

Analysis of Effects of Environmental Dynamism, Entrepreneurial Orientation, and Dynamic Capability on the Performance of SMEs

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Abstract - Economists and researchers acknowledge that SMEs (small, and medium enterprises) have a good enough flexibility in the face of environmental change. Although, some issues became an obstacle for this type of business to improve its performance. The purpose of this thesis was to examine and analyze the environmental effects of Dynamism, entrepreneurship orientation, dynamic capability for performance of SMEs, so that these types of businesses could grow and thrive. The study was conducted to 210 SMEs (small and micro enterprises) which are spread throughout Jakarta, Depok, Bandung, Yogyakarta and Jember. The method used SEM (Structural Equation Model). The results showed that environmental Dynamism has the greatest influence on the change in the performance of SMEs in Indonesia. However, dynamic capability did not affect the performance improvement at the level of SMEs.

Keywords—SME; Environmental Dynamism; Entrepreneurial Orientation, Dinamic Capability, Firm Performance

I. INTRODUCTION

Micro, Small and Medium Enterprises (SMEs) is one type of business that is considered quite flexible in the face of environmental change (Guo and Cao, 2013). SMEs have an organizational structure that is simple, so make the effort jobs is able to adapt more quickly in response to movement of the business world. Based on the national history of Indonesia in 1998 (Carre & Thurik, 1998), when Indonesia was hit by the economic crisis, SMEs being the only type of business that can survive at a time when various large businesses should be "folded". On toughness SME, Indonesia was able to bounce back from the crisis.

Tedjasuksmana (2014) said there were a few roles of micro, small and medium enterprises (SMEs) in the economy of Indonesia, namely: (1) its position as a major player in economic activity in various sectors, (2) provision largest employer, (3) an important player in the development of local economic activity and community development, (4) the creators of new markets and sources of innovations, and (5) contribution to maintain the balance of payments through export activities of society so as to reduce poverty and others. SMEs have a pretty good contribution to the national economy, providing employment for 97.2% of total employment provided and accounted for about 56.5% of GDP in 2014 (CBS, 2014). This makes SMEs have national economic activity is quite strategic.

As one type of business that has great potential in economic development, SMEs can not be separated from the various obstacles in its development. SMEs turned out to be quite difficult to grow their businesses become larger. The obstacles are one of them can not be separated from the influence of an increasingly dynamic environment. The dynamic environment became one of the challenges to be faced by the organization in its business (Baron, 2010). Increasingly dynamic environment led to various changes in the model of competition, consumer demand, business trends and others. The changes that are a challenge for any company, can be countered by increasing its capabilities so that more flexible in following currents business changes occur.

The literature and the opinion of the experts explained that SMEs indeed become a variety of business is taken into account to maintain the strength of economic growth, but it remains a major challenge to sustain their performance in the long term (Ates, et.al, 2013). Competitive advantage would be one measure to assess the performance of each company. One of the distinguishing capabilities is the effect of the dynamic capability that is owned by the company.

In addition to dynamic capabilities, the owner of the company needs to build entrepreneurial orientation in business. One of the challenges faced by SMEs is how the business is able to meet market demand. Long (2013) said that the higher the entrepreneurial orientation of the company, then the chances of the company to meet the market demand would be even greater. Entrepreneurship orientation become the focus of its own for SMEs, especially in the use of the opportunities and resources to the type of business (Alarape, 2014).

SMEs have some problems that limit the motion of running a business. Some problems and challenges of SMEs are also described by the Ministry of Cooperatives and SMEs in their strategic plan within the period from 2015 till 2019. SMEs face issues related to HR (human resources) is low, the role of support systems are less than optimal, as well as the lack of effective policies and related regulations. Meanwhile, SMEs also face some challenges in the development of its business, including the following: increased formalization of business, productivity, capacity to build partnerships in global marketing, use of the opportunities MEA, as well as the improvement of policies and regulations that are responsive to increased performance and competitiveness of SMEs.

