

## The Model of Firm Performance Improvement through Entrepreneurial Competence

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### Abstract

*Micro, Small and Medium Enterprises (MSMEs) are flourishing in Indonesia and contributing greatly to Gross Domestic Product of Indonesia. This attracted the attention of many people to examine more about Micro SME and its development. The purpose of this study is to identify the variable forming firm performance with case studies on food MSMEs in Bandung city. This study tried to answer questions about the MSME performance improvement model of Bandung city. The method used is survey by distributing questionnaires to 40 MSMEs in Bandung. Testing of variable in this research by using Partial Least Square (PLS) test. The findings of the study revealed that firm performance model (MSMEs) has a significant influenced by entrepreneurial competency moderated by competitive scope. The managerial implication of this research is expected that the actors of MSMEs can improve their ability on financial knowledge and organize their business in order to grow and become big company in the future which can give contribution of bigger economic development to the country.*

*Keywords: Firm Performance; Entrepreneurial Competence; MSME*

JEL Classification: M12

### 1. Introduction

Micro, Small and Medium Enterprises (MSMEs) are rife in Indonesia and play a role as the motor of the economy in Indonesia. This can be seen from the increasing contribution of MSMEs sector to Gross Domestic Product (GDP) and employment by MSMEs, and contribution of MSMEs to export. Based on the article on the official website of the Ministry of Industry, during the last five years

the contribution of MSMEs to GDP increased from 57.84% to 60.34% (Kompas, 2016). Employment by MSMEs also increased over the last 5 years, from 96.99% to 97.22%. In 2015, MSMEs contribution to Indonesian exports reached 15.8%.

MSMEs are also developing in Bandung, the capital of West Java. Based on the article UNESCO (Gibbons, 2015), Bandung is a city famous for its creativity. In 2015, Bandung was named one of the cities included in UNESCO Creative City Network (UCCN). In 2012, MSMEs in Bandung reaches 3,000 units and continues to grow every year. MSMEs in Bandung consist of various sectors, such as culinary, fashion, handicrafts, arts, and others. Based on the article on the site finance seconds (Riyanti, 2016) states that MSMEs in the city of Bandung is growing rapidly. In this article also mentioned that in 2016 the growth of SMEs in the city of Bandung reached 7.8%, while economic growth in Indonesia only 4.7%.

There are several programs conducted by Bandung City Government to support MSMEs including: Gadgets Mobile Application for License, against illegal moneylenders program, creative centre, and little Bandung store in another country. Bandung Municipal Government program to develop MSMEs will succeed if greeted by the spirit to advance by the MSMEs, so that MSMEs can avoid the business decline and failure. The main problems that cause MSMEs failure are business management capability, limited human resource quality, and weak access to financial institutions (Adawiyah, 2011).

Other causes of MSMEs failure are poor decision making, inability of management (management in competence), lack of experience and poor financial control (Scarborough & Zimmerer, 2000). Demographics, psychological, behavioral, and managerial and technical abilities are the main causes of MSMEs failure (Gerli, Gubitta, & Tognazzo, 2011). So it can be concluded that the competence of MSMEs actors is very decisive in the business development that it does as expressed by (Sánchez, 2012). Competence is the most measurable and related to firm performance (Herron & Robinson, 1993). The advance or retreat of MSMEs can be seen from the entrepreneurial competence of the owner.

This research uses descriptive design that tries to reveal some factors forming the improvement of firm performance through applying influence of entrepreneurial competence variable with moderated by organizational capability and competitive scope variable. This research model has been applied previously by (Sánchez, 2012) at SMEs in Spain. Compared to previous research conducted by (Sánchez, 2012), in this study we tested the model again with different characteristics MSMEs especially in Bandung, Indonesia.

## 2. Literature Review

In this research will be studied about the firm performance on the existing food MSMEs in Bandung. Business owners are generally known as "entrepreneurs" and requirements that must be owned by entrepreneurs to succeed business is competence. Competence was initially assessed by (Boyatzis, 1982) who declared competence as "a capacity that exists in a person that leads to behaviour that meets the job demands within the parameters of organizational environment, and that, in turn brings about desired results". (Spencer & Spencer, 1993) states that competence is a characteristic that exists within a person which will determine the effectiveness and / or superior performance of his work.

