

Can innovation mediate the effect of adaptability, entrepreneurial orientation on business performance?

Enni Savitri^{a*}, Emrinaldi Nur DP^a and Almasdi Syahza^b

^aFaculty of Economics and Business, Universitas Riau, Indonesia

^bFaculty of Teachers Training and Education, Universitas Riau, Indonesia

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ABSTRACT

Business performance is one of the entrepreneurial behavior benchmarks. Small, and Medium Enterprises (SMEs) are required to have dynamic capabilities and strategies that can seize opportunities and improve the market. The aim of this paper is to analyze the effect of adaptability and entrepreneurial orientation on business performance through innovation as mediation. Based on interviews and questionnaires distributed to 115 SMEs in coastal areas. The research results show that adaptability and entrepreneurial orientation have effects on innovation. Adaptability and entrepreneurial orientation have no effects on business performance. Innovation has effects on business performance. Adaptability and entrepreneurial orientation have effects on business performance through innovation as mediation. This study enriches the current literature by providing a contribution and insights to understanding how Resources Based View (RBV) theory affects business performance and innovation on SMEs in coastal areas in Indonesia. The implications of this study on entrepreneurship orientation in SMEs will help to increase resources for innovation. This emphasizes how the RBV approach used in this research helps improve business efficiency by leveraging existing capital in microbusinesses into a source of excellence. The government is working on policies to enhance the efficiency of SMEs in Indonesia.

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1. Introduction

Small, and Medium Enterprises (SMEs) play a significant role in the development of the economy (Venancio & Pinto, 2020), especially in terms of the aspects relating to creating employment opportunities, equal income distribution, development of the rural economy, and non-oil and gas exports. Nowadays, the pressure of global business competition as well as other factors such as technological development, demographic and social change, innovation ability, financial support, and entrepreneurship, have affected SMEs. Therefore, SMEs should have dynamic capabilities and strategy to seize business opportunities and improve the market. The success of a business is determined by its performance (Savitri et al., 2020). The business performance shows the company's level of achievement in a certain period (Wheelen & Hunger, 2015). Many factors affect the company performance such as entrepreneurial orientation (Gupta & Batra, 2016; Veselovsky et al., 2019), adaptability culture (Umrani et al., 2017; Ngo & Loi, 2008), and innovation (Rangus & Slavec, 2017; Terziovski, 2010; Ha et al., 2020; Snieška et al., 2020). Other factors that also affect the company performance are business strategy, human resource management, entrepreneur characteristics, and the business itself. However, research that emphasizes the mediating role of innovation on the relationship between adaptability and entrepreneurial orientation toward SME performance has not been

* Corresponding author.

E-mail address: enni.savitri@lecturer.unri.ac.id (E. Savitri)

available in developing countries like Indonesia. Research on the role of adaptability, entrepreneurial orientation, and innovation on business performance has been partially found in various pieces of management literature, but those empirical studies are mostly conducted on large companies in industrialized countries. To date, the research results that integrate those four variables in an empirical model are still unclear. The market dynamic in developing countries is very different from industrialized countries. In general, market conditions in developing countries are characterized by low market growth, changing buyer preferences, and high intensity of competition. On the other hand, some developing countries have experienced rapid market growth, high demand for products, and a high number of new competitors.

This research tries to develop the empirical research model on the role of adaptability, entrepreneurial orientation, and innovation as intangible resources and competitive advantage to improve business performance. The research idea is developed based on Resources Based View (RBV) theory. This research combines the variables of entrepreneurial orientation, innovation, and adaptability to determine their effects on business performance. Entrepreneurship and innovation are two interrelated discourses in the business environment. Innovation implements creativity in developing unique ideas or solutions, while entrepreneurship transforms ideas or innovations into actual products. This research is conducted in coastal areas and watersheds of Indonesia. Some of the population there, especially those in rural and coastal areas, have a low level of welfare. This condition can be seen from the subsistence level of the economy, low productivity, and low skill levels. The intense competition of SMEs in Indonesia has encouraged entrepreneurs to develop entrepreneurial orientation with high innovation to improve their business performance. Besides, entrepreneurs should also have adaptability and innovation to surpass competitors, creating customer satisfaction orientation and coordination among functions. This research explains the effect of adaptability and entrepreneurial orientation on business performance and innovation as mediation. The research results show that adaptability and entrepreneurial orientation affect innovation. Innovation affects business performance. Adaptability and entrepreneurial orientation affect business performance through innovation as mediation. The originality of this research is to use the RBV theory in explaining the relationships between entrepreneurial orientation, adaptability, and business performance by observing the role of innovation in coastal areas in Indonesia.

