

The Influence Of Entrepreneurial Orientation On Firm Performance: An Analysis Of The Mediating Role Of Knowledge Management And Dynamic Capabilities In Smes In Malang Raya

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Abstract

This study examines the impact of entrepreneurial orientation on firm performance by analyzing the mediating roles of knowledge management and dynamic capabilities in Micro and Small Enterprises (MSEs) in Malang Raya, Indonesia. MSEs contribute significantly to the Indonesian economy, yet many face challenges in sustaining their businesses, such as low innovation, limited access to capital, and difficulty adapting to market changes. This research aims to identify the extent to which entrepreneurial orientation—including innovation, proactiveness, and risk-taking—enhances MSE performance through the implementation of knowledge management and dynamic capabilities.

Data were collected from 125 MSE owners in Malang Raya through surveys and analyzed using the Structural Equation Modeling Partial Least Squares (SEM-PLS) approach. The findings reveal that entrepreneurial orientation has a direct positive effect on MSE performance. Furthermore, knowledge management and dynamic capabilities are proven to serve as significant partial mediators in this relationship. These findings underscore the importance of knowledge-based strategies and adaptive capabilities in improving operational efficiency and fostering innovation in a dynamic business environment.

The implications of this study include practical recommendations for MSEs to strengthen their entrepreneurial orientation, optimize knowledge management, and develop dynamic capabilities. It also suggests that government support in the form of expanded access to training and technology resources is essential for enhancing MSE competitiveness in local and global markets. With this approach, MSEs in Malang Raya are expected to make greater contributions to national economic growth and improve their competitiveness sustainably.

Keywords: *Entrepreneurial Orientation; Business Performance; Knowledge Management; Dynamic Capabilities; Micro and Small Enterprises (MSEs); Malang Raya; SEM PLS; Innovation; Proactiveness; Risk-Taking Courage; Indonesian Economy.*

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I. Introduction

Measuring company performance is essential to enhance operational efficiency and effectiveness while identifying weaknesses that need improvement (Mahmudova, 2018). High performance reflects the success of business strategies, operational efficiency, and the ability to meet customer needs, which ultimately leads to increased profitability, market share, and company reputation (Taouab & Issor, 2019). However, many companies, including MSMEs, face performance challenges that lead to their inability to survive. Approximately 50%-60% of MSMEs fail within the first three years of operation, negatively impacting national economic stability (Republika, 2019).

MSMEs account for 99.99% of all businesses in Indonesia, employing 96.92% of the workforce and contributing 60.51% to the GDP, making them the primary drivers of the domestic economy (Widia & Junika Putra, 2021). Despite this, their contribution to exports and productivity remains low compared to larger enterprises (Ilham Maulana, n.d.; umkmindonesia, 2018). Key challenges include business informality, low human resource capacity, lack of innovation, and limited access to capital and technology (Kristinawati & Tjakraatmadja, 2018).

To support MSME performance, the government has implemented programs such as PEN, BPUM, KUR, and OSS. However, only a small proportion of MSMEs have been able to utilize these programs effectively (CNN Indonesia, 2021; Kompas, 2022). In this context, entrepreneurial orientation, knowledge management, and dynamic capabilities are crucial factors that can enhance the competitiveness and sustainability of MSMEs in the global market (Hendrawan & Wijaya, 2020; Kristinawati & Tjakraatmadja,

2018). In-depth research is needed to understand the role of these three factors in improving MSME performance, particularly in Malang Raya, which serves as a hub for MSME growth in East Java.

II. Literature Review

Company Performance Measurement

Company performance is defined as the result of business activities reflecting the efficiency and effectiveness of implemented strategies (Kotane & Kuzmina-Merlino, 2017). Performance measurement is utilized to evaluate goal achievement, encompassing financial aspects such as profitability and ROI, as well as non-financial aspects like customer satisfaction and product quality (Dewata et al., 2018). Good performance signifies successful business strategies and strengthens a company's position in the market (Mahmudova, 2018; Taouab & Issor, 2019).