This theory of competence then developed into something that should exist in the managerial position employees in a company (managerial competency) Burgoyne, 1988; Albanese, 1989; Stuart and Lindsay, 1997 which was cited by (Xiang, 2009). Managerial competency discusses personal characteristics such as the nature, knowledge, skills and attitudes of individual managers. Research conducted by (Sidek & Mohamad, 2014) states that managerial competency has a significant and positive influence on business growth.

Basically entrepreneurs and managers have the same role in terms of management (organizing) and personnel management, so that in its development entrepreneurs adopt the theory of competence in running their business. Then in the last few years the study of competence in this business is to study the characteristics of entrepreneurial competency (Xiang, 2009).

This study refers to research that has been done by (Sánchez, 2012). In his research Sanchez found entrepreneurial competence will affect firm performance is devoted to small business or SMEs in the Spanish. In his model, entrepreneurial competency will affect the organizational capability and the competitive scope of the organization and has direct impact on firm performance. The explanations of each variable that forms the model of firm performance improvement are described below.

### *2.1 Entrepreneurial Competence*

Nakhata cited by (Sari P. A., 2014) defines entrepreneurial competence as an individual characteristic, including personality trait, knowledge and skills that will be directed to the effectiveness or height of entrepreneurial performance that can be estimated through entrepreneur behaviour. So if the entrepreneurial competence possessed by a good entrepreneur then it is expected that the performance of the company that he leads will be good too. While the measurement indicators on entrepreneurial competence include: (1) Personal

strength competencies; (2) Organizational skill; (3) Leadership; (4) Self-management; (5) Opportunity recognition; (6) Analytical and strategic thinking; (7) Learning for continuous improvement.

### *2.2 Organizational Capability*

Organizational capability is the organizational ability to innovate can maintain the quality of products or services to its stakeholders, effective in costing and also flexibly related to its organizational structure (Sánchez, 2012). In this increasingly global era, innovation is an absolute thing must be owned by the organization. The process of innovation is the implementation of social systems that exist within the organization. In this process the human role is needed as an intangible factor. And this ultimately affects the level of education, competence and employee innovation behaviour. The ability of organizational innovation depends on human capital, knowledge and entrepreneurship where it is owned solely by the company's intangible assets (Szczepańska-Woszczyzna, 2014). This also applies to small businesses or SMEs.

Characteristics of the MSMEs sector is to have a dynamic approach to the environment that must be responsive to changes in customer needs and wants and coupled with the scarce resources it has and this will hamper opportunities to innovate. So that MSMEs at least need good support from financial factor and knowledge (Szczepańska-Woszczyzna, 2014).

Referring to research conducted by (Sánchez, 2012) organizational ability is the ability of the organization to innovate, can maintain the quality of products or services to its stakeholders, effective in cost calculations and also flexible related to the organizational structure. In this research, organizational capacity building refers to (Sánchez, 2012) with construct dimensions, including: innovative capabilities, quality, cost effectiveness, and flexibility.

### *2.3 Competitive Scope*

Today's organizations are faced with a dynamic environment that has the rapid characteristics of technological change, short product life cycle, and globalization. Competitive scope can be measured by taking into account the external environment, such as technological advances, market heterogeneity, business dynamics, market interest, product in industry, product life cycle, environmental generosity, perceived opportunities, market demand, and competitive concentration (Chandler & Hanks, 1994). While (Sánchez, 2012) in his research quotes from Zahra (1993) and Miller (1988) about the competitive scope for measuring the environment is divided into several indicators, among others: technological opportunities, industrial growth, market heterogeneity, perception

of the importance of new products. In this study the measurement of competitive scope refers to (Sánchez, 2012).

#### *2.4 Firm Performance*

Firm Performance as a process of evaluating how well the company managed and delivered the value of the company to customers and other stakeholders (Moullin, 2007). The word "evaluation" is used because it will provide more and broad guidelines for people involved in performance measurement. Where this is followed by (Antony & Bhattacharyya, 2010) on measuring the performance of MSMEs in India.

