantage had a direct effect on financial performance. The results of the indirect effect test showed that innovation also has an indirect effect on financial performance through competitive advantage. However, the results of this study failed to prove that entrepreneurial orientation affects financial performance through competitive advantage.

Keywords: Entrepreneurship orientation, innovation, competitive advantage, financial performance.

Introduction

Small and Medium Enterprises (SMEs) refer to enterprises run by individual or a group of people productively or commercially whose total asset and sales are regulated by law. In East Java, Jember have the largest number of SMEs. In Indonesian economy, this business plays a very important role especially since the economic crisis in Indonesia their role and number have been significantly increased. Therefore, it become the backbone for Indonesian economic development and at the same time provide the main source of income for everyone, especially in terms of employment (Edi, 2018). In addition, SMEs are the main helpers to revive the regional economy, especially since some SMEs have been able to break through the export market (Widyani, 2013).

Mutegi, *et. al.* (2015) explained that the performance of SMEs is the result of company program achieved by a person or group of people with the division of tasks during a certain period with predetermined standards. Some opinions state that the performance of SMEs is often related to the company's ability to deal with problems in its business environment (Birley and Westhead, 1993), personality traits or talents (Naffziger, 1995; Littunen, 2000; Baron and Markman, 2003). However, Small and Medium Enterprises (SMEs) have so far faced various weaknesses, such as weak ability to adapt to strategic environmental changes, lack of skill in responding to business opportunities, lack of creativity in innovation that is dealing with imported products. The same thing is also explained by Sugiarto (2008) that the internal weaknesses of some SMEs are lack of managerial abilities, skills, access to technology and asset.

Based on this background, it can be argued that there is a phenomenon of decreasing performance of SMEs due to competitive advantage impairment. On the other hand, SMEs have become the backbone of the economy by contributing to the gross domestic product. In addition, the rapidly increasing number of SMEs has become the main source of income for the community as well as a source of employment in Jember Regency. Therefore, it is important to examine and analyze the determinants of competitive advantage to improve the financial performance of SMEs.

Entrepreneurship orientation

Lumpkin and Dess (1996) explained Entrepreneurial orientation are a process, practice and decision-making activities that lead to new entry. Ahimbisibwe and Abaho (2013) stated that companies that have a strong entrepreneurial orientation will be more willing to take risks, and not only stick to past strategies. Entrepreneurial orientation is a company orientation that has a principle of identifying and exploiting opportunities (Lee and Chu, 2011). Patel and D'Souza (2009) defined entrepreneurial orientation as an orientation to be the first in terms of innovation in the market, have an attitude to take risks, and be proactive to changes that occur in the market. Hafeez et al (2012) stated that companies that have a strong entrepreneurial orientation will have the ability to be more strongly innovative.

Innovation

Atalay et al. (2013) stated that product innovation is an introduction and development of goods or services that are different from the previous ones and complement the deficiencies of the previous invention by emphasizing more on quality aspects. According to Prokosa (2005) innovation is a company mechanism to adapt to a dynamic environment.

Competitive advantage

Competitive advantage grows fundamentally from the value that allows the company to create value for its buyers beyond the costs incurred by the company to create it (Porter, 1985: 3). According to David (2011: 9), competitive advantage is anything a company can do so that it is better than rival companies. Meanwhile, according to Dessler (2001: 81) are all the factors that an organization may have to differentiate products or services from competitors' products and services to increase the market percentage. However, it is further said that the most important thing is to maintain the sustainability of this competitive advantage (Barney and Clark, 2007). Adner and Zemsky (2006), a competitive advantage perspective that considers a demand-based perspective.

Financial Performance

The concept of financial performance according to Gitosudarmo and Basri (2002: 275) is a series of financial activities in a certain period which are reported in the financial statements including the income statement and balance sheet. According to Fahmi (2011: 2) financial performance is an analysis carried out to see the extent to which a company has implemented proper and correct financial implementation rules.