However, MSMEs in Indonesia still face numerous challenges that hinder performance improvement. Most MSMEs operate informally, have limited access to capital, and struggle to adapt to technology (Republika, 2019; umkmindonesia, 2018). Consequently, their contribution to international trade is only 15.65%, significantly lower than large enterprises, which account for 84.35% (Ilham Maulana, n.d.).

Entrepreneurial Orientation

Entrepreneurial orientation comprises dimensions of innovation, proactivity, and risk-taking, which significantly impact company performance (Hendrawan & Wijaya, 2020). Innovation enables companies to create new products that enhance competitiveness, while proactivity helps them respond swiftly to market opportunities (Putri, 2017). Risk-taking is crucial for navigating uncertainties and pursuing business opportunities (Lumpkin & Dess, 2001).

However, an excessive focus on innovation without considering other factors can increase the risk of failure (Kristinawati & Tjakraatmadja, 2018). Therefore, entrepreneurs need sufficient experience and knowledge to maximize the benefits of entrepreneurial orientation.

Knowledge Management

Knowledge management encompasses the processes of acquiring, storing, and applying relevant information to support decision-making (Alavi & Leidner, 2001). Knowledge is considered an intangible asset that can enhance operational efficiency, innovation, and competitiveness (Kristinawati & Tjakraatmadja, 2018).

Effective knowledge management assists companies in understanding market changes, identifying new opportunities, and developing innovative solutions (Siti-Zubaidah, 2016). However, implementing effective knowledge management remains a challenge for MSMEs, particularly in financial management and technology utilization (Adyuta & Prabandari, 2022).

Dynamic Capabilities

Dynamic capabilities refer to a company's ability to adapt to environmental changes, integrate resources, and renew competencies (Teece, 2007). This concept includes three main dimensions: sensing (opportunity identification), seizing (opportunity exploitation), and transforming (resource reconfiguration) (Buttar & Kocak, 2011).

Dynamic capabilities enable companies to remain competitive in dynamic markets through continuous innovation (Makadok, 2010). For MSMEs, developing these capabilities is essential to overcome challenges such as low innovation levels and technological adaptation (Kristinawati & Tjakraatmadja, 2018).

MSMEs' Contribution to the Economy

MSMEs are the backbone of Indonesia's economy, contributing 60.51% to GDP and absorbing nearly 97% of the workforce (Widia & Junika Putra, 2021). However, their contribution to exports and productivity remains low due to limitations in innovation, capital, and technology (Ilham Maulana, n.d.; umkmindonesia, 2018).

The government has launched various programs, such as BPUM, KUR, and OSS, to support MSMEs, yet their utilization is still limited. Only 26.5% of MSMEs have gone digital, necessitating further efforts to improve the accessibility of these programs (CNN Indonesia, 2021; Kompas, 2022).

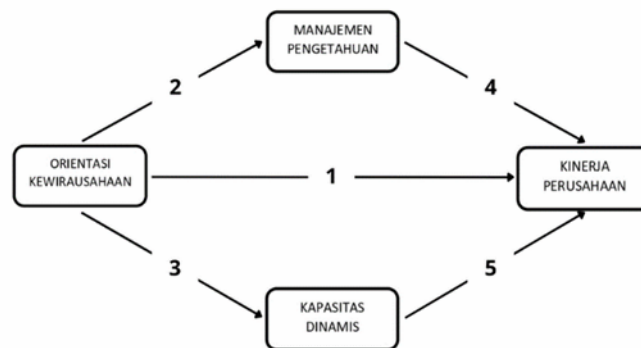


Figure 1. Conceptual Framework and Hypotheses

The literature above indicates that entrepreneurial orientation, knowledge management, and dynamic capabilities are critical factors in improving MSMEs' performance. However, many MSMEs in Malang Raya, in particular, still face challenges in implementing these strategies. Further research is needed to understand how these factors interact and impact MSMEs' performance, specifically in the Malang Raya region.

III. Research Methodology

Research Approach

This study employs a quantitative approach with a survey method to collect primary data from Micro and Small Enterprises (MSEs) in the Malang Raya region. The data obtained is analyzed using the Structural Equation Modeling-Partial Least Square (SEM-PLS) technique, which allows for simultaneous testing of relationships between independent, mediating, and dependent variables. SEM-PLS is selected for its effectiveness in handling complex research models, even with relatively small sample sizes.