Human resources within an organization are those who have a role as designers, producers and deliverers of it. Therefore, the purpose of the human resources division is to determine the various activities that have an important contribution in terms of achieving company performance (Mathis & Jackson, 2004). This theory applies to large or small companies.

The firm performance construct refers to research conducted by (Antony & Bhattacharyya, 2010) on measuring the performance of MSMEs in India is defined as a measurement of the extent to which the company can be managed and convey the value adopted by the company to customers and other stakeholders where it is similar with previous research conducted by (Moullin, 2007). The performance measurement indicators of the organization include: innovativeness, creativeness, competitiveness, effectiveness, efficiency, productiveness, profitability.

#### *2.5 Theoretical Framework and Hypothesis*

Based on previous research conducted by (Man, Lau, & Snape, 2008) and (Sánchez, 2012) entrepreneurial competence has positive effect on firm performance. This is also supported by previous research which states that there is a positive correlation between company performance and entrepreneurial competence (Wiklund & Shepherd, 2005). Based on the findings of previous research it can be concluded hypothesis as follows:

*H<sub>1</sub>: There is a positive influence between entrepreneurial competences towards firm performance.*

Entrepreneurship competence in addition to affect the performance of the company also affects the competitive scope and organizational capability (Sánchez, 2012). Entrepreneurial competence is influential in interpreting the conditions of competitive environment in business. This is supported by previous research which states that companies with managers with entrepreneurial competence tend to pay attention and manage the competitive environment of

the business around them to find new opportunities and consolidate their competitive position (Covin & Miles, 1999).

Based on the findings of previous research it can be concluded hypothesis as follows:

*H<sub>2</sub>: There is a positive influence between entrepreneurial competences towards organizational capability.*

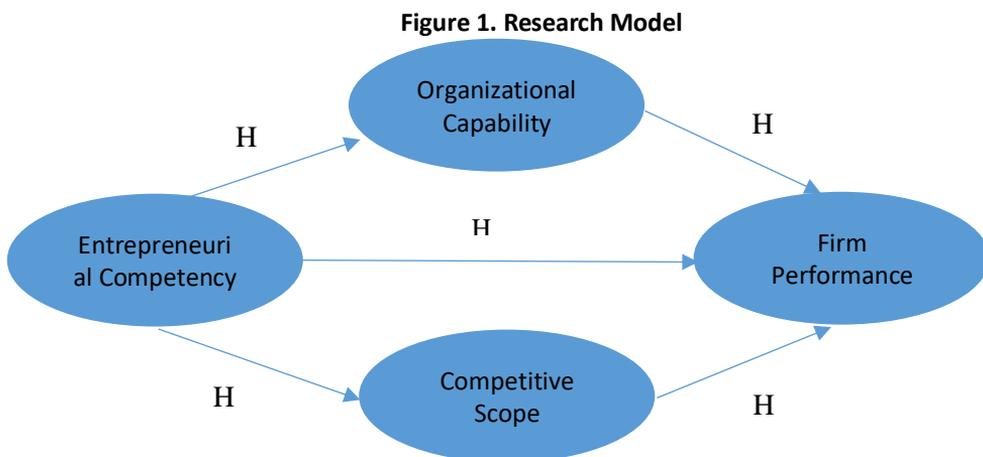
*H<sub>3</sub>: There is a positive influence between entrepreneurial competences towards competitive scope.*

Resources that company managed can be as organizational capability and can develop into a competitive advantage. In other words entrepreneurial competence also has an influence on organizational capability (Sánchez, 2012). Meanwhile, organizational capabilities have an influence on firm performance. This is supported by previous research which states that firm performance is influenced by organizational capabilities, namely the ability to integrate, build, and configure its resources (capabilities) and competence (Zott & Amit, 2006). Competitive scope is the right tool to ensure company performance (Sánchez, 2012). This is supported by previous research which states that companies that have more opportunities to innovate, marketing innovation, and the growth of industry and can collaborate all have high performance (Dollinger, 1992).

