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Antecedents and Consequences of Organizational Innovation: Study on Small and Medium Enterprises in the Consumer Goods Industry

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ABSTRACT
Small and medium-sized enterprises (SMEs) play a very important role in the economic development and growth of a country. SMEs have great potential in business but face many challenges in innovation implementation. This research aims to examine the level of industrial competition, organizational innovation, and company performance in SMEs and to analyze the influence of industrial competition and organizational innovation on company performance. This is a descriptive and verification study with explanatory surveys. Small and medium scale enterprises in West Bandung Regency were examined with purposive sampling technique and the sample size was 31 SMEs. Hypothesis testing was conducted through variant-based structural equation models and processed by the Partial Least Square (PLS) program. The results show that the level of industrial competition faced by SMEs is high, the level of implementation of organizational innovation is good, and the level of company performance achievement is also good. Furthermore, industrial competition has a positive influence on organizational innovation while organizational innovation has a positive effect on company performance so that industrial competition affects company performance through organizational innovation. In this research, organizational innovation is discovered as an intervening variable between industrial competition and company performance; this has not been discussed in previous studies.

Keywords: *Industry competition, Organizational innovation, Company performance, SMEs, Small and medium-sized enterprises.*

1. INTRODUCTION

Small and medium-sized enterprises (SMEs) play a significant role in economic development and growth. In developing countries, SMEs are very important not only in labor absorption but also in gross domestic product (GDP) growth [1]. According to Chittithaworn *et al.*, SMEs have advantages in technology innovation that can ease product development and strengthen family relationships due to their quick adaptation ability towards changing market conditions compared to large scale companies and their dynamic managerial as well as entrepreneurial roles [2].

Innovation is the most basic thing to be considered as an important aspect of success to compete in the market [3]. Organizational innovation is regarded as a foundation of competitive advantage sustainability [4]. Besides, the innovation is truly linked with entire managerial efforts to improve organizational practices, procedures, mechanisms, systems, etc., and in promoting collaboration, information sharing, coherency, cooperation, improving awareness, and innovation [5]. Furthermore, innovation is often viewed as a growth catalyst in the economy and business. By implementing innovation strategies, SMEs can achieve success and business sustainability. Product innovation is crucial to maintain market share, process innovation is vital in maintaining competitive price levels, and managerial innovation is important for maintaining a flexible and durable organization. However, not every innovation has a positive effect on company performance. In addition, although innovation is important, it is not sufficient to increase profitability [3].

In the SME consumer goods industry, some companies implement innovation on their products so that they are in demand by foreign markets. Besides, they conduct marketing innovations through digital marketing to reach the online market. However, some problems occur in SMEs in the consumer goods industry, such as

the problems of human resource wages and raw materials. In other words, it indicates a problem with the process and product innovation. SMEs are engaged in various business fields, such as snacks, processed products, handicrafts, and others. Most of them are still constrained by limited marketing so that it is difficult to develop. Therefore, modern markets are a good way to introduce SMEs products.

Based on those indications, this research aims to examine the level of industrial competition, organizational innovation, and company performance in SMEs. Besides, it studies the influences of industrial competition on organizational innovation, organizational innovation on company performance, and industrial competition on company performance.

2. LITERATURE REVIEW

Researches about innovation in small and medium-sized enterprises (SMEs) have been widely conducted. Marketing innovation research in manufacturing and service companies was carried out by Molina-Castillo *et al.* [6]. Nieves and Diaz-Meneses worked on a marketing innovation study in the hotel industry [7]. O'Dwyer *et al.* evaluated marketing innovation in SMEs [8]. Research on product innovation in manufacturing companies in Turkey was carried out by Aydin [9]. Other research in SMEs was conducted by Ko *et al.* and Wahyono [10], [11]. Widya Hastuti *et al.*[12] analyzed process innovation in SMEs [12]. Administrative innovation research has been done out by Cho *et al.* [13]. Research on administrative innovation has also been carried out by Moreno *et al.* [14]. This study discusses Porter's five triggers of industrial competition which are the causes of organizational innovation [15].