2. Literature Review and Hypothesis Development

The RBV theory states that organizational resources including tangible and intangible resources are a source of competitive advantage. The organization's performance is shaped by a unique combination of resources the organization has. These resources include physical assets and competencies. The sources of competitive advantage in a company are often multifactorial. Therefore, those sources cannot only refer to one resource (Fleisher & Bensoussan, 2003). This condition indicates that efforts are needed to connect various resources as a driver of competitive advantage. Adaptability is defined as a complex set of beliefs, assumptions, and symbols of organization value that differ from one organization to another (Barney, 1991). One of the important indicators of adaptability is organizational learning. Based on RBV theory, organizational learning is considered to be one of the important resources in achieving sustainable competitive advantage. Organizational learning is a complex resource that is difficult to imitate, useful for product development activities, and can be maintained as a source of competitive advantage (Moya-Clemente et al., 2021). An organization should develop an environment that encourages the development of ideas to facilitate innovation (Chen, 2017). Tuominen et al. (2004) state that some components of adaptability are significantly different from a more innovative company to a less innovative company. These indicate that adaptability has a positive role in improving innovation. Based on the description above, the proposed research hypothesis is:

H₁: Adaptability affects innovation.

Retnawati and Retnaningsih (2020) describe entrepreneurial orientation as a tendency of individuals to innovate, be proactive, and willing to take risks in starting a business. According to the RBV perspective, entrepreneurial orientation is an organizational capability that contributes to creating a positional advantage and unique organizational resources. So, entrepreneurial orientation is one of the resources of competitive advantage. Gupta and Batra (2016) state that entrepreneurial orientation is an intangible resource and capability in achieving competitive advantage and improving the performance of a small business. Traditionally, the literature considers innovation as an indicator of entrepreneurship because entrepreneurial orientation can improve the company's proactiveness, the willingness to take a risk, and innovate. Thus, entrepreneurial orientation and innovation may be related. Entrepreneurial orientation is one of the antecedents of innovation, so it is expected that entrepreneurial orientation plays a positive role in improving innovation. According to Alhakimi and Mahmoud (2020) as well as Xia and Ge (2019), entrepreneurial activities have a direct influence on product, process, and administrative innovation. Based on the description above, the following hypothesis is put forward:

H₂: Entrepreneurial orientation affects innovation.

Adaptability is an important factor in organizational success. Business performance can be improved by managing organizational culture. It can encourage the development of effective and efficient organizational mechanisms, influence economic and social goals, and encourage cooperation among the organization's members (Riyanto & Hapsari, 2020). Organizational culture has the potential to influence organizational performance. The organization's values and beliefs will determine how the organization is run and how it performs (Steiger et al., 2014). Lots of companies have a competitive

advantage and are extremely successful because they have a powerful factor, which is organizational culture. Organizations that have strong adaptability often experience sales growth and increased market share. Adaptability as an aspect of the nature of culture has a major influence in a changing environment. Adaptability has three components that are positively related to business performance, i.e. creating change, customer focus, and organizational learning. Adaptability has a positive role in business performance. Ngo and Loi (2008), as well as Umrani et al. (2017) find a positive relationship between adaptability culture and organization performance. Based on the description above, it is expected that there will be a positive role of adaptability on business performance. Therefore, the following hypothesis is put forward:

H₃: Adaptability affects business performance.

Entrepreneurial orientation is a company orientation that has the principle of identification and exploration toward opportunities (Lee & Wenyi, 2011). Hafeez et al. (2012) state that a company that has a strong entrepreneurial orientation will have the ability to innovate more than other companies. Lee and Wenyi (2011) state that a company that has a strong entrepreneurial orientation is more courageous in taking risks. In a dynamic environment, entrepreneurial orientation is a very important factor for company survival. Entrepreneurial orientation becomes the basis for entrepreneurs to look for opportunities to gain success. Entrepreneurial orientation is an important contributor to a company's success as well as the key to improving company performance (Mahmood and Hanafi, 2013; Arief et al., 2013). Better company performance can stimulate entrepreneurial orientation. Furthermore, the effect of entrepreneurial orientation on company performance is more visible in SMEs (Bakar et al., 2016). A better entrepreneurial orientation will improve the company's capability in selling products towards better business performance. Entrepreneurial orientation has a directly positive and significant relationship with company performance. Entrepreneurial orientation is determined by the strength of the entrepreneur's orientation. Entrepreneurial orientation determines the growth of a small company (Gupta & Batra, 2016; Alvarez-Torres et al., 2019). Based on the description above, the next proposed research hypothesis is as follows:

H₄: Entrepreneurial orientation affects business performance.

Improvements in business performance are driven by efforts to innovate in the business environment (Ha et al., 2020). Innovation works more efficiently and effectively in most small businesses (Chen, 2017). However, many SMEs are unable to innovate at all. Various kinds of literature have discussed the obstacles faced by SMEs in innovating, such as lack of financial resources, inadequate management, and marketing, lack of skilled workers, lack of information and external relations, or barriers due to government regulations. One of the significant characteristics of an entrepreneur is the ability to innovate (Terziovski, 2010). A company will not be able to survive without innovation. The customers' wants and demands are always changing. Thus, the company needs continuous innovation to survive. Rangus and Slavec (2017), Terziovski (2010), and Ha et al. (2020) find a positive relationship between innovation and business performance. Based on the description above, the following hypothesis is put forward:

H₅: Innovation affects business performance.