Based on the findings of previous research it can be concluded hypothesis as follows:

*H<sub>4</sub>: There is a positive influence between organizational capabilities towards firm performance.*

*H<sub>5</sub>: There is a positive influence between competitive scopes towards firm performance.*



### 3. Research Method

This research uses quantitative approach and survey method in collecting data on MSMEs in Bandung. Sample used is purposive sample with criteria only MSMEs in culinary field only. Questionnaires were given to 40 respondents with an equally large proportion for men and women. The questionnaires using the likert scale with 5 level of statement respondent, (e.g. “strongly disagree” - “strongly agree”). This research aims to test the variable entrepreneurial competence towards firm performance especially for MSMEs in the city of Bandung. This research model is also equipped with moderator variable that are organizational capability and competitive scope.

This research uses data analysis method using SmartPLS version 3.0 software. PLS is an analysis of variance-based structural equation that can simultaneously perform testing of measurement models as well as testing structural models. The measurement model is used for validity and reliability test, while structural model is used for causality test (hypothesis testing with prediction model). Based on the opinion of (Ghozali, 2008) explains that PLS is a soft modelling analysis method because it does not base on the assumption of data must be with measurement scale, distribution free and certain samples which means the number of samples can be small (under 100).

Dimensions used to measure entrepreneurial competence, organizational capability, competitive scope and firm performance adopted from various authors. The dimensions used in entrepreneurial competence variables consist of seven dimensions: personal strength competencies, organizational skills, leadership, self-management, opportunity recognition, analytical and strategic thinking, learning for continuous improvement (Sari, 2014). Variable organizational capability has four dimensions consisting of: innovative ability, quality, cost effectiveness, flexibility (Sánchez, 2012). Just as entrepreneurial competence variables, competitive scopes also adopt from (Sánchez, 2012), technological opportunity, industrial growth, market heterogeneity, perceived importance of new product. Finally for variable firm performance dimensions used are: innovativeness, creativeness, competitiveness, effectiveness, productiveness, efficiency, profitability (Antony & Bhattacharyya, 2010).

## 4. Result

### 4.1 Outer Model Evaluation

At this stage of the evaluation process measured the relationship between latent variables with indicator or manifest. In this firm performance improvement model there are four constructs. Evaluation done at this stage by using the reliability and validity test of the model where it aims to ensure that the constructed reflective model is eligible. In the results of this evaluation we can see the value of the loading factor to determine the correlation between the indicator and its construct. The higher the loading factor value, the better the indicator will be in explaining the latent construct.

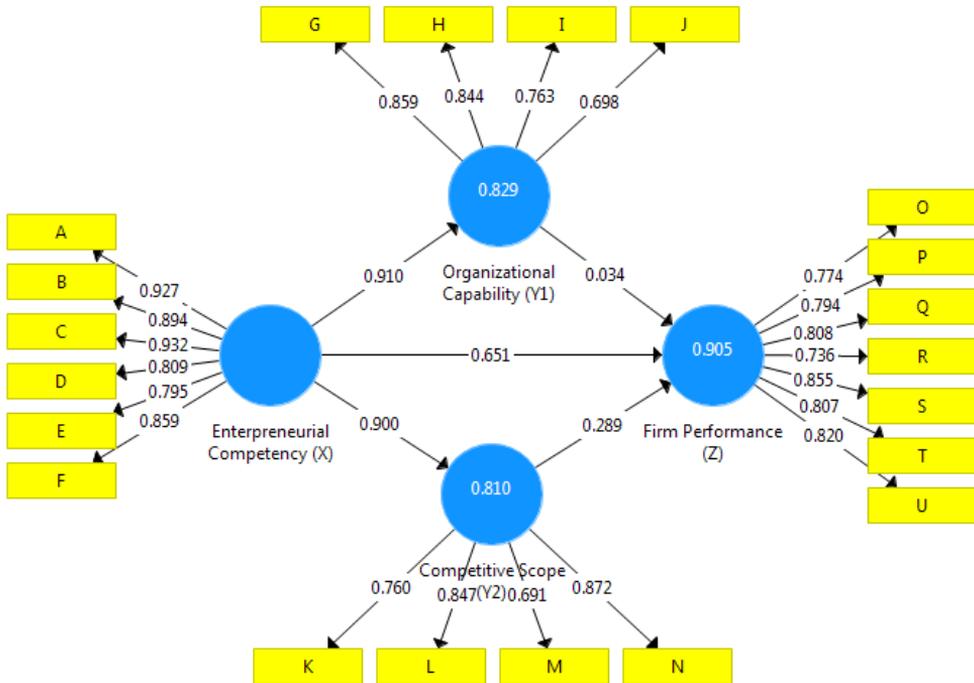
The value of the tolerable loading factor  $> 0.5$ , if less then it will be reduced from the model. In Figure 2 can be seen that each indicator used to measure each latent variable then worth  $> 0.5$  so it can be concluded all these indicators significantly able to reflect each variable that is tested. The average variance extracted (AVE) value for entrepreneurial competence, organizational capability, competitive scope, and firm performance are each valued at 0.759; 0.63; 0.633; and 0.64 met the criteria in the convergence validity test because  $> 0.5$ .