The Influence of Entrepreneurship Orientation on Competitive Advantage

Companies that have a good entrepreneurial orientation will be able to reach targets and market positions better than their competitors. The reason is, because the company is continuously observing market changes and at the same time it will respond quickly to the changes that occur. The company's ability to be proactive and dare to take risks gives the company the ability to create more innovative products. As a result, companies can outperform their competitors so that they have a competitive advantage because they will be able to satisfy customers and identify the factors that affect customers. This is in accordance with a research conducted by Koh (1997), Ismawanti (2008), Supranoto (2009) and Djojobo and Tawas (2014) which found that companies with a proper entrepreneurial orientation can reach the target market and be in a forward market position compared to their competitors.

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H1: Entrepreneurial orientation has a positive effect on competitive advantage.

The Influence of Innovation on Competitive Advantage

Atalay et al. (2013) stated that product innovation is the introduction and development of new types of goods or services that are different from the previous ones and complement the deficiencies of the previous invention. Companies that have high innovation power will have a competitive advantage. As explained by Wahyono (2002) that continuous innovation in a company is a basic need which in turn will lead to the creation of a competitive advantage.

Song and Parry (1997) explained that the competitive advantage of a product is one of the decisive factors for the success of a new product. Cooper

(2000) stated that the advantages of new products are very important in a highly competitive global market circle. These advantages cannot be separated from the development of the resulting innovative products so that they will have market advantages. Furthermore, Chen et al. (2009) which allows firms to better maintain their advantage. In addition, Kuczarski (2003) also stated that to achieve competitive advantage, innovation must always focus on creating something new in the world.

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H2: Innovation has a positive effect on competitive advantage.

The Influence of Entrepreneurship Orientation on Financial Performance

Entrepreneurial orientation is a company orientation that has a principle of identifying and exploiting opportunities (Lumpkin and Dess, 1996). Miller (1983) defines entrepreneurial orientation as an orientation to be first in terms of innovation in the market, to have an attitude to take risks, and to be proactive to changes that occur in the market. Companies that have a good entrepreneurial orientation will have better financial performance because companies that have a strong entrepreneurial orientation will be more willing to take risks, and not only stick to past strategies (Lumpkin and Dess 1996). In a dynamic environment, entrepreneurial orientation is very important for the survival of the company. Entrepreneurial orientation which consists of the dimensions of innovation, proactive, risk taking, competitive aggressiveness and autonomy has an effect on SMEs business performance (Arshad et al., 2014).

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H3: Entrepreneurial orientation has a positive effect on financial performance

The Influence of Innovation on Financial Performance

Freeman (2004) assumed innovation as an effort by the company through the use of technology and information to develop, produce and market new products for the industry. In other words, innovation is the modification or discovery of ideas for continuous improvement and development to meet

customer needs. Thus, companies that have high innovation will be able to meet customer needs so they will be able to improve their financial performance. Where performance is the desired result of the action (Gibson, et.al., 1995).

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H3: Innovation has a positive effect on financial performance

The Competitive advantage on Financial Performance

Competitive advantage is a company's ability to accomplish a much higher and superior performance compared to competitors in similar industries through outstandingly managed characteristics and resources. Day and Wensley (1988) stated that competitive advantage is a form of strategy to help companies maintain their survival. Ferdinand (2003) stated that in a competitive market, the company's ability to achieve an outstanding performance is highly dependent on the degree of competitive advantage. Companies that have a competitive advantage will have better financial performance because they have a much higher and superior performance than their competitors. Research conducted by Rose, et.al (2010) and Lee and Chu (2011) showed that competitive advantage has a positive influence on company performance.