The RBV theory describes that a unique combination of tangible and intangible resources is a real source of competitive advantage. According to Marketing and Strategic Management literature, two intangible resources affect organizational performance, namely organizational culture and organizational innovation (Assensoh-Kodua, 2019). Adaptability has a positive role in improving innovation in micro-business that the higher the adaptability, the higher the innovation. Zhang et al. (2009) argue that adaptability has a positive influence on business performance. Meanwhile, Rangus and Slavec (2017) state that innovation has a positive influence on business performance. It means the relationship between adaptability and business performance is hypothesized to be an indirect relationship. Therefore, innovation plays a mediating role in adaptability and business performance. Implicitly, the effect of adaptability on business performance is mediated by innovation. Based on the description above, the next research hypothesis is as follows:

H₆: Adaptability affects business performance through innovation.

Entrepreneurial orientation is an important component of business development. Lee and Wenyi (2011) state that the higher the entrepreneurial orientation, the greater the company's ability to market its product towards better business performance. Furthermore, innovation is also an important component of business development. Innovation will increase the added value of a product as well as creating a new product to fulfill customer satisfaction. Without innovation, a company will not be able to compete with competitors. In Pakistan, innovation becomes a missing link that connects entrepreneurial orientation and performance for SMEs. It also has a crucial relationship in business growth and is one of the factors that differentiates the excellence of one business from another (Hafeez et al., 2012). It means the relationship between entrepreneurial orientation and business performance is hypothesized to be an indirect relationship, Alegre and Chiva (2013) and Parkman et al. (2012) argue that innovation mediates the effect of entrepreneurial orientation on company performance. Based on the description above, the following hypothesis is put forward:

H₇: Entrepreneurial orientation affects business performance through innovation.