Reliability test in this research can be seen from the value of Composite Reliability. This value indicates the level of conformity of the indicator in forming the latent variable construct. The value of composite reliability for the latent variables of Entrepreneurial Competence (X), Organizational Capability (Y1), Competitive Scope (Y2), and Firm Performance (Z) respectively by 0.949; 0.871; 0.873; and 0.925 on a scale of 0-1. In addition to using composite reliability values, reliability tests are also obtained from cronbach's alpha. In Table 1 the following can be seen that all variables have a value of cronbach's alpha  $> 0.7$  so it meets the criteria. Based on the tests that have been done it can be concluded that all tested variables are valid and reliable.

**Table 1. Construct Reliability and Validity**

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Competitive Scope (Y2)	0.804	0.816	0.873	0.633
Enterpreneurial Competency (X)	0.935	0.941	0.949	0.759
Firm Performance (Z)	0.906	0.908	0.925	0.64
Organizational Capability (Y1)	0.802	0.81	0.871	0.63

Figure 2. Coefficient of Structural Modeling Standardization



4.2 Structural Model

Structural model is a model that connects exogenous latent variables with endogenous latent variables or in other words shows the relationship of endogenous variables with other endogenous variables. In Table 2 and Figure 3 the following briefly summarizes the values used in the structural model and the path diagram of the hypothesis testing of this research.

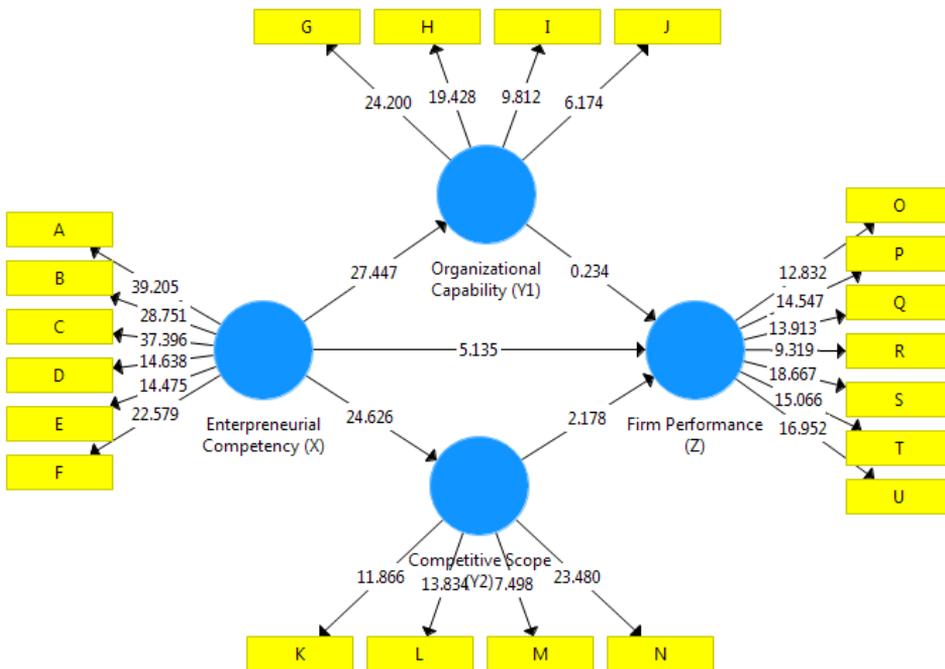
Table 2. Summary of Statistical Test Results