Therefore, in order to improve the performance of SMEs (Small and Micro Enterprises), this study seeks to build a proper model in order to SMEs in Indonesia can grow and develop. The study was conducted by analyzing the

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environmental effects of Dynamism on entrepreneurial orientation, dynamic capability and performance of MSEs.

II. THEORETICAL BACKGROUND

2.1 Environmental Dynamism

The environment has an influence on strategy, process, and organizational performance (Pasaribu, 2013; Goll & Racheed, 2004). In a turbulent business environment, the company leaders must be responsive for scanning the external business environment in order to improve company performance. Dynamic environment explains the amount and rate of change facing companies in the environment settings (Schneider & Spieth, 2013; Dess & Beard, 1984; Miller & Friesen, 1983).

A dynamic environment is characterized by rapid change and the emergence of a crisis situation (Shamir & Howell, 1999; Pawar & Eastman, 1997). In general, dynamic environment and instability describes the rate of change in the external environment (Dess & Beard, 1984).

The increasing dynamism of the environment occurs, it will make it increasingly difficult for all parties as the top management team, the stakeholders (stakeholders), and other parties to access accurately on environmental conditions present and future (Jiao et. Al , 2011). The dynamic environment is also defined as the rate the tendency of consumers and the services offered by the organization changed continuously (Wijibenga & Witteloostuijin, 2007).

2.2 Entrepreneurial Orientation

Entrepreneurship and strategic management concern for the growth and wealth creation (Tuluca & Yurtkur, 2015). Shane (2006) stated that entrepreneurship is an important part of the world economic system. It gives the sense that the economic development front, certainly needed a businessmen or owners of a company that continues to innovate, and certainly supported by a strong entrepreneurial character.

Entrepreneurial orientation (EO) is described as a strategic process at the company level in which businesses use to gain a competitive advantage (Rauch & Frese, 2009). EO is also defined as an effort of the organization to be able to find and accept new opportunities as well as taking responsibility for the impact on the change (Moris et. al, 1996).

In measuring the EO, Miller (1983) composed of three dimensions, namely: risk-taking, innovativeness, and proactiveness. Several other authors also measured EO into three dimensions as Miller stated (Ortega, 2013; Hakala, 2011; Covit et. al, 2006).

2.3 Dynamic Capability

Teece, et. al (1997) defined dynamic capability as the company's ability to analyze, establish new opportunities and protect assets and to reconfigure the knowledge and competencies with the aim for achieving a sustainable competitive advantage. The definition is in line with Helfat, et. al (2007) which gives a description that dynamic capabilities as the capacity of an organization to expand, create or modify the resource base.

In a situation of rapid change and unpredictability (Eisenhardt & Martin, 2000), the organization's ability to develop new forms of competitive advantage referred to as "dynamic capabilities" (Teece et. al, 1997). Competitive

advantage can be achieved by improving the competence of the company's resources in creating something called VRIN (valuable, rare, inimitable, and nonsubstitutable) (Nedzinskas et. al, 2013).

Teece (2007) said that through the dynamic capabilities, companies can manage resources more optimally. Dynamic capability not only can be used on large companies with the organization that has been structured, but this theory can also be used in the context of Micro and Small Enterprises (SMEs), such as research in Lithuania (Nedzinskas et. al, 2013).

Nedzinskas (2013) in his study, measurements of dynamic capability through three indicators, namely: sensing, seizing and reconfiguring. All three indicators are also based on previous research (Teece, 2007).

2.4 Firm Performance

The company's performance can be a reference to how the company achieved substantial success in business. Lin & Huang (2012) stated that performance of a partner company associated with the dynamic capabilities. In studies that have been done Sikander (2013), suggested that the strategy of using technology to do exactly, so that the company's business objectives can be achieved (performance).