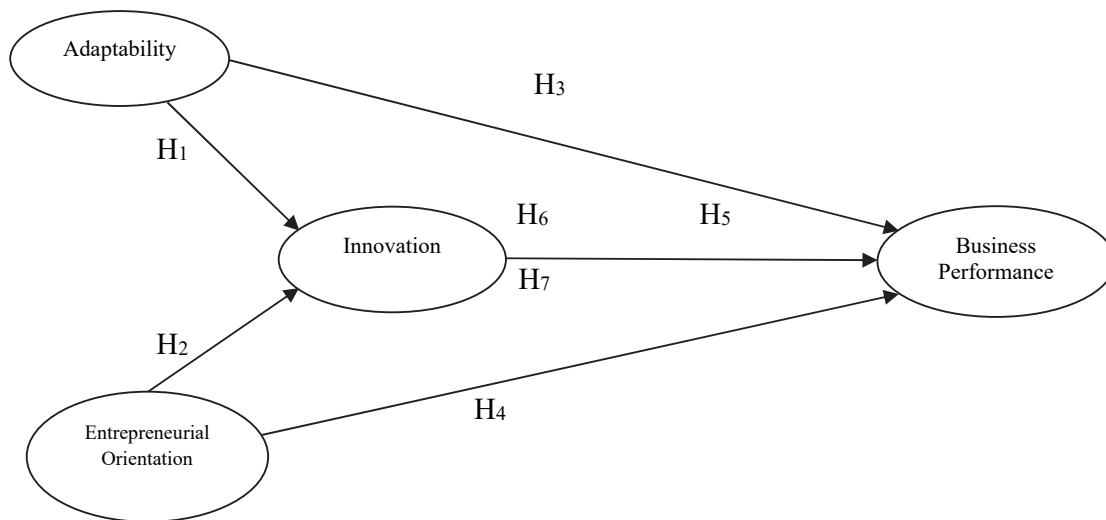


Fig. 1. Research Framework

3. Research Method

There are 115 SMEs in coastal areas in Indonesia. They are selected as the research samples using the Simple Random Sampling method. Samples also meet the criteria of having the legal status of SMEs has and having been established for at least two years (i.e., Domicile Permit, Business Permit, Halal Certificate, Tax Identification Number). The primary data were obtained by the questionnaire from the SMEs office. Around 585 questionnaires were distributed but out of them only 360 were returned that represents 67.95 percent response rate. Organizational culture or adaptability is a complex set of beliefs, assumptions, and symbols of organizational values that differ from one organization to another (Barney, 1991). Adaptability indicators include conducting change, customer focus, supplier focus, and organizational learning. Entrepreneurial orientation is a tendency of individuals to innovate, be proactive, and willing to take risks in starting a business. The measurement indicators of entrepreneurial orientation include innovativeness, proactiveness, risk-taking, competitive aggressiveness, and autonomy (Miller, 1983). Innovation is ideas, practices, or objects that are considered new to persons or other user units. The measurement indicators of innovation include product innovation, process innovation and marketing innovation. Business performance is a result of resource empowerment through an efficient and effective strategy (Wheelen and Hunger, 2015). The measurement indicators of business performance include sales growth, profit growth, and asset growth, all of which are compared to the previous year's growth. Analysis of path analysis has been used in order to analyze the data. The study uses path analysis to determine the causal relationship, with the aims of explaining the direct or indirect influence of the dependent variable and the independent variables. It analyzes whether there is an influence on adaptability, entrepreneurial orientation, on business performance through innovation.

4. Results

4.1 Hypothesis Testing

4.1.1 Result of the Evaluation of the Structural Model or Inner Model

The coefficient of determination uses R^2 that shows what percentage of endogenous variation can be explained by the construct that is hypothesized to influence it (exogenous). R^2 only exists for the endogenous variable. The result of *the* R^2 value indicates the innovation variable which can be explained by the adaptation and orientation variables is only 35%. It means the effect of adaptation and orientation toward innovation is a moderate effect. Furthermore, the performance variable which can be explained by the adaptation, innovation, and orientation is only 27%. It means the effect of adaptation, innovation, and orientation toward the performance is also a moderate effect.

Table 1

Test Result of Model Fit Indices

No.	Model Fit and Quality Indices	Fit Criteria	Analysis Result	Explanation
1.	Average Path Coefficient (APC)	$p < 0.05$	0.280 ($p = 0.001$)	Good
2.	Average R-Squared (ARS)	$p < 0.05$	0.293 ($p = 0.001$)	Good
3.	Average Adjusted R-Squared (AARS)	$p < 0.05$	0.293 ($p = 0.001$)	Good
4.	Average Block Variance Inflation Factor (AVIF)	Acceptable if ≤ 5 Ideally ≤ 3.3	1.228	Ideal
5.	Average Full Collinearity VIF (AFVIF)	Acceptable if ≤ 5 Ideally ≤ 3.3	1.389	Ideal
6.	Tenenhau Goodness of Fit (GoF)	Small ≥ 0.1 Medium ≥ 0.25 Large ≥ 0.36	0.556	Large

As shown in Table 1, the value of the Average Block Variance Inflation Factor (AVIF) is 1.228 and the Average Full Collinearity VIF (AFVIF) is 1.389, both of which are less than 3.3. It means there is no multicollinearity problem between

the indicator of exogenous variables. While the value of Tenenhaus Goodness of Fit (GoF) is 0.556, which is higher than 0.36, it indicates that the predictive power of the model is large. The result of the Tenenhaus Goodness of Fit (GoF) calculation shows the measurement performances of the model (outer model) and structural model (inner model) are appropriate because it has a value of 0.556 (above 0.36). Therefore, this research model, which includes the factors that affect innovation-mediated performance, is appropriate and proper to use.

The result of the research hypotheses test is shown in Fig. 2.

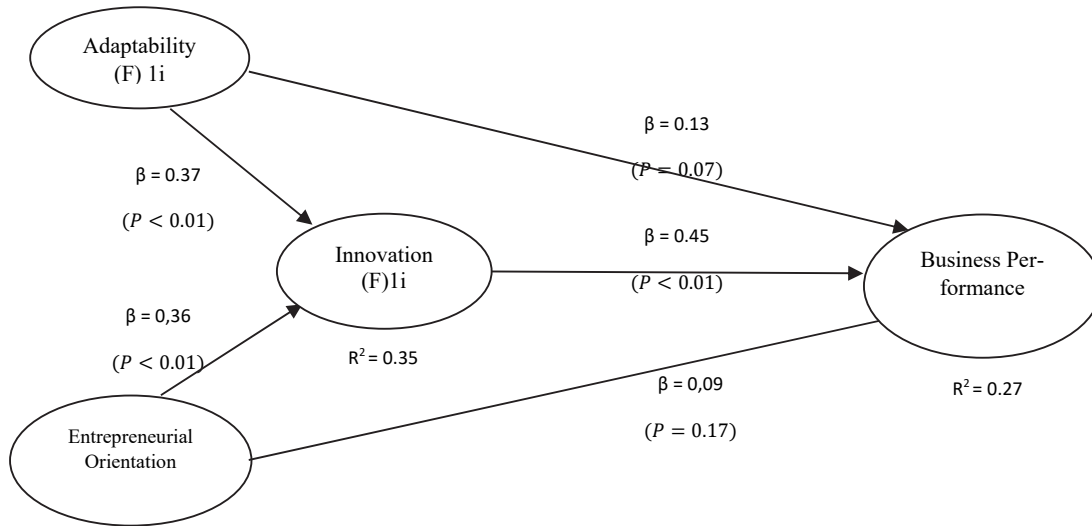


Fig. 2. Statistical Result of the Effect between Variables

Details of the result of hypothesis 1 to hypothesis 5 testing are shown in Table 2. It appears that adaptability affects innovation; entrepreneurial orientation affects innovation; adaptability does not affect business performance; entrepreneurial orientation does not affect business performance, and innovation affects business performance.