Path	Coeff.	Tvalue	Conclusion	Rsquare
Entrepreneurial competence (X) → Organizational capability (Y <sub>1</sub> )	0.910	27.447	Significant	0.829
Entrepreneurial competence(X) → Competitive scope (Y <sub>2</sub> )	0.900	24.626	Significant	0.810
Organizational capability(Y <sub>1</sub> ) → Firm Performance (Z)	0.034	0.234	Not Significant	0.905

Entrepreneurial competence(X)→ Performance(Z)	Firm	0.651	5.135	Significant
Competitive scope(Y <sub>2</sub> )→ Performance(Z)	Firm	0.289	2.178	Significant

Based on table 2 above, X, Y<sub>1</sub>, and Y<sub>2</sub> together give an effect of 90.5% to Z, while the remaining of 9.5% is the influence of other factors not examined. For the variable X gives the effect of 82.9% to Y<sub>1</sub> while the remaining of 17.1% is the influence of other factors that are not observed. For the variable X gives an effect of 81% to Y<sub>2</sub> while the remaining 19% is the influence of other factors that are not observed.

Figure 3. Hypothesis Testing Path Diagram

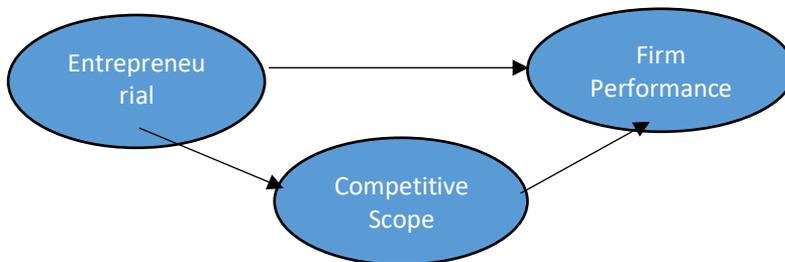


### 4.3 Research Finding Model

Based on the results of research that has been described previously it can be concluded that entrepreneurial competence significantly influence the organizational capability. However, the construct of entrepreneurial competence moderated by the organizational capability does not have a significant effect on the firm performance of the MSMEs. Later it was revealed that entrepreneurial competence had an effect on the competitive scope. And the construct of

entrepreneurial competence that is moderated by competitive scope construct has an effect on firm performance. So the model of firm performance improvement through entrepreneurial competence of food MSMEs in Bandung is as follows:

**Figure 4. Research Finding Model**



## 5. Discussion and Conclusion

### 5.1 Discussion

#### 5.1.1 The Influence of Entrepreneurial Competence Moderated by Organizational Capability to Improve Firm Performance

From the Hypothesis Testing Path Diagram can be seen that entrepreneurial competence (X) gives a significant influence towards organizational capability (Y<sub>1</sub>) with  $t_{\text{value}}$  of 27,447. This can be interpreted that entrepreneurial competence influences in line with the capability of the organization. If the competence of entrepreneurship increases then it will be followed by the improvement of organizational capability. The factors that form entrepreneurial competence such as: personal strength competencies, organizational skills, leadership, self-management, opportunity recognition, analytical and strategic thinking, and learning for continuous improvement will impact the organizational capability to innovate in producing or processing products produced by MSMEs, the quality of products, organizational capability of business cost efficiency and flexibility regarding organizational structure in its business environment.

The results of this research indicate that the majority of respondents (as much as 55%), the level of education is bachelor degree. The majority of respondents have skills and knowledge about business. These skills and knowledge

are the ability to conceptualize business over the next 5 years, creating business plans, looking at business opportunities, strategizing business, managing and directing resources, setting targets and committing to fulfilling them, and good time management. In addition, high education also forms the mindset of respondents, especially in business. In managing the business respondents become more visionary and forward-oriented, so more planned and directed in running the business. This makes the ability of respondent organizations that have higher entrepreneurial skills than respondents whose entrepreneurial competencies are low or nonexistent. So if it is linked between the results of research with previous research conducted by (Xiang, 2009), (Gerli, Gubitta, & Tognazzo, 2011), (Oyeku, Oduyoye, Elemo, Akindoju, & Karimu, 2014) which states that entrepreneurial competence will have a significant effect towards the organizational capability.

