



The Effect of Innovation, Customer Orientation and Digital Marketing on Business Performance Through Competitive Advantage as An Intervening Variable

(Study on UMKM Fashion and Crafts in Central Java)

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Abstract

This study aims to determine the role of Competitive Advantage in mediating the influence of Innovation, Customer Orientation with Digital Marketing on Business Performance (MSMEs). This research is included in quantitative research with explanatory research. The type of data used is primary data from questionnaires distributed to MSME Fashion and Craft business actors assisted by PT.XYZ in the Central Java region amounting to 104 people. The analysis technique used in this research is Partial Least Square-Structural Equation Modeling (PLS-SEM) with the SmartPLS approach. Hypothesis testing was carried out using the Bootstrap resampling method developed by Geisser and Stone, while the test statistic was the t statistic or t-test. The results of this study indicate that Competitive Advantage successfully mediates between Innovation and Customer Orientation on business performance (MSMEs). However, Competitive Advantage did not succeed in mediating between Digital Marketing and Business Performance (MSMEs).

Keywords: Innovation, Customer Orientation, Digital Marketing, Competitive Advantage, Business Performance.

INTRODUCTION

In the midst of a pandemic, it is necessary to have a perfect strategy so that MSMEs are still able to sell their products and receive profits, so that business performance (MSMEs) can continue to grow. During this pandemic, one strategy that allows MSME players to market their products without being constrained by policies during the pandemic is through innovation. In an increasingly competitive business landscape, innovation is recognized as a key driver for businesses that want to create value and sustainable competitive advantage (Wang and Wang, 2012). Innovation can be described into two levels viz: improvements and new directions (Verganti, 2016). While improvements are new solutions that aim to optimally an existing definition of value or an established problem (Verganti, 2016), new directions of innovation are more radical creating a new set of value propositions and new pathways. The emphasis on innovation has led to significant investigation by practitioners and researchers seeking to understand the role of innovation in enterprise performance (Datta and Roumani, 2015).

Not surprisingly, Enterprises with greater innovation have demonstrated a greater ability to develop new capabilities and respond to the evolving business climate leading to better performance (Calantone et al., 2002). Enterprise performance is a measure of how well an Enterprise can meet its goals and objectives compared to its main competitors (Cao and Zhang, 2011). In the Innovation variable, there are two different hypotheses. Innovation has no relationship to business performance (Surosowati, 2020 and Lestari, 2021). And innovation has a significant relationship to business performance (Rusenbergs, et al 2011); (Agus, 2021).

In building an innovation, customer orientation is necessary to achieve success. The definition of Customer Orientation itself is the willingness of the business to understand the needs and desires of customers and satisfy these customers. It is a process and activity that connects the creation and satisfaction of customers by continuously assessing customer needs and wants. In this new normal era, businesses are faced with highly competitive competition. The shift from a product and sales philosophy to a holistic marketing philosophy gives businesses a better chance of winning the competition. The basis of a well-formed marketing orientation is strong customer relationships. Marketers must relate to customers to inform involve themselves and maybe even encourage them into the process. (Wulandari, 2012). A positive relationship between customer orientation and business performance. This is in accordance with the results of Wulandari's research which states that Customer Orientation affects business performance. While in Customer Orientation on business performance there are also two differences in implications, namely Customer Orientation has a significant effect on business performance (Wulandari 2012, and Maurya et al 2015). And customer orientation has no significant relationship to business performance (Rachmat 2006).

In addition to innovating and being customer-oriented, MSMEs in this pandemic era must be able to carry out digital marketing strategies as one of the solutions in improving their business performance. Digital marketing is a promotional activity and market search through digital media online by utilizing various means such as social networks. The virtual world is no longer only able to connect people with devices, but also people with other people around the world (Mustika, 2019). Digital marketing usually consists of interactive and integrated marketing to facilitate interaction between producers, market intermediaries and potential consumers. Based on McKinsey's research, only around 30% of businesses in Indonesia use digital instruments in developing their business. Seeing this, we can conclude that the potential for digital marketing in Indonesia is still very large (Sulaksono, 2020). In fact, we know that MSMEs have an important role in driving the wheels of the Indonesian economy, especially in creating jobs and empowering home