Table 2
Result of Hypothesis Testing of Direct Effect

Hypothesis	Path	Direct Effect		Explanation
		Coeff	p-value	
H ₁	Adaptability → Innovation	0.37	< 0.01	Significant (+)
H ₂	Entrepreneurial Orientation → Innovation	0.36	< 0.01	Significant (+)
H ₃	Adaptability → Business Performance	0.13	0.07	Insignificant
H ₄	Entrepreneurial Orientation → Business Performance	0.09	0.17	Insignificant
H ₅	Innovation → Business Performance	0.45	< 0.01	Significant (+)

4.1.2 Result of Direct Effect Test

The test of the effect of the mediating variable is conducted in two ways: 1.) calculating the path coefficient by including the mediating variable in the empirical model, and 2.) calculating the path coefficient without including the mediating variable in the empirical model. The result of the test on the direct effect model is shown in Fig. 3, as follows:

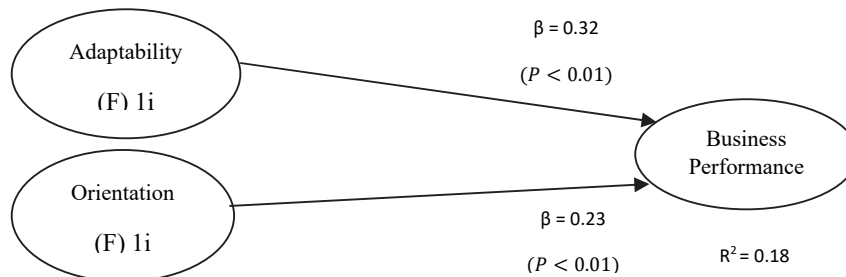


Fig. 3. Result of Testing the Direct Effect Model

Fig. 3 shows the estimation result of path coefficients while testing the effect power of predictor variable toward criterion without the role of mediation is shown in Table 3. The test result shows adaptability and entrepreneurial orientation do not affect business performance.

Table 3

Test Result of the Direct Effect of Independent Variable on the Dependent

Path	Direct Effect		Explanation
	Coeff.	p-value	
Adaptability → Business Performance	0.32	< 0.01	Significant (+)
Entrepreneurial Orientation → Business Performance	0.23	< 0.01	Significant (+)

4.1.3 Result of Indirect Effect Test

Table 4 shows the path of the indirect effect of adaptability to innovation, and innovation to business performance has a significant coefficient. The coefficient of adaptability to business performance is insignificant ($p = 0.07$), but testing on the direct effect model shows that the coefficient of adaptability to business performance is significant ($p = 0.01$). A change of coefficient and p-value on the relationship of adaptability to business performance occurs before and after the inclusion of the innovation variable, so it can be concluded that innovation is a form of full mediation. Therefore, H6 is accepted, meaning that innovation can mediate the relationship of adaptability to business performance.

Table 4

Result of the Sixth Hypothesis Testing

Path	Direct Effect		Explanation	Path
	Coeff	p-value		
Adaptability → Innovation	0.37	< 0.01	Significant (+)	Indirect effect
Adaptability → Business Performance	0.13	0.07	Insignificant	Indirect effect
Innovation → Business Performance	0.45	< 0.01	Significant(+)	Indirect effect
Adaptability → Business Performance	0.32	< 0.01	Significant (+)	Direct effect

The indirect effect of entrepreneurial orientation variable toward business performance is mediated by innovation, as shown in Table 5. The result shows the path of the indirect effect of innovation to business performance, and entrepreneurial orientation to innovation, have a significant coefficient. The coefficient of entrepreneurial orientation variable to business performance is insignificant, but testing on the direct effect model shows that the effect of entrepreneurial orientation on business performance is significant, with a coefficient value of 0.23 and a p-value of 0.01. A change of coefficient and p-value on the relationship of entrepreneurial orientation to business performance occurs before and after the inclusion of the innovation variable, so it can be concluded that innovation is a form of full mediation. It means innovation can mediate the relationship of entrepreneurial orientation to business performance.