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H3: Competitive advantage has a positive effect on financial performance

The Influence of Entrepreneurship Orientation on Financial Performance through Competitive Advantage

Entrepreneurial orientation is an orientation that has a principle of identifying and exploiting opportunities (Lumpkin and Dess, 1996). Furthermore, Miller (1983) defined entrepreneurial orientation as an orientation to be the first in terms of innovation in the market, to have an attitude to take risks, and to be proactive to changes that occur in the market. Companies that have good entrepreneurial orientation will have better financial performance if their competitive advantages are also good. This is because companies that have a strong entrepreneurial orientation will be more willing to take risks, and not only

stick to past strategies (Lumpkin and Dess 1996). In a dynamic environment, entrepreneurial orientation is very important for the survival of the company. Entrepreneurial orientation which consists of the dimensions of innovation, proactive, risk taking, competitive aggressiveness and autonomy has an effect on SMEs business performance (Arshad et al., 2014).

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H3: Entrepreneurship orientation has a positive effect on financial performance through competitive advantage

Innovation affects financial performance through competitive advantage

Innovation is a company effort in the form of using technology and information to develop, produce and market new products for industry (Freeman 2004). In other words, innovation is the modification or discovery of ideas for continuous improvement and development to meet customer needs. Thus, companies that have high innovation will be able to meet customer needs so that they will improve financial performance, performance is the desired result of behavior (Gibson, et.al., 1995). The increase in financial performance will be even higher if followed by a highly competitive advantage because competitive advantage is the company's ability to have a much higher and superior performance compared to competitors.

Based on the results of the literature review and empirical evidence mentioned above, the proposed hypothesis is as follows:

H3: Entrepreneurship orientation has a positive effect on financial performance through competitive advantage

Research Method

The population in this study were SMEs in the cultivation industry in Jember district. The sampling technique used purposive sampling method, which is a method in which the sampling technique is based on certain considerations. The sample was selected based on the essential and relevant characteristics of the study (Soeratno and Arsyad, 1999). The criteria in this study are described as

follows: 1). Respondents are owners or managers of business units; 2) Respondents have owned or managed a business unit for at least 3 years; and 3) Respondents have a workforce of more than 10 people.

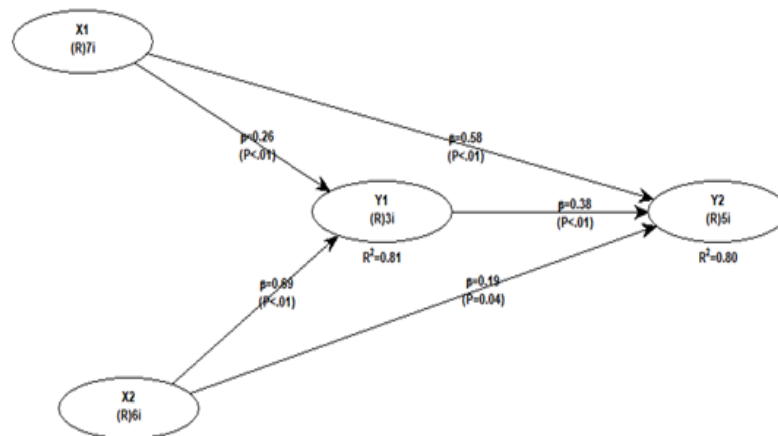
There are some variables used in this study, they are entrepreneurial orientation, innovation, competitive advantage, and performance. The analysis technique used in this research is the Structural Equation Model (SEM) which is operated through the version 7.0 warp program. Research modeling through SEM enables a researcher to answer both regressive and dimensional research questions, namely measuring what the dimensions of a concept are (Ferdinand, 2006).

Result and Discussion

This study used 73 respondents from SMEs in the cultivation industry sector in Jember district. The selected SMEs are businesses that have been in business for at least 3 years, this is an indicator that they are committed to running the business. The descriptive statistics of respondents showed that the majority of SMEs are owned by male entrepreneurs, it is 68%. The description of the types of MSMEs business that became the research sample consisted of food, beverage, ready-made clothing, leather goods and footwear, wood and cork goods including woven bamboo, rattan and the like, paper goods, furniture, and rubber goods. and plastic.