However, the organizational capability ( $Y_1$ ) does not give a significant effect to the improvement of firm performance ( $Z$ ) with  $t_{\text{value}} 0.234$ . Based on the results of research that has been done revealed that most respondents are not able to manage the cost of business effectively. This is a common phenomenon happening to MSMEs in Indonesia where financial management is still a constraint even though most of the educational background is bachelor degree but maybe who have knowledge about finance is not much, for example, personal finance is still mixed with their business. Then the flexibility of respondents in organizing the organizational structure to change the external and internal business environment is still quite low. This is due to organizing MSMEs in Indonesia is still very simple where the business owner concurrently various roles in organization managerial for example as a marketer, funding, fund management, producing products and other operational functions. Meanwhile, according to (Szczepańska-Woszczyna, 2014) characteristics of MSMEs sector should have a dynamic approach to the environment where it should respond quickly to changes in customer needs, wants and accompanied by scarcity of resources it has and this will hamper opportunities to innovate.

Analysis of respondent's description of their gross income business revealed that 45% of respondents had gross income below 10 million / year. Thus it can be concluded that although most of the respondents are graduated from higher education has not been able to increase their gross income due to lack of knowledge in managing finances. So that MSMEs at least need the support both from financial factors and knowledge to be able to grow and compete with others.

While the direct influence of entrepreneurial competence ( $X$ ) towards firm performance ( $Z$ ) with  $t_{\text{value}} 5.315$ . Thus, entrepreneurial competence ( $X$ ) does not give influence to firm performance ( $Z$ ) through organizational capability ( $Y_1$ ). It can

be concluded that  $H_1$  and  $H_2$  can be proven whereas  $H_4$  can not be proven in this study.

### *5.1.2 The Influence of Entrepreneurial Competence Moderated by Competitive Scope to Improve Firm Performance*

From the Hypothesis Test Path Diagram can be seen that the entrepreneurial competence (X) gives a significant influence towards competitive scope ( $Y_2$ ) with  $t_{\text{value}}$  of 24,626. It can be interpreted that entrepreneurial competence influences in line with the competitive scope. If entrepreneurial competence increases then it will be followed by an increase in the competitive scope. So that the factors that form entrepreneurial competence such as: personal strength competencies, organizational skills, leadership, self-management, opportunity recognition, analytical and strategic thinking, and learning for continuous improvement will have an impact on the competitive scope of MSMEs to seek technological opportunities in supporting their business, growing in the industry, having a heterogeneous market segment, able to observe/see the importance of updating the resulting product.

The results of the analysis of respondent's description in this research revealed that as many as 72.5% of respondents are in the age range between 20-30 years old. Respondents in this age range are more adaptive and quick respond to the technological opportunities that can support business processes or product promotion. Along with the development of product marketing technology is growing and shifting towards social media like facebook, Instagram, website and so on. It emphasizes that the factors of creativity, entrepreneurship and innovation are the absolute "thing" of the organization.

Based on the results of testing the hypothesis of competitive scope ( $Y_2$ ) gives a significant influence towards the improvement of firm performance (Z) with  $t_{\text{value}}$  2.178, while the direct influence of entrepreneurial competence (X) towards firm performance (Z) with  $t_{\text{value}}$  5.315. Thus, the entrepreneurial competence (X) gives influence to firm performance (Z) through competitive scope ( $Y_2$ ). So it can be concluded that  $H_3$  and  $H_5$  can be proven in this research.

### *5.2 Conclusion*

The conclusions of this research are: 1). Entrepreneurial competence significantly influences organizational capability. However, the construct of entrepreneurial competence moderated by the organizational capability does not have a significant effect on the firm performance (MSMEs). 2). Entrepreneurial competence influences the competitive scope. And entrepreneurial competence

variables that are moderated by competitive scope variables affect the firm performance. 3).The entrepreneurial competence model has significant influence on the firm performance only if it is moderated by the competitive scope alone.

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