Table 5

Result of the Seventh Hypothesis Testing

Path	Direct Effect		Explanation	Path
	Coeff	p-value		
Entrepreneurial Orientation → Innovation	0.36	< 0.01	Significant (+)	Indirect effect
Entrepreneurial Orientation → Business Performance	0.09	0.17	Insignificant	Indirect effect
Innovation → Business Performance	0.45	< 0.01	Significant (+)	Indirect effect
Entrepreneurial Orientation → Business Performance	0.23	< 0.01	Significant (+)	Direct effect

5. Discussion

5.1 The Effect of Adaptability on Innovation

The low ability of SMEs to create change, organizational learning, and customer focus, indicates a lack of adaptive values that improve innovation, be they related to process innovation or product innovation. According to the perspective of RBV theory, a unique combination of tangible and intangible resources is a real source of advantage competitively (Barney, 1991). One intangible resource is organizational culture. An organization should develop an environment that encourages and supports the development of ideas to facilitate innovation (Mazur & Zaborek, 2016). Organizational culture is considered an important factor in innovation performance. The low ability of SMEs to create change, organizational learning, and customer focus, shows that adaptive value is less able to increase innovation, both process innovation, and product innovation. These results are the low indicators of ability to create change, organizational learning, and customer focus show that SMEs lack adaptive cultural values that can increase innovation, both process innovation, and product innovation. Parkman et al. (2012) find that a higher level of innovation is concerned with emphasizing the culture of learning and development. Organizational learning can be easily associated with the result of innovation. Xia and Ge (2019) describe that the important part of the first

stage of the innovation process is openness to innovation: whether the organization members are willing to learn and change, or whether they are resistant to innovation. The results of this research are in line with the research of Savitri et al., (2020), which shows that organizational cultures with flexibility and adaptability have positive impacts on organizational innovation. Tuominen et al. (2004) have also found that adaptability plays a positive role in improving innovation.

5.2 The Effect of Entrepreneurial Orientation on Innovation

Entrepreneurial orientation is found to play a positive role in improving innovation, meaning that entrepreneurial orientation can increase the ability to innovate. According to the perspective of RBV theory, entrepreneurial orientation is an organizational capability that contributes to the creation of unique organizational resources that have a positional advantage. This statement is following the phenomena observed in the field. The low results of innovation and risk-taking indicators show that SMEs pay less attention to the willingness to innovate and the courage to take risks in developing new products. A company orientation that has the principle of identifying and exploiting existing opportunities (Lee & Wenyi, 2011). The component of entrepreneurial orientation includes creativity in innovating, courage in taking a risk, flexibility, anticipating, and being proactive in promoting products as well as creating changes to products. The high number of product innovations among SMEs in Indonesia is partly due to the influence of entrepreneurial orientation. The respondents' perceptions show that they consider SMEs in Indonesia to have a high entrepreneurial orientation, when taking into account the courage of SMEs in terms of: taking risks; the ability to change according to customer demands; responsiveness to all changes and opportunities; and having experience in entrepreneurship. Entrepreneurial orientation is one of the antecedents of innovation (Alegre and Chiva, 2013). It is an orientation of trying to be the first to innovate products, dare to take risks, and take positive action to beat competitors (Miller, 1983). A manager who has the courage to take risks and accept failure will tend to introduce new products in response to possible changes in customer demand. Lee and Wenyi (2011) describe that in the context of entrepreneurship, proactiveness is concerned with the a forward-looking perspective, and tending to take the initiative by anticipating and pursuing new opportunities to seize market opportunities. Several researchers, such as Alhakimi and Mahmoud (2020) and Xia and Ge (2019), argue that entrepreneurial activities have a direct effect on the innovation of product, process, and administration. Entrepreneurial orientation is one of the important drivers of innovation (Parkman et al., 2012). The results of this research are in line with the research of Hafeez et al. (2012) in Pakistan, and Galindo and Picazo (2013) in ten developing countries.

5.3 The Effect of Adaptability on Business Performance

The research result shows adaptability does not improve the performance of SMEs. Most SME entrepreneurs are not always willing to practice new, more efficient, and economical ways of producing goods. They are also less able to respond well to changes in the business environment and work well with workers and other parties to make changes. Most micro-entrepreneurs have not encouraged their workers to innovate, have not seen failure as a learning opportunity, and have not realized that learning is an important goal in their daily work. This is perhaps because of the low level of education of SME entrepreneurs, and a lack of technical skills in producing innovative goods. Most SMEs entrepreneurs are not always willing to practice more efficient and economical new ways to produce goods. They are also less able to respond well to various changes in the business environment, as well as to cooperate well with workers and other parties to make changes. Most micro-entrepreneurs have not encouraged their workers to innovate, have not seen failure as a learning opportunity, and have not realized that learning is an important purpose in daily work. It may be due to the low level of education of SME entrepreneurs, and the lack of technical skills in producing innovative goods. The results of this research are in line with the research of Bourgeois (1980) which states that adaptability doesn't affect business performance. Stoica et al. (2008) also find that the relationship between adaptability and performance is non-linear. However, a different result is found in the research of Ngo and Loi (2008) and Umrani et al. (2017), which suggests a positive relationship between cultural adaptability and organizational performance.