Population and Sample

The research population includes all MSEs in Malang Raya. Based on data from Diskop UKM Jatim (2019), there are 762,857 business units in this region. The sample is selected using purposive sampling, with the criteria that respondents must be actively involved in managing their businesses.

The sample size is determined using the rule of thumb, which recommends 5–10 times the number of indicators used in the research model. With 22 indicators, the minimum required sample size is 110 respondents. To ensure validity and reliability, this study involves 125 respondents.

Research Variables and Measurement

The study involves three main groups of variables:

- a. **Independent Variables:** Entrepreneurial orientation (covering innovation, proactiveness, and risk-taking dimensions).
- b. **Mediating Variables:** Knowledge management (including knowledge acquisition, sharing, and application) and dynamic capabilities (comprising sensing, seizing, and transforming).
- c. **Dependent Variable:** Firm performance, encompassing financial performance (profitability, ROI) and non-financial performance (customer satisfaction, product quality).

Each variable is measured using a 5-point Likert scale, where 1 indicates strong disagreement and 5 indicates strong agreement.

Research Instrument

The research instrument is a questionnaire designed based on validated indicators from previous studies. Construct validity is tested using Confirmatory Factor Analysis (CFA), while reliability is measured using Cronbach's Alpha and Composite Reliability.

Data Analysis Techniques

Data analysis is conducted through the following stages:

- a. **Descriptive Statistics:** To describe respondent characteristics and data distribution.
- b. **Validity and Reliability Testing:** Using SEM-PLS to ensure the indicators are valid and reliable.
- c. **Hypothesis Testing:** Using SEM-PLS to examine direct and mediated relationships among independent, mediating, and dependent variables.

Research Procedure

- a. Data Collection: Data is collected through online questionnaires distributed to selected respondents.
- b. Data Processing: Collected data is checked for outliers and missing values.
- c. Data Analysis: Data is processed using statistical software for SEM-PLS, focusing on structural and measurement model testing.

Hypothesis Design

This study tests five main hypotheses:

- H1: Entrepreneurial orientation positively impacts firm performance.
- H2: Entrepreneurial orientation positively impacts knowledge management.
- H3: Knowledge management positively impacts firm performance.
- H4: Entrepreneurial orientation positively impacts firm performance through knowledge management.
- H5: Entrepreneurial orientation positively impacts firm performance through dynamic capabilities.

This methodology is expected to provide valid and relevant results for understanding the role of entrepreneurial orientation, knowledge management, and dynamic capabilities in improving the performance of MSEs in Malang Raya.

IV. Results And Discussion

The validity of research items was assessed through Convergent Validity and Discriminant Validity tests to evaluate the loading factor values. Indicators with loading factor values below 0.6 were considered invalid and excluded from the research model. An indicator is deemed valid if its outer loading value exceeds 0.6.

Figure 2. Convergent Validity Results

	Kapasitas Dinamis	Kinerja Perusahaan	Manajemen Pengetahuan	Orientasi Kewirausahaan
KD1	0,828			
KD2	0,770			
KD3	0,853			
KD4	0,837			
KD5	0,852			
KD6	0,882			
KP1		0,867		
KP2		0,887		
KP3		0,842		
KP4		0,890		
MP1			0,762	
MP2			0,756	
MP3			0,790	
MP4			0,776	
MP5			0,730	
MP6			0,710	
OK1				0,814
OK2				0,731
OK3				0,745
OK4				0,793
OK5				0,766
OK6				0,808

Source: Data Processed, 2024

The research findings indicate that all variable indicators are valid, with high loading factor values. Dynamic Capabilities demonstrate values ranging from 0.770 to 0.882, signifying excellent measurement consistency. Firm Performance also exhibits strong validity with loading factor values ranging from 0.842 to 0.890. Although Knowledge Management shows slightly lower loading factor values, between 0.710 and 0.790,

its indicators still meet validity criteria. Meanwhile, Entrepreneurial Orientation has values between 0.731 and 0.814, indicating sufficient contributions from each indicator. Overall, these results confirm the validity and consistency of the indicators in measuring the research variables.