industries to earn daily income. MSMEs are a good platform for productive job creation. MSMEs are labor-intensive businesses, do not require certain requirements such as the level of education, expertise (skills) of workers, and the use of relatively little business capital and the technology used tends to be simple (Ananda and Susilowati, 2019). The use of digital marketing provides new hope for MSMEs to survive the pandemic and develop into an economic powerhouse because the digital era is inevitable. Development of online-based promotional media by cooperating with application-based purchasing services. The use of applications provides an opportunity to expand market reach and become an important medium for communicating with customers as in the covid era where interaction with customers was limited (Narto and HM, 2020). The development of digital technology allows MSME players to market their products online and make transactions through the banking system online as well. This certainly facilitates transactions in the midst of a pandemic policy that limits direct interaction between traders and buyers. This will also have a positive effect on the performance of our MSME businesses, so that it can create growth in turnover, profit and repeat orders. Meanwhile, in the Digital Marketing Variable there are also two differences in hypothesis results, namely Digital Marketing has a significant effect (Swastuti, 2018 and Hendrawan, 2019). And Digital Marketing has no significant effect (Ezra, 2022).

Problem Identification

Based on the results of previous research, there is still controversy over several variables of Innovation, Customer Orientation and Digital Marketing on business performance (MSMEs), so it is still interesting to conduct further research, so that it is expected to explain the efforts of micro, small and medium enterprises in improving their business performance. Based on the description above, the formulation of the problem in the study: How to build a model of Innovation, Customer Orientation and Digital Marketing to improve business performance (MSMEs) through Competitive Advantage in Central Java. The general objective of this study is to test the empirical model that mediates the controversy about the effect of innovation, customer orientation, and digital marketing on business performance (MSMEs) by including competitive advantage variables as intervening variables. As for the specific objectives of this study are: the effect of innovation, customer orientation, and digital marketing on business performance (MSMEs) both directly and indirectly through the mediation of competitive advantage and compare the Resource Based Theory developed by Peteraf and Barney (2003) with the facts in the field.

LITERATURE REVIEW

Resources Based Theory (RBT)

According to (Wernerfelt, 1984) Resources Based Theory (RBT) is a theory developed to describe an advantage for companies which states that competitive advantage will be created if a company has professional resources

that are not available in other companies. This theory reviews how companies are able to utilize and manage existing resources. Where in the form of tangible assets and intangible assets. States that a potential strategy to improve company performance is to unite tangible and intangible assets. Resource-Based Theory (RBT) is an idea that develops in the theory of strategic management and competitive advantage of companies that believe that companies will achieve excellence if they have superior resources (Belkaoui, 2003). Some of the intangible assets in question are Innovation, Customer Orientation and Digital Marketing. By managing some of these intangible assets, businesses or MSMEs can affect MSME Business Performance and be able to provide an added value to their business.

Relationship between variables and hypothesis development

The Effect of Innovation on Competitive Advantage.

Innovation can make a product have an advantage over other products and can maintain a business position in the market. Competitive advantage is defined as a situation in obtaining an average profit higher than its competitors, so that the business can be said to be one step ahead of its competitors (Udaya et.al., 2013). Research conducted by (Hamdan, 2020), which uses Human Resource Variables, Innovation, Competitive Advantage and Business Sustainability. The results of his research state that there is a significant influence between Innovation and Competitive Advantage. Referring to the description above, the hypothesis proposed in the study is as follows:

H1: The influence between Innovation on Competitive Advantage.

The Effect of Customer Orientation on Competitive Advantage

Customer orientation is the acquisition and use of information about events, trends and relationships from customers in an organization, which is future action (Choo in Zaini et.al., 2014). The description above is in accordance with research by (Setiawan, 2015) who conducted research on the effect of customer orientation on competitive advantage in processing MSMEs in Palembang, with the results stating that customer orientation has a significant effect on competitive advantage. The process of identifying customer needs is useful for developing the adaptive capabilities of MSMEs, one of which is through the ability to access customers and be able to adjust and utilize strengths. Referring to the description above, the hypothesis proposed in the study is as follows:

H2: The influence between Customer Orientation on Competitive Advantage.