Performance becomes a measurement system that plays an important role in the development strategy of the company as well as an evaluation of the attainment of organizational goals (Rahman & Ramli, 2014; Velez-Gonzales et. al, 2011). At various empirical research, organizational performance measurement can be done by looking at the performance of a financial and non-financial performance.

2.5 Small and Micro Enterprises (SMEs)

Micro, Small and Medium Enterprises (SMEs) in Indonesia currently has a major contribution to the GDP and the economy of Indonesia (bi.go.id). It is also one of the positive impacts on the ability of SMEs resilient in the face of economic turmoil that is compared to other types of businesses.

The success of SMEs turned out to provide a wide impact on the national economy. In 2014, the number of SMEs in Indonesia was as much as 57.89 million units or about 99.99% of the total number of businesses nationwide. In addition, SMEs contribute to employment for 96.99% and amounted to 60.35% of GDP (beritasatu.com).

Some versions of related SMEs based on the number of employees, amount of turnover, as well as business assets. The Ministry of Cooperatives and SMEs of Republic of Indonesia provide a definition of SMEs based on the amount of assets and turnover, there are: 1) Micro, which has the maximum assets of IDR 50 million; 2) Small businesses with the assets between IDR 50 million to 500 million; and 3) Medium enterprise which has total assets of more than IDR 500 million.

III. RESEARCH MODEL AND METHODOLOGY

3.1 Research Model

One of the important factors that affect the competitive strategies in each of the companies is the business

environment (Ting, 2006; Randall et. Al, 2003; Huang et. Al, 2002; Naylor et. Al, 1999; Fisher 1997). Environmental conditions are constantly changing or dynamic external factors affecting the company in any business activity that is lived. In general, dynamic environment and instability describe the rate of change in the external environment (Dess & Beard, 1984).

Some of these statements suggest that in a dynamic environment, it takes a behavior to take risks are quite high (Ruiz-Ortega et. Al, 2013). Dare to take risks is one of the characteristics of entrepreneurial orientation (Zehit et. Al, 2015; Ruiz-Ortega et. Al, 2013; Hakala, 2011; Covit et. Al, 2006; Atuahene- Gima and Ko, 2001; Miller 1983).

Ying Li (2012) stated that the EO has long been recognized as the key to creating innovative activities, due to the dynamic environment requires employers to be able to integrate the resources and resolve discontinuities. Meanwhile, in order to maintain their competitive edge, companies need to update their resources either externally through a process of dynamic capabilities (Teece, Pisano, & Sharen, 1997; Makadok, 2001; Helfat et al, 2007; etc.).

Based on some of the above description, the environmental impact study to analyze the dynamic, entrepreneurial orientation, and dynamic capabilities on the performance of SMEs in a number of MSE (Micro and Small Enterprises) in Indonesia. Figure 1 illustrates model in this study.

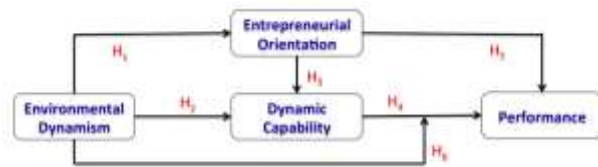


Fig 1. Research Model

Based on the research model that has been illustrated in Figure 1, then the hypothesis in this study are as follows:

H₁ : Environmental Dynamism positively affect Entrepreneurial Orientation of SMEs in Indonesia

H₂ : Environmental Dynamism positively affect Dynamic Capability of SMEs in Indonesia

H₃ : Entrepreneurial Orientation positively affect Dynamic Capability of SMEs in Indonesia

H₄ : Dynamic Capability positively affect Performance of SMEs in Indonesia

H₅ : Entrepreneurial Orientation positively affect Performance of SMEs in Indonesia

H₆ : Environmental Dynamism is moderating positively on the relationship between Dynamic Capability and Performance of SMEs in Indonesia

3.2 Methodology

This study uses quantitative methods and data on each respondent was obtained through primary data collection. Primary data were obtained through questionnaires collecting the respondent.