Figure 3. Heterotrait–Monotrait Ratio (HTMT)

	Kapasitas Dinamis	Kinerja Perusahaan	Manajemen Pengetahuan	Orientasi Kewirausahaan
Kapasitas Dinamis				
Kinerja Perusahaan	0,717			
Manajemen Pengetahuan	0,544	0,834		
Orientasi Kewirausahaan	0,606	0,809	0,686	

Source: Data Processed, 2024

The statement above explains that discriminant validity in this study has been well achieved. The Heterotrait-Monotrait Ratio (HTMT) for each variable is below 0.9, indicating that each variable construct is clearly distinct from one another, in accordance with good discriminant validity criteria (Sarstedt et al., 2016). Furthermore, discriminant validity was also assessed using the Average Variance Extracted (AVE), where the AVE value for each construct is greater than 0.5. This demonstrates that the indicators within each construct sufficiently explain a significant amount of variance, meeting the accepted standards for discriminant validity.

Figure 4. Average Variance Extracted (AVE)

	Average Variance Extracted (AVE)
Kapasitas Dinamis	0,702
Kinerja Perusahaan	0,760
Manajemen Pengetahuan	0,569
Orientasi Kewirausahaan	0,604

Source: Data Processed, 2024

It can be concluded that the Average Variance Extracted (AVE) values for each construct in this study demonstrate good convergent validity. The Dynamic Capacity construct has an AVE value of 0.702, Company Performance has 0.760, Knowledge Management has 0.569, and Entrepreneurial Orientation has 0.604, all exceeding the recommended minimum threshold of 0.5. These AVE values indicate that the indicators within each construct effectively explain the variance of their respective constructs, signifying strong convergent validity and reliable research analysis results.

Figure 5. Composite Reliability

	Composite Reliability
Kapasitas Dinamis	0,934
Kinerja Perusahaan	0,927
Manajemen Pengetahuan	0,888
Orientasi Kewirausahaan	0,901

Source: Data Processed, 2024

The research findings indicate that the Composite Reliability values for each construct are excellent, with Dynamic Capacity reaching 0.934, Company Performance 0.927, Knowledge Management 0.888, and Entrepreneurial Orientation 0.901. All these values exceed the minimum threshold of 0.7, indicating very high internal consistency and strong reliability of the indicators used to measure each construct. Therefore, the research instrument can be relied upon to measure the existing variables.

V. Hypothesis Test

The Effect of Entrepreneurial Orientation on Firm Performance

This study shows that entrepreneurial orientation has a significant impact on firm performance, with a T Statistics of 4.241 and a P Value of 0.000, indicating that firms with a high entrepreneurial orientation tend to have better performance. Entrepreneurial orientation includes innovation, risk-taking, and proactivity, which enable firms to adapt to market changes, identify new opportunities, and utilize resources more effectively. Furthermore, entrepreneurial orientation also contributes to the development of the firm's dynamic capabilities

(T Statistics 3.440, P Value 0.001), enhancing the firm's ability to innovate and adapt. Knowledge management, which is influenced by entrepreneurial orientation (T Statistics 6.499, P Value 0.000), also plays a crucial role in improving decision-making effectiveness and creating additional value for the firm. Overall, the findings of this study emphasize that entrepreneurial orientation is a key driver of firm performance, dynamic capabilities, and knowledge management, which support innovation and sustainable growth, as well as enhancing the firm's competitiveness in the market. This research strengthens the findings of Zhang & Zhang, 2012; Ibarra-Cisneros & Hernandez-Perlines, 2019; Shah & Ahmad, 2019; Lechner & Gudmundsson, 2014, which show that entrepreneurial orientation has a positive and significant impact on firm performance.