The Effect of Digital Marketing on Competitive Advantage

Planning and developing business products at affordable prices must attract consumer interest. Determination of the right product distribution channel as a means of outperforming competitors. Promotional activities by utilizing technology become their creativity and innovation (Müller, 2018). Research

conducted by (Rahayu, 2021) also shows a significant influence between Digital Marketing and competitive advantage.

H3: The influence between Digital Marketing on Competitive Advantage.

Effect of Innovation on Business Performance

The results of several studies show that innovation has a direct and positive effect on business performance. Research conducted by (Nguyen, 2011) conducted research on the effect of Marketing Capability and Innovation on Business performance in Vietnam, the results showed that marketing capability and innovation greatly affect business performance in Vietnam. There is a significant relationship between innovation and performance (Gurhan et.al, 2011). The results revealed that innovative enterprises have higher sales and exports. Also, higher product innovation correlates with higher market share. Innovative enterprises especially those with higher innovation scores for product, process, and organizational innovation had significantly higher total sales in exports. Research results that show the opposite about the effect of innovation and performance were found by (Rosenbush, 2011) that innovation has no significant relationship with SME performance.

H4: The influence between Innovation on Business Performance.

Effect of Customer Orientation on Business Performance

Research (Ruekert, 2010) describes customers as the level at which business units 1) obtain and use information from customers, 2) develop a strategy that can find customer needs, 3) implement strategies by listening to customer needs and shortcomings. The above discussion is in accordance with research conducted by (Wulandari, 2012) which examines the effect of customer orientation on business performance with the following results: Customer orientation affects the performance of MSMEs. Consumer growth which is an indicator of business performance can occur if the business is able to adapt to changes in surrounding customers, thereby minimizing the difference between the products produced by the business and consumer needs. Conducted research on the effect of customer orientation on MSME performance, and the result is that customer orientation has a positive effect on business performance (Maurya et.al., 2015). The adaptation process carried out by the business to customers makes the company know the needs of consumers and results in reduced barriers to entry into the segment so that business performance will increase. Referring to the description above, the hypothesis proposed in the study is as follows:

H5: The influence between Customer Orientation on Business Performance.

Effect of Digital Marketing on Business Performance

Chaffey and Chadwick (2012), digital marketing can be defined as a tool to achieve marketing targets through digital technology applications which include desktops, cell phones, tablets, and other digital platforms. Digital

marketing is a modern communication that uses the internet and digital technology and has a relationship with traditional communication to achieve goals. Therefore, to create a good integrated message, digital marketing must be followed by a promotional mix to be more optimal. In (Swastuti's, 2018) that Digital Marketing has an influence on business performance and affects the development of MSMEs. Meanwhile, research conducted by (Hendrawan, 2019) states that Digital Marketing conducted by PT.X can increase sales. Along with increasing digital transformation, businesses can achieve better customer offerings through greater customization, increased customer satisfaction and reduced sales costs (Brynjolfsson and Hitt, 2000) ; (Mithas et al., 2005). In research conducted by Agus Kurniawan, et al (2021) which states that Digital Marketing Transformation affects Business Performance. Referring to the description above, the hypothesis proposed in the study is as follows:

H6: The influence between Digital Marketing on Business Performance.

Effect of Digital Marketing on Business Performance

Businesses experience competitive advantage when actions in an industry or market create economic value and when several competing businesses engage in similar actions (Barney, 2010). Competitive advantage is expected to be able to achieve profits as planned, increase the market, increase customer satisfaction and continue the survival of a business (Saiman, 2014). The results of this study state that there is a significant influence between competitive advantage and MSME performance. Every organization has unique characteristics of the organization that cannot be imitated or owned by competitors. This uniqueness is able to create a competitive advantage of an organization which will improve the performance of the business / organization. Businesses that have good competitiveness will tend to have good performance. This is supported by research conducted by Ismail et.al (2010) entitled "The Relationship Between Organizational Competitive Advantages for firm performance" which is moderated by age and business size.

H7: Competitive Advantage has a significant influence on business performance.

The Effect of Innovation on Business Performance Through Competitive Advantage.