5.4 The Effect of Entrepreneurial Orientation on Business Performance

Entrepreneurial orientation doesn't affect business performance. Although the level of entrepreneurial orientation is high, it will not directly improve business performance. In fact, entrepreneurial orientation tends to play a negative role in business performance. This may be due to the fact that entrepreneurship activities generally require more resources than conservative organizations (Alvarez-Torres et al., 2019). Efforts in finding opportunities for new activity and products often require high cost and time without a performance improvement guarantee. Thus, if this is not properly managed, it will result in a decrease in business performance. Most SMEs do not take the initiative in looking for opportunities to try new activities and are less active in anticipating changes in consumers. In the aspect of innovativeness, it is known that SMEs are trying to develop new products, and are not always trying to make changes to product types gradually or radically. SME owners think that the innovative products they have produced so far have not produced maximum profits even though the time and capital costs which have been spent are quite large; additionally, most products with the latest designs are mostly only used as materials for exhibition and trade promotion purposes. In the aspect of competitive aggression, SME actors tend to avoid direct competition with other micro-entrepreneurs, are less aggressive in competing and strive less to beat competitors.

SME entrepreneurs are not aggressive in competing and tend to avoid direct competition with other micro-entrepreneurs. They also tend not to give freedom to their workers to pursue a business opportunity. Micro-business workers cannot make decisions on their own without the owner's permission. Furthermore, most SME entrepreneurs don't have the courage to achieve a breakthrough in producing goods but prefer to produce low-risk goods. They also doubt that the courage to enter new markets is necessary to achieve the company's goals. The results of this research are in line with the research of Boohene (2018) and Lomborg et al. (2017) where it is stated that entrepreneurial orientation doesn't give positive results in terms of performance. However, the results of this research are not in line with the research of Gupta and Batra (2016) and Alvarez-Torres et al. (2019), which find a positive effect of entrepreneurial orientation on business performance.

5.5 The Effect of Innovation on Business Performance

Innovation affects business performance and has an important function in management. In product innovation, process innovation, and marketing innovation, SMEs do not implement their innovative activities to improve business performance. The findings of this research show that innovation plays a positive role in improving business performance: the higher the innovation, the higher the business performance. It means innovation is one of the important factors that determines the level of business performance improvement. A higher level of innovation will encourage a higher level of SME performance in Indonesia. In contrast, if the level of innovation is low, the SME's performance will also decline. According to Barney (1991), to achieve a competitive advantage, the company's resources should have four important criteria; they should be: valuable, rare, inimitable, and irreplaceable. Nieves et al. (2014) show that the Resource-Based View affects the innovation capacity of a company. The strategy of the Resource-Based View affects increasing the organization's performance (Urbancova, 2013). The results of this research are in line with the argument of Snieška et al. (2020) which states that innovation cannot be separated from business life because innovation is the soul of a company; innovation can develop anywhere and be carried out by anyone. Innovation is not only carried out by large companies but also small companies need to innovate for the sustainability of their business. Innovation provides a means for an organization to create a competitive advantage in the market, which, in turn, will provide superior financial performance (Chen, 2017). On the other hand, when innovation has the potential to create opportunities in improving performance, it can be very costly and risky and has the potential to decrease financial performance (Nieves et al., 2014). These findings are in line with Terziovski's (2010) which state that innovation is the main driving factor of the performance of SMEs, especially in the manufacturing sector. The same findings are also present in the food sector, where innovation has a close relationship with the performance of SMEs. This means that whatever business sector they are engaged in, SME entrepreneurs should be able to create an innovative atmosphere and actions to encourage better business performance. This research is also consistent with the research of Ranguis and Slavec (2017) and Ha et al. (2020).

5.6 The Effect of Adaptability on Business Performance Through Innovation

Innovation plays a role as the mediating variable of adaptability on business performance. In other words, adaptability doesn't have a direct positive role in improving business performance. But if innovation is added as a mediator to this relationship, adaptability will indirectly play a positive role in improving business performance. Based on the RBV theory, adaptability can be a source of competitive advantage that will affect business performance. Furthermore, business performance is determined more by the outcome process that accompanies it. The improvement of business performance as the final result will depend on the escalation of innovation as a result of the mediating process in the relationship between entrepreneurial orientation and business performance. The findings of this research explain why several companies experience low business performance even though they have a high level of adaptability. This may be due to the absence of innovation as a determinant of business performance in this relationship. This means that even though the company can create various changes and always carry out organizational learning, if those actions are not able to create innovation of products or processes, then it doesn't play a positive role in business performance. Therefore, it is acceptable to conclude that adaptability through the mediation of innovation will be able to improve business performance.