The model is built in this research is expected to help SMEs to take advantage of business opportunities optimally. The purpose of this study was to test hypotheses about the

relationship between the environmental dynamic, entrepreneurial orientation, dynamic capability and performance of the company. Data were collected through a survey questionnaire distributed online as well as directly to the respondent.

The unit of analysis in this study is the small businesses in Indonesia specifically in Jakarta, Depok, Bandung, Yogyakarta and Jember. Respondents in this study are the owner or person in charge of SME. The target sample size is the number of 180 SMEs. Methods of data analysis used in this study are SEM (Structural Equation Model). In the SEM analysis, a statistical tool used in this study was 8.8 lisrel software.

IV. RESULT AND DISCUSSION

4.1 Result

SEM analysis was used to test hypotheses about the relationship between the environmental dynamic, entrepreneurial orientation, dynamic capability, and performance of SMEs. Hypothesis testing will be done based on coefficient and t-value contained in the entire latent variables. The following Table 1 will show the results of analysis of the research hypothesis.

Table 1. Hypotheses Test Result

Hypotheses	t-value	Coefficient
H ₁	7.04	1.02
H ₂	6.82	.80
H ₃	2.11	.21
H ₄	-.46	-.29
H ₅	1.97	.56
H ₆	3.51	.67

Based on Table 1, it can be seen that some of the hypothesis in this study received or have significant influence, namely: H₁, H₂, H₃, H₅, and H₆. Hypothesis 4 regarding the effect of the dynamic capabilities of the performance does not have a significant effect. So in this study, hypothesis 4 was rejected.

4.2 Discussion

Based on the research results, there is a hypothesis that is rejected, whereas the five other hypothesis is accepted. The discussion will detail explanation of each hypothesis test results performed.

- a. Environmental Dynamism positively affect Entrepreneurial Orientation of SMEs (H₁: positive significant)

The external environment has a strong influence on how the company manages its strategy in achieving the desired results, such as an increase in the volume of sales, profits, income and many other things that give a positive value for the company. SMEs in this study was very influenced by the external environment is dynamic, in accordance with the results shown in Table 1, with a value of 7.04 which is large enough to influence the entrepreneurial orientation.

The external environment is increasingly dynamic in the study include: consumer dynamism and dynamism

competitors. According to the data analysis of the study, the SMEs are quite aware and understand that this is indeed the consumers and their competitors more dynamic. Their competitors have a sales strategy that is increasingly diverse and demand from consumers continues to grow. So businesses need to be responsive to address these challenges, by improving entrepreneurial orientation.

Jogja which became one of the areas of research has batik is sufficiently developed. One of the big challenges facing the batik makers is how to maintain customer loyalty. Through entrepreneurial orientation, they are able to innovate as a solution over the other batik competitors who sell at a cheaper price. Programming is done by creating a combination of "batik tulis" and "batik cap" to produce more economical.

b. Environmental Dynamism positively affect Dynamic Capability of SMEs (H2: positive significant)

The results of the analysis to support several previous studies that say that the dynamic environment has a positive influence on the dynamic capabilities (Helfat, et. Al, 2007; Walker & Priem, 2003; Eisenhardt & Martin, 2000; Teece et. Al, 1997). The existence of an increasingly dynamic environment, make the SMEs involved and to better optimize the dynamic capabilities possessed.