Data from respondents then tested its model through hypothesis testing using path analysis. The results of path analysis are presented in the following figure:

Figure 1. Path analysis result



Based on Figure 1, it can be explained that entrepreneurial orientation and innovation have a direct effect on competitive advantage. Competitive advantage has a direct effect on financial performance. Entrepreneurial orientation and innovation have an indirect effect on financial performance. Other results indicate that entrepreneurial orientation does not have an indirect effect on financial performance through competitive advantage. However, innovation is able to provide evidence that affects financial performance through competitive advantage.

Outer Model Evaluation

Evaluation of the outer model is carried out by three criteria, namely convergent validity, discriminant validity, and composite reliability. Machfud and Dwi (2013: 66) explained that the loading between 0,40-0,70 should still be well-thought-out.

Table 1. Output Combined Loading and Cross-loading

Entrepreneurship Orientation (X1)	Innovation (X2)		Competitive Advantage (Y1)		Financial Performance (Y2)		p-value	Fulfilled/ or did not fulfill the convergent validity	
	Indicator	Ind	Ind	Y1	Ind	(Y2)			
X1.1	0.956	X2.1	0.959	Y1.1	0.989	Y2.1	0.936	<0.001	Fulfilled
X1.2	0.959	X2.2	0.947	Y1.2	0.981	Y2.2	0.946	<0.001	Fulfilled
X1.3	0.951	X2.3	0.959	Y1.3	0.992	Y2.3	0.966	<0.001	Fulfilled
X1.4	0.947	X2.4	0.979			Y2.4	0.963	<0.001	Fulfilled
X1.5	0.934	X2.5	0.973			Y2.5	0.965	<0.001	Fulfilled
X1.6	0.924	X2.6	0.978						Fulfilled

Source: authors' calculation

1). Discriminant Validity

Discriminant validity gained from cross loading value measurement and construct value. If the construct correlation of each indicator is higher than the other construct value, then the discriminant validity is fulfilled.

Table 2. loading value of laten construct and other constructs

Indicator	Loading	>	Loading value to other constructs				Notes
			X1	X2	Y1	Y2	
X1.1	0.956	>		-0.206	0.180	-0.056	Fulfilled the Discriminant Validity
X1.2	0.959	>		0.034	-0.118	0.039	Fulfilled the Discriminant Validity
X1.3	0.951	>		-0.001	0.334	0.045	Fulfilled the Discriminant Validity
X1.4	0.947	>		-0.004	-0.107	-0.051	Fulfilled the Discriminant Validity
X1.5	0.934	>		0.125	-0.007	0.045	Fulfilled the Discriminant Validity
X1.6	0.924	>		0.103	-0.011	-0.078	Fulfilled the Discriminant Validity
X1.7	0.920	>		-0.009	-0.195	0.070	Fulfilled the Discriminant Validity
X2.1	0.959	>	0.137		-0.128	0.033	Fulfilled the Discriminant Validity
X2.2	0.947	>	-0.136		0.135	0.037	Fulfilled the Discriminant Validity
X2.3	0.959	>	0.066		-0.088	-0.043	Fulfilled the Discriminant Validity
X2.4	0.979	>	0.024		0.120	-0.001	Fulfilled the Discriminant Validity
X2.5	0.973	>	-0.102		-0.030	0.004	Fulfilled the Discriminant Validity
X2.6	0.978	>	-0.078		0.017	-0.022	Fulfilled the Discriminant Validity
Y1.1	0.996	>	0.079	0.024		-0.024	Fulfilled the Discriminant Validity
Y1.2	0.999	>	-0.031	-0.010		0.005	Fulfilled the Discriminant Validity
Y1.3	0.999	>	-0.042	-0.012		0.017	Fulfilled the Discriminant Validity
Y2.1	0.983	>	0.206	-0.011	-0.246		Fulfilled the Discriminant Validity
Y2.2	0.947	>	0.263	-0.150	-0.240		Fulfilled the Discriminant Validity
Y2.3	0.985	>	-0.018	-0.029	0.170		Fulfilled the Discriminant Validity
Y2.4	0.968	>	-0.104	-0.103	0.206		Fulfilled the Discriminant Validity
Y2.5	0.997	>	-0.081	-0.002	-0.001		Fulfilled the Discriminant Validity

Source: authors' calculation

Based on the table above, all indicators' variable were fulfilled the discriminant validity, which means the loading value of each variable is higher than the other construct variable.