Research (Gurhan et.al, 2011) there is a significant relationship between innovation and performance. The results reveal that innovative businesses have higher sales and exports. Also, higher product innovation correlates with higher market share. Innovative businesses especially those with higher innovation scores for product, process, and organizational innovation have significantly higher total sales in exports. Research conducted by (Ketut, 2018) found that innovation has a significant influence on competitive advantage so that it also affects the performance of MSME businesses in Gianyar Regency, Bali province. Pointing to the description above, we can justify that:

H8: Competitive Advantage can mediate Innovation on Business Performance.

The Effect of Customer Orientation on Business Performance Through Competitive Advantage.

In research (Maurya et.all., 2015) conducted research on the effect of customer orientation on the performance of MSMEs, and the result is that customer orientation has a positive effect on business performance. Christian (2019) conducted research on the effect of customer orientation on competitive advantage in processing MSMEs in Rembang, with the results stating that customer orientation has a significant effect on business performance through competitive advantage as an intervening variable. Pointing to the description above, we can justify that:

H9: Competitive Advantage can mediate Customer Orientation on Business Performance.

The Effect of Digital Marketing on Business Performance Through Competitive Advantage.

In research conducted by (Kurniawan, et all., 2021) which states that Digital Marketing Transformation affects Business Performance. Research conducted (Swastuti, 2018) revealed that digital marketing management has an impact on improving business performance, through competitive advantage. Research conducted by (Rahayu, 2021) also shows a significant influence between Digital Marketing and competitive advantage. Pointing to the description above, we can justify that:

H10: Competitive Advantage can mediate Digital Marketing on Business Performance.

RESEARCH METHODS

This research is included in quantitative research because the research data is in the form of numbers and analysis using statistics. While the type of research is explanatory research, because it intends to explain the position of the variables studied and the influence between one variable and another. The type of data used is primary data from the research sample with a simple random sampling technique which obtained 104 MSME Fashion and Craft business actors assisted by PT.XYZ. Collection using a questionnaire in the form of a list of questions for MSME actors. The data analysis in this study used Descriptive Analysis with a minimum scoring technique of 1 and a maximum of 10. The analysis technique used in this research is Partial Least Square-Structural Equation Modeling (PLS-SEM) with the SmartPLS approach.

RESULTS AND DISCUSSION

Characteristics of Respondents

Of the 104 respondents, 19 were male and 85 were female. This indicates that the majority of Fashion and Craft business owners are women and indicates that women are the foundation of the economy. As for the distribution of

business length, <5 years were 61 people, 6-10 years were 39 people, while 11-15 years were 3 people and >15 years were 1 person. The distribution of the respondents' education level is mostly D3-S1, namely 71 people, then respondents with high school / high school education levels, and there are 19 respondents with S-2 education levels and 14 people.

Validity Test

The output results show that the loading factor for each construct above the required 0.50 to 0.60 is considered sufficient (Chin, 1998). The results of the complete outer loading can be seen in the following tables:

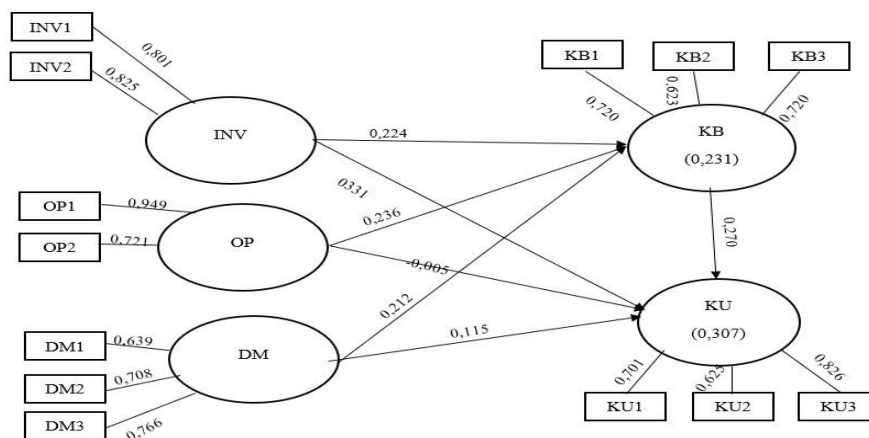
Table 1
Factor Loading Value per Indicator after Dropping