2.1 Industrial Competition

Industrial competition occurs between two or more companies in one industry that produce the same or similar products. The level of intense industrial competition is determined by the number of competitors in the industry, customer loyalty, product differentiation, and prices. The industrial competition also occurs on costs, dependence on resources, and the application of technology by companies in the industry.

According to Porter, the trigger factors in the industrial competition are (1) competition between companies in the industry today, (2) the presence of newcomer companies, (3) competition from substituted goods companies, (4) bargaining power of suppliers, and (5) bargaining power of buyers [15]. Thus, a large number of competitors, new entrants, and substitute goods encourage companies to increase their competitive ability.

2.2 Organizational Innovation

Bashir and Long classify innovation into two types; management innovation and technology innovation [16]. Francis and Lublin show various organizational innovations including product innovation, organization innovation, technology innovation, and service innovation; the real innovation ability can merely be presented by the comprehensive considerations [17]. Meanwhile, Damanpour and Gopalakrishnan state that innovation is the implementation of behavior or idea, which could be in the forms of a system, policy, program, device, process, product, or service that is new to the adopting organization [18].

According to Wang *et al*, product innovation refers to the perception of newness/novelty/originality or the uniqueness of the product [19]. In addition, kinds of innovation include marketing innovation, process innovation, behavioral innovation, and strategic innovation.

The administrative innovation dimension refers to the novelty of the management system, embracing and introducing new management systems. Organizational innovation can be measured through product innovation, process innovation, marketing innovation, service innovation, and administrative innovation [20].

2.3 Organization Performance

Organizational performance can indicate how well an organization achieves its goals and results in several precise targets such as market share proportion, sales volume, employee motivation, customer satisfaction, and performance quality. The organization will be successful if it accomplishes its objectives (effectiveness) by using minimal resources (efficiency). Thus, the organizational theory supports the idea of an organization that can achieve performance goals using limited resources. In this context, profit becomes one of many performance indicators [21].

One of the company performance measurements that can be used is the Balanced Scorecard (BSC) introduced by Kaplan *et al.* [22]. BSC measures company performance through four perspectives; finance, customers, business processes, and human resources. Good financial performance is a reflection of good service to consumers, effective internal processes, and good human resource performance [23].

2.4 Industrial Competition, Innovation, and Company Performance

Innovation and performance improvement are usually discussed in previous studies regarding SMEs. Bigger flexibility allows small companies to be more innovative and take a greater role because they are in a good position

to react to changes occurred in the market and have shorter and quicker decision processes. By dominating a market niche through innovation efficiency, SMEs can achieve a competitive advantage [24]. The enterprises have a better capability for customization and can adapt faster and learn to new tasks and strategies in improving company performance.

According to Gupta *et al.* [25], competition can be both a trigger and a consequence of innovation. Figure 1 shows the research paradigm.

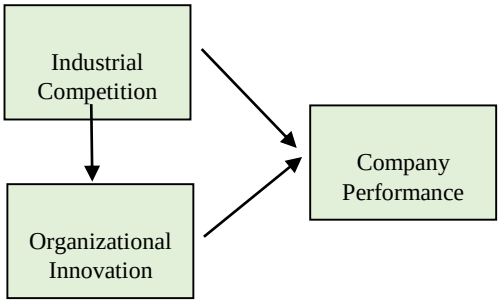

Figure 1 Relationship between Industrial Competition, Innovation, and Company Performance

Hypothesis:

1. Industrial competition positively influences organizational innovation.
2. Industrial competition and organizational innovation positively influence company performance.

3. METHODOLOGY

This research was conducted to analyze the influence of industrial competition on organizational innovation and its impact on company performance. Thus, the type of this research was verification/explanation. This study used the explanatory survey method to reveal the clarity of the relationship between the research variables. The data were collected in a certain period of time from small and medium-sized enterprises in the consumer goods industry in West Bandung Regency. The owners of the companies became the respondents/key informants.

The purposive sampling technique was employed, resulted in 31 SMEs which produced consumer goods and have operated for at least 2 years. The 31 respondents were the representative from 16 districts in West Bandung Regency.