2) Composite Reliability

A construct is said to be reliable if the composite reliability value is > 0.70 . Here are the results of the latent variable output.

Table 3. Composite reliability and Cronbach's Alpha values

	X1	X2	Y1	Y2	Criteria	Notes
Composite reliability	0.982	0.988	0.991	0.981	$>0,70$	Reliable
Cronbach's Alpha	0.979	0.986	0.987	0.976	$\geq 0,5$ good and $\geq 0,3$ adequate	Reliable

3). Evaluation of the Structural Model (Inner Model)

The evaluation of the structural model (inner model) is intended to test the suitability of the model. There are 3 test indices used, namely the average path coefficient (APC), average R-squared (ARS) and average variance factor (AVIF). The criteria used are that APC and ARS are accepted with the condition that the p-value is <0.05 and the AVIF is smaller than 5 (Sholihin and Ratmono, 2013: 61).

The results of output model fit indices are presented in the following table:

Table 4. Output Model Fit Indices Results

P-value index Criteria Description

	Index	p-value	Criteria	Notes
Average path coefficient (APC)	0,341	$P<0.001$	$p < 0,05$	Accepted
Average R-squared (ARS)	0,415	$P<0.001$	$p < 0,05$	Accepted
Average block VIF (AVIF)	3.197		acceptable if ≤ 5	Accepted

The table above indicates that the APC is 0.341 with a p-value <0.001 . Meanwhile, ARS value is 0.415 with p - value <0.001 . The APC meets the criteria because it has a value of $p <0.001$. Likewise, the p value of ARS is $p <0.001$. The AVIF value must be <5 because based on these data the AVIF value is 3,197. Thus, the inner model can be accepted.

Hypothesis Testing

Direct Effect Test

Table 5. Direct Effects

Criteria	Variable	Y1	Y2
Path coefficient	X1	0.259	0.581
	X2	0.692	0.190

	Y1		0.385
	Y2		
p-values	X1	0.009	<0.001
	X2	<0.001	0.045
	Y1		<0.001
	Y2		

Based on the data above, it can be concluded that entrepreneurial orientation (X1) has a direct effect on competitive advantage (Y1) of 0.259 with a significance value of $p < 0.05$. Innovation (X2) has a direct effect on competitive advantage (Y1) of 0.692 with a significance value of $p < 0.001$. Entrepreneurial orientation (X1) has a direct effect on financial performance (Y2) of 0.581 with a significance value of $p < 0.001$. Innovation (X2) has a direct effect on performance (X2) of 0.190 with a significance value of $p < 0.05$. Competitive advantage has a direct effect (Y1) on financial performance (Y2) of 0.385 with a significance value of $p < 0.001$.

Indirect Effect Test

Table 6. Indirect Effect for paths with 2 segments and p value

	X1	X2
X1		
X2		
Y1		
Y2	0.109 ($p > 0.05$)	0.266 ($p < 0.001$)

The table indicates that the indirect effect of entrepreneurial orientation variables on financial performance through competitive advantage is 0.109 with $P > 0.05$ (not significant). Meanwhile, the indirect effect of innovation on financial performance through competitive advantage is 0.266 with $p < 0.001$ (significant).

Discussion

Based on hypothesis testing, it is known that orientation has an effect on the competitive advantage of MSMEs in Jember Regency. That is, the ability of MSMEs managers to be proactive and dare to take risks enable MSMEs to create innovative products ahead of competitors. The ability to innovate for MSMEs in the processing industry requires new and unique business activities. The ability to innovate is important in the essence of entrepreneurial characteristics. MSMEs managers are also willing to take risks in making uncertain decisions but provide opportunities for better results. The proactive nature of MSME managers is intended to gain a wider market. This is in line with the results of research which states that entrepreneurial orientation has a significant effect on the competitive advantage of MSMEs (Usvita, 2015). Furthermore, these results are also in line with research which states that the better the

entrepreneurial orientation a business has, the better the achievement of competitive advantage from the business will be (Tahir, Pasda, and Widhi, 2018).