Variables	Indicator	Loading Value	Description
Innovation (X1)	INV.1	0,801	Valid
	INV.2	0,825	Valid
Customer Orientation (X2)	OP.1	0,949	Valid
	OP.2	0,721	Valid
Digital Marketing (X3)	DM.1	0,639	Valid
	DM.2	0,703	Valid
	DM.3	0,766	Valid
Competitive Advantages (Z)	KB.1	0,720	Valid
	KB.2	0,623	Valid
	KB.3	0,720	Valid
Bussiness Performance (Y)	KU.1	0,701	Valid
	KU.2	0,625	Valid
	KU.3	0,826	Valid

Source: Primary data processed, 2022

And described in the Model Structure as follows:

Figure 1
Outer After Dropping Process



Source: Primary data processed, 2022

Based on the loading value of all respondents in table 5.0, it is found that the loading value of each indicator on each variable has a loading value > 0.50 so it can be concluded that all indicators on all respondents have met convergent validity.

Reliability Test

The output results show that the loading factor for each construct is still above the required 0.50 to 0.60 which is considered sufficient for a study in a field that can still be developed (Ghozali, 2015). The results can be seen in table 2 as follows:

Table 2
Composite Reliability

Category	Composite Reliability Value				
	INV	OP	DM	KB	KU
All Respondents	0,633	0,707	0,638	0,728	0,764

Source: Processed Primary Data, 2022

Based on the results obtained in the table above, it is known that all variables from all respondents have the required composite reliability value of 0.50-0.60, so it can be concluded that all variables in all sample criteria are said to have met the composite reliability requirements.

Testing the structural model (Inner Model)

The results of the SmartPLS calculation of the coefficient of determination can be seen from the following table:

Table 3
Coefficient of Determination

Matrix	R-Square	R-Square Adjust
Competitive Advantages	0,231	0,208
Bussiness Performance	0,307	0,279

Source: Primary data processed, 2022

Table 4
PLS Predict

Kategori	RMSE	MAE	MAPE	Q ² Predict
KB1	1,312	1,125	20,005	0,081
KB2	1,296	1,134	19,385	0,027
KB3	1,131	0,918	14,928	0,093
KU1	1,295	1,101	18,447	0,065
KU2	1,165	0,982	15,952	0,014
KU3	1,375	1,154	23,385	0,167

Source: Primary data processed, 2022

From the model built, the coefficient of determination (adjusted R Square) on Business Performance is 0.279. The total determination value of 0.279 means

that 27.9% of variation in business performance is influenced by variations in innovation, customer orientation, digital marketing and competitive advantage, while the remaining 72.1% is explained by other factors not included in the model. So from the Adjust R Square value, the influence of the four exogenous variables on changes in endogenous variables falls into the weak category. (Hair et.al.2011). Based on the data presented in table 4.6, it can be seen that the Q square value on the dependent variable of each indicator $Q^2 \text{ square} > 0$. So it can be concluded that this study has a good / good observation value (Chin, 1998).

Table 5
ss Hypothesis Testing of Direct Influence and Indirect Influence

		Ori.saml (O)	Stad.Dev (STDEV)	T Statistics (O/STDEV)	P Values	KET
H1	Inov -> Kebers	0,224	0,093	2,417	0,016	Diterima
H2	Orpelg -> Kebers	0,236	0,093	2,542	0,011	Diterima
H3	Digmar -> Kebers	0,212	0,113	1,885	0,060	Diterima
H4	Inov -> Kinjus	0,331	0,092	3,597	0,000	Diterima
H5	Orpelg -> Kinjus	-0,008	0,109	0,071	0,943	Ditolak
H6	Digmar -> Kinjus	0,115	0,102	1,120	0,263	Ditolak
H7	Kebers -> Kinjus	0,270	0,094	2,875	0,004	Diterima
H8	Inov -> Kebers -> Kinjus	0,061	0,035	1,749	0,081	Diterima
H9	Orpelg -> Kebers - > Kinjus	0,064	0,034	1,846	0,065	Diterima
H10	Digmar -> Kebers - > Kinjus	0,057	0,042	1,366	0,173	Ditolak