Some manufacturers of food / beverage in Depok, Bandung, and Jember, in response, have been able to see changes in the environment to understand the challenges faced competition. One optimized dynamic capability is to maintain product quality and product ownership is unique and difficult to imitate by competitors.

c. Entrepreneurial Orientation positively affect Dynamic Capability of SMEs (H3: positive significant)

The research result supports previous empirical studies (Subha & Narasimha, 2011; Jiao et. Al, 2010; Zahra et. Al, 2006; Jantunen et. Al, 2005). Owned entrepreneurial orientation, would make the company be more innovative in improving the quality of its products.

d. Dynamic Capability positively affect Performance of SMEs (H4: not significant and rejected)

The results of the study do not support several previous studies (Arifin & Firmanzah, 2015; Pezeshkan et. Al, 2015; Nedzinskas et. Al, 2013; Peteraf et. Al, 2013; Arend, 2012). In the context of SMEs, when seen from several indicators of research, it has a reliable workforce, have products that are unique and difficult to imitate, and the market acceptance of a product for theoretical capability of dynamic did not have much effect on increasing sales volumes, increased profits, revenue, or award obtained in the business.

In the context of SMEs, the performance improvement is more influenced by the ability or the purchasing power of consumers and economic stability. SMEs in sectors like handicrafts and garment industry in this study have quite complained about the amount of revenue, profitability and sales volume tends to decrease when compared to last year. This was caused by the decline in purchasing power, especially on local products.

e. Entrepreneurial Orientation positively affect Performance of SMEs (H5: positive significant)

The results of the analysis in this study supports several empirical studies earlier which led to that there is a significant relationship positive between entrepreneurial orientation on performance (Kim & Jyeock, 2016; Shan et. al, 2016; Zehir et. al, 2015; gupta et. al, 2014 ; Long, 2013). In the context of SMEs, the results of this study will enrich the academic literature that supports that the better a company has an entrepreneurial orientation, then the company will be able to improve its performance.

The innovative and proactive attitude in this research is able to produce a further effect on relationships how SMEs improve their performance. Almost all industrial sectors expressed the same thing that the more innovative and proactive in an effort to take risks in creating a unique product, it will affect the increase in sales volume.

f. Environmental Dynamism is moderating positively the relationship between Dynamic Capability and Performance of SMEs (H6: positive significant)

The results of the analysis in Table 1 that support some previous research that says that dynamic environments have a moderating influence positively on the relationship between capability and dynamic performance (Fainshmidt, 2014; Tiantian et. Al, 2014; Sirmon & Hitt, 2009; Zhan & Luo, 2008). In the context of SMEs, although quite dynamic business environment, however, uniquely SMEs are increasingly stimulated to adapt and improve its performance. Characteristics of SMEs are more flexible in adapting to all the changes that happen to be one of the foundations that these types of businesses are considerable potential in the national economy.

V. CONCLUSSION AND IMPLICATIONS

5.1 Conclusion

The importance of the right model for SMEs will help to optimize the potential of its resources and improve company performance. Increasing the performance of SMEs was very influenced by changes in the dynamic environment, through the entrepreneurial orientation of the perpetrators of such business. The external environment has an enormous influence on the business activity of SMEs. Changes in consumer tastes and the movement of competitors is an indication of the increasingly dynamic business environment.

5.2 Implications

Based on the research results, it obtained three implications. Managerial implication mentions that the SMEs to further optimize the dynamic capabilities, such as creating a product that is difficult to imitate by competitors. In addition, the environmental theory of dynamic external factors is the most encouraging changes in the behavior of SMEs in creating a performance became the theoretical implications. Finally, the policy implications may be mentioned that the government should make regulations which is more structured from the central government to the regions in order to the implementation could be more implementing effectively.

VI. LIMITATIONS

This research have several limitations, they are : (1) the sample size was still small; (2) the study did not conduct a comparative analysis of the respondent were divided into three sectors of the industry; and (3) the assessment of the performance of the SMEs had limited access, and it was only measured by the perceptions of business owners. For further studies, researchers are expected to get a larger sample size, in order to have better describe about the condition of SMEs in Indonesia. In addition, a comparative analysis of differences in the industrial sector needs to do to be able to add more comprehensive discussion. Afterward, the performance assessment is expected not only based on the perceptions from its owners, but it also can be seen on the financial condition and the market analysis of each of the respondents .

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