5.7 The Effect of Entrepreneurial Orientation Through Innovation on Business Performance

Innovation plays a role as the mediating variable of entrepreneurial orientation on business performance. The findings of this research show that entrepreneurial orientation has an indirect effect on business performance. Entrepreneurial orientation doesn't play a direct positive role in improving business performance. But if innovation is added as a mediator to this relationship, entrepreneurial orientation will indirectly play a positive role in improving business performance. There are two ways to improve business performance: by increasing innovation; and by improving entrepreneurial orientation before increasing innovation. This research proves that the enhancement of innovation is not only achieved by observing the external environment of market opportunities, but also by paying attention to the aspects of an externally oriented organizational culture and entrepreneurial orientation. The findings of this research explain why several companies experience low performance even though they have a high entrepreneurial orientation. This may be due to the absence of innovation as a determinant of business performance in this relationship. This means that even though the company has a high level of entrepreneurial orientation through entrepreneurship activities, if the company is not able to create innovation in terms of product or process, then the high level of entrepreneurial orientation doesn't have a positive role in business performance.

These findings are in line with the research of Alegre and Chiva (2013), Parkman et al. (2012) and Hafeez et al. (2012) which state that higher entrepreneurial orientation will indirectly improve business performance through the full mediation of innovation. This means that through the mediation of innovation, entrepreneurial orientation will be able to improve business performance.

6. Conclusion and suggestion

6.1 Conclusion

Adaptability affects innovation. SMEs need a high level of adaptability to be able to adapt well to changes in the external environment, so they can improve innovation. Entrepreneurial orientation affects innovation. As an intangible resource, entrepreneurial orientation plays a positive role in improving innovation in SMEs. Adaptability doesn't affect business performance. The creation of changes and organizational learning as the main indicators of the adaptability of SMEs does not directly improve sales and profit. Entrepreneurial orientation does not affect business performance. The entrepreneurial orientation of SMEs does not directly generate profit. Innovation affects business performance. Improvement in innovation will determine the success of the business performance of SMEs. SMEs that have high adaptability and have high innovation will be able to improve business performance. Meanwhile, to increase innovation, micro-businesses must be able to develop adaptability in the form of creating change, organizational learning, and focusing on customers and suppliers.

6.2 Suggestion

SMEs that have high adaptability and have high innovation will be able to improve business performance. Meanwhile, to increase innovation, micro-businesses must be able to develop adaptability in the form of creating change, organizational learning, and focus on customers from suppliers. Adaptability improves business performance through innovation. Many SMEs have a high level of adaptability but their business performances are still low. SMEs can create various changes along with the changes in the external environment; they also always carry out organizational learning activities. If these efforts can lead to innovation of a product or process, then the creation of changes from organizational learning will play a positive role in business performance. Through innovation, entrepreneurial orientation will be able to improve the business performance of SMEs. SMEs need a high level of entrepreneurial orientation to improve business performance through innovation enhancement. The ability of SMEs to continuously create adaptive change and organizational learning will gradually improve their innovation. Those conditions will have an impact on increasing sales and profit growth, thus affecting their business performance positively.

7. Limitations and research implementation

7.1 Limitations

There are several limitations in this research that should be considered. First, the measurement of research variables relies only on the perceptions of business owners. The perceptions of other stakeholders such as customers, suppliers, or workers are not considered in this research. Future research should use several respondents in each sample of micro-enterprises. In particular, for the adaptability variables, it is better not only to use micro-entrepreneurs as respondents but also to use workers so that the possibility of measurement error can be minimized. Second, this research does not use a control variable. The measurement of the variables also does not differentiate in terms of gender in the research sample. Future research should use control variables such as the micro-entrepreneurs' age, especially in testing the role of entrepreneurial orientation and innovation on business performance. Besides, the differences in micro-business performance that are based on the respondents' characteristics such as gender, for example between male and female micro-entrepreneurs, would be interesting to study in future research.

7.2 Research Implementation

The large contribution of RBV in this study can be proven in the magnitude of the value of the direct effect of adaptability in improving entrepreneurial orientation in micro-enterprises. Besides, the role of entrepreneurship orientation in MSMEs can offer resources to increase innovation. This shows that the RBV approach in this study contributes to improving business performance by turning existing resources in micro-businesses into a source of excellence.

7.3 Managerial Implications

The findings of this study may contribute ideas to the government for policies to improve the performance of MSME businesses. The results of this study can provide the best solutions regarding policies in order to solve problems based on phenomena related to innovation and business performance in SMEs. In micro-businesses that have resource characteristics with a high level of entrepreneurial orientation, improving business performance can be achieved by efforts to increase innovation. Meanwhile, in micro-businesses that have resource characteristics with a low level of entrepreneurial orientation,

improving business performance can be achieved by increasing adaptability accompanied by increased innovation. Activities to empower and foster micro and small businesses need to be carried out continuously to improve adaptability, entrepreneurial orientation, and business performance innovation.

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