The Influence of Entrepreneurial Orientation on Knowledge Management

This study shows that entrepreneurial orientation has a significant impact on knowledge management, with a T Statistic of 6.499 and a P Value of 0.000, indicating that companies with a high entrepreneurial orientation tend to have more effective knowledge management. Entrepreneurial orientation encourages innovation, creativity, and a willingness to take risks, all of which are crucial in managing knowledge. It also fosters an environment that supports collaboration and the exchange of ideas among employees. This helps companies develop systems for collecting, storing, and distributing knowledge, as well as leveraging external knowledge, such as market trends and industry best practices. Effective knowledge management allows companies to optimize resources, make better strategic decisions, and enhance their competitive advantage. Overall, this study emphasizes the importance of integrating entrepreneurial principles into knowledge management strategies to create an environment that is more adaptive, innovative, and supportive of long-term business growth. This research reinforces the findings from Adam et al., 2022; Engelen et al., 2015; Latif et al., 2020; Iqbal & Malik, 2019, which show that entrepreneurial orientation has a positive and significant effect on knowledge management.

The Influence of Entrepreneurial Orientation on Dynamic Capabilities

This study shows that entrepreneurial orientation has a significant impact on a company's dynamic capabilities, with a T Statistic of 3.440 and a P Value of 0.001, indicating that companies with a high entrepreneurial orientation tend to have better dynamic capabilities. Dynamic capabilities include a company's ability to integrate, build, and reconfigure resources to adapt to market changes and face new challenges. Entrepreneurial orientation encourages companies to innovate, take risks, and adapt quickly through continuous learning. Thus, entrepreneurial orientation not only enhances innovation but also strengthens a company's ability to manage change and capitalize on opportunities. Therefore, companies are advised to prioritize entrepreneurial orientation in their business strategies to improve dynamic capabilities, ensure sustainability, and achieve competitive advantage in an increasingly competitive market. This research reinforces the findings from Buttar & Kocak, 2011; Liu & Xi, 2022; Kurnia Fitriati et al., 2020; Correia et al., 2022; Abu-Rumman et al., 2021, that entrepreneurial orientation has a positive and significant effect on dynamic capabilities.

The Influence of Knowledge Management on Company Performance

This study shows that knowledge management has a significant impact on company performance, with a T Statistic of 4.264 and a P Value of 0.000, indicating that effective knowledge management can substantially improve performance. Knowledge management involves the collection, storage, and distribution of relevant knowledge, enabling companies to make better decisions, develop innovative products, and improve operational efficiency. Good knowledge management practices also enhance the company's responsiveness to market changes, support organizational learning, and foster a collaborative culture that encourages innovation. Therefore, companies that invest in effective knowledge management will be able to increase productivity, innovation, and competitiveness, as well as achieve optimal performance and sustainability in the market. This research supports findings from Gharakhani & Mousakhani (2012), Rauch et al. (2009), Ha et al. (2021), and Bakar et al. (2015) that knowledge management has a positive and significant impact on company performance.

The Influence of Dynamic Capabilities on Company Performance

This study shows that dynamic capabilities have a significant impact on company performance, with a T Statistic of 4.212 and a P Value of 0.000, indicating that companies with strong dynamic capabilities tend to perform better. Dynamic capabilities refer to a company's ability to integrate, build, and reconfigure resources to adapt to market changes and capitalize on new opportunities. This enables companies to manage change proactively, accelerate innovation, and enhance customer experience, which positively affects performance, including sales and customer satisfaction. Dynamic capabilities also support continuous organizational learning, strengthen internal capabilities, and broaden the company's insight into emerging trends and technologies. Overall, the results of this study emphasize that dynamic capabilities are a key factor in improving company performance, allowing companies to be better prepared to face market challenges and create sustainable

competitive advantages. This research reinforces findings from Abu-Rumman et al. (2021), Kurnia Fitriati et al. (2020), and Correia et al. (2022) that dynamic capabilities have a positive and significant impact on company performance.

VI. Conclusion

This study shows that entrepreneurial orientation, knowledge management, and dynamic capabilities have a significant impact on company performance. Entrepreneurial orientation enhances dynamic capabilities and the effectiveness of knowledge management, which positively contributes to company performance. Effective knowledge management increases productivity and efficiency, while dynamic capabilities help companies adapt and innovate. The integration of these three variables is crucial to improving company performance in a competitive market.

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