Based on hypothesis testing, it is known that innovation has an effect on the competitive advantage of SMEs in Jember district. This shows that the main factor affecting competitive advantage is product innovation. Hills (2008) defines innovation as an idea, practice or object that is considered new by an individual. Product innovation will create various product designs, thereby increasing alternative choices, increasing the benefits or value received by customers, which in turn will improve product quality as expected by customers (Prajogo and Sohal, 2003). MSMEs managers in the processing industry sector in Jember Regency think that efforts to introduce innovation can lead and reduce the possibility of competitors to innovate earlier (Djojobo and Tawas, 2014). The results of this study are in line with research conducted by (Sherlin, 2016: Tahir, Pasda, and Widhi, 2018). Improved financial performance is built by entrepreneurial orientation with indicators of innovation, courage to take risks and to act proactively. Therefore, SMEs managers in the processing industry in Jember Regency have the courage to take risks by trying new things or strategies that have the opportunity to improve financial performance. As a result, financial performance can be directed to transform it in facing long-term challenges. These findings are in line with the opinion of Poudel et al. (2012) which states that entrepreneurial orientation is an organization's strategic resource with the potential to generate competitive advantage. The potential for entrepreneurial orientation and its impact on business performance. The results of this study are also in line with the results of previous studies, for example research by Wiklund (1999) and Wiklund and Shepherd (2005).

These findings indicate that MSMEs managers in facing increasingly fierce competition need to continuously innovate. Innovation can be in the form of new product development or new product introductions. The innovation strategy, which includes the process of innovation, product innovation, and organizational innovation can boost performance because the implementation of innovation is an important aspect that can add value to company competitiveness (Robertson, 2002). Thus, the application of these four important aspects in business will improve their financial performance. These findings are in line with some of Lena Ellitan's (2006) study.

The results of this study indicated that a competitive company can create higher economic value than other companies in its industry. SMEs that have the ability to compete or have a market position can improve their financial performance. The same thing is explained by David (2011: 9) who states that competitive advantage is an action taken by a company so that it

is better than rival companies. The results of this study support the research results of Widyaningdyah and Aryani (2013).

Entrepreneurial orientation has no effect on financial performance through competitive advantage. The results of this study indicate that the entrepreneurial orientation of the creative industry sector has not been maximally innovative that can produce a competitive advantage. Business actors have not dared to take full advantage of existing business potentials or opportunities, such as entering new markets or producing new products. As a result, SMEs have not been able to create higher economic value than other companies in their industry. The results of this study do not support the results of research conducted by Wiklund and Shepherd (2005), Wiklund (1999), and Frank et al. (2010) who have succeeded in proving empirically the positive effect of entrepreneurial orientation on business performance.

SMEs in the processing industry in Jember Regency continue to innovate in the use of technology and information to develop, produce and market new products for industry (Freeman 2004). In other words, innovation is in the form of modification or idea discovery to meet customer needs so as to increase competitive advantage and have an impact on financial performance. MSMEs processing industry considers that the increase in financial performance will be even higher if it is followed by a highly competitive advantage because it will enable them to have a much higher and superior performance compared to competitors.

Conclusion

The entrepreneurial orientation and innovation have a direct effect on competitive advantage and financial performance. The results of this study indicate that the ability of SMEs managers to be proactive and dare to take risks enable them to create innovative products. Product innovation for the processing industry is important to increase alternative product choices and to increase added value for customers. A company is said to have a competitive advantage if it can create higher economic value than other companies. Therefore, an increase in financial performance will be greatly influenced by customer response to a company's products.

The results of this study also prove that innovation has indirect effect on financial performance through competitive advantage. However, this study failed to prove that entrepreneurial orientation had indirect effect on financial performance through competitive advantage.

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