Source: Primary data processed, 2022

For hypothesis testing using a statistical value of alpha 10% (Ferdinand, 2013) the statistical value is > 1.96 . So that the criteria for acceptance or rejection of the Hypothesis is H1 accepted and H0 rejected when the t-statistic > 1.96 . To reject or accept a hypothesis using probability, H1 is accepted if the P Value is 0.10 (Hulland, et al, 1996). Based on Table 5. it is known that H1 (accepted), meaning that Innovation has a significant influence on competitive advantage with a positive direction, in agreement with (Vanessa, 2014), and (Wulandari, 2012) which states that Innovation has a significant positive effect on competitive advantage. H2 (accepted), Customer Orientation has a significant effect on competitive advantage with a positive direction, in agreement with (Cristian, 2019) and (Maurya et.all., 2015) which state that Customer Orientation has a positive effect on competitive advantage. H3 (accepted), meaning that digital marketing has a significant effect on competitive advantage, in agreement with (Lestari, 2021) and (Agus, et all., 2021) which state that Digital Marketing has a positive effect on competitive advantage. H4 (accepted), meaning that Innovation has a significant effect on business performance in a positive direction, agreeing with (Rosenburg, 2011), (Wulandari, 2012), and (Vanessa,

2014) who state that Innovation Affects Business Performance, while also refuting the opinions of (Nguyen, 2011), (Lestari, 2021) and (Surosowati, 2020). H5 (rejected), meaning that Customer Orientation has no significant effect on business performance, this agrees with (Rachmat, 2006), which states that Customer Orientation has no effect on Business Performance, but refutes the opinions of (Wulandari, 2012), (Maurya et al., 2015) and (Christian, 2019) which state that Customer Orientation has a significant effect on Business performance. H6 (rejected), meaning that digital marketing has no significant effect on business performance, in agreement with (Ezra, 2022) where digital marketing has no effect on the performance of MSMEs, as well as refuting the opinion of (Agus, 2021), (Lestari, 2021), (Swastuti, 2018) which states that Digital Marketing has a positive influence on Business Performance. H7 (accepted), meaning that competitive advantage has a significant effect on business performance in a positive direction, in agreement with (Cristian, 2019) and (Surosowati, 2020) who state that competitive advantage affects business performance. which shows that competitive advantage significantly and positively affects business performance. H8 (accepted), meaning that innovation has a significant influence on business performance through competitive advantage, this opinion is in accordance with the research of (Ketut, et al., 2018) which states that there is a significant indirect effect between innovation on business performance through business performance. H9 (accepted), meaning that customer orientation has a significant effect on business performance through competitive advantage, in agreement with the research of (Azizah, et al., 2017) where customer orientation has a significant effect on business performance through competitive advantage. H10 (rejected), meaning that digital marketing does not have a significant effect on business performance even through competitive advantage as a mediating variable, in agreement with (Ezra's, 2022) where digital marketing has no effect on MSME performance through competitive advantage.

Conclusions and Implications

Conclusion on the research problem

This study seeks to answer the differences in research results on the effect of innovation, customer orientation, and digital marketing on business performance (MSMEs), by building an empirical model of innovation, customer orientation, and digital marketing for micro, small and medium enterprises in an effort to optimize business performance. Based on the empirical studies that have been carried out, it can be concluded that: 1).The competitive advantage construct can mediate the effect of innovation and customer orientation on business performance; 2). The innovation construct affects business performance; 3), The effect of innovation on business performance mediated by competitive advantage, turns out to have a greater influence than the direct effect of innovation on business performance.

Managerial implications

Based on the empirical results above, it can be seen that customer orientation is the variable that has the least influence on business performance (MSMEs) compared to innovation and digital marketing. For this reason, to optimize the business performance of MSME players, it is necessary to innovate continuously through product innovation and business organization, through the ATM (Observe, Imitate, Modify) process for companies or businesses that continue to carry out the innovation process, so that MSME players can continue to survive.

Limitations of the study

After analyzing and drawing conclusions, the limitations of this study were found, namely: four variables that affect business performance in this study only have an impact of 23.10% while the rest is influenced by other variables not examined in this study;

Future research agenda

It is necessary to conduct an interview process as additional in-depth information using languages that are easily understood by respondents and retest the model, especially the rejected hypothesis.

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