A questionnaire through a personal interview was used for data collection. The questionnaire consisted of 11 questions of industrial competition variable, 27 questions of organizational innovation, and 12 questions of company performance. Descriptive analysis was assigned to find out the level of SMEs' industrial competition, organizational innovation, and company performance. Moreover, inferential analysis using variant-based structural equation models (Partial Least Square statistical technique) was employed to analyze the influence of the variables.

3.1 Partial Least Square Model Analysis

Before analyzing the data further, a model evaluation was carried out. PLS model evaluation was performed by examining the inner and outer models. The outer model was evaluated to assess the validity and reliability of the construct.

3.1.1 Validity Test Result

Construct validity shows how good the results obtained from the measurement, in accordance with the theories employed to describe a construct. It consists of discriminant validity and convergent validity [26].

Convergent validity associates with the principle that the gauges of a construct should be strongly correlated. The convergent validity test using PLS was assessed based on the correlation between the item score and the construct score. A score $\geqslant$ 0.30 is regarded to achieve the minimum standard, $\geqslant$ 0.40 is considered better, and > 0.50 is considered practically significant. Meanwhile, the rule for convergent validity is outer loading > 0.7; communality > 0.5, and average variance extracted (AVE) > 0.5 [26].

The discriminant validity test is based on cross-measurement with the construct. It is to compare the AVE roots for every construct with the connection between the constructs and the other constructs in the model. The model has enough discriminant validity if the AVE root for every construct is bigger than the correlation between the construct and the other constructs in the model. Table 1 presents the validity test in PLS.

Table 1. Validity Test Parameters in PLS Measurement Model

Validity Test	Parameters	*Rule of Thumbs*
Convergent	Loading Factor	> 0,7
	Average variance extracted (AVE)	> 0,5
	Communality	> 0,5
Discriminant	AVE Root and Latent Variable Correlation	AVE root > Latent Variable Correlation
	Cross loading	> 0,7 in one variable

3.1.2 Reliability Test Result

There are two approaches to conduct reliability test in PLS; Cronbach's alpha and composite reliability. Cronbach's alpha examines the lower limit of the reliability value of a construct while Composite reliability evaluates the real value of the reliability of a construct. However, composite reliability is regarded better in assessing the internal consistency of a construct [26]. Rule of thumb, the alpha value or Composite reliability must be greater than 0.7 although the value of 0.6 is still acceptable [27].

Table 2 shows Cronbach's alpha value and the Composite reliability value. Composite reliability values for organizational innovation, company performance, and industrial competition are greater than 0.7, meaning that the constructs are reliable.

Table 2. AVE Value, Cronbach's Alpha, and Composite Reliability

	Cron-bach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Organization Innovation	0,847	0,861	0,907	0,766
Performance	0,863	0,869	0,916	0,785
Competition	0,851	0,867	0,910	0,772

4. RESULTS AND DISCUSSION

The description below presents the assessment results of industrial competition, organizational innovation, and companies' performance of consumer goods industries.

4.1 Industrial Competition Condition

Industrial competition faced by companies in the consumer goods industry is revealed through the industry's assessment of statements that cover 5 (five) dimensions, namely industry competitors, substituted goods competitors, new competitors, bargaining power of suppliers, and bargaining power of buyers. The results are shown in Table 3.

Table 3. Industry Perception towards Industry Competition

Dimensions	Mean
Industry competitor condition	3,9
Competitor for substituted goods condition	3,6
New competitor condition	3,7
Supplier bargaining power	3,2
Buyer bargaining power	3,3

Table 3 shows the conditions of industrial competition in the consumer goods industry, which are explained as follows:

1. The competition condition among existing competitors is high because of the large number of competitors, high level of differentiation, and high level of customer loyalty.
2. The competition condition regarding substituted goods is high because of the large number of substituted goods that allows consumers to freely choose products of industrial competitors or substituted goods competitors.
3. The competition condition with new competitors is high because many of them enter the industry without any obstacles.
4. Regarding the supplier aspects, the competition condition is low due to a large number of suppliers. The market structure is a monopolistic competitive market. Unique services of suppliers allow SMEs to find suppliers easily.
5. Price sensitivity occurs so that the level of competition faced is low. The market structure is a monopolistic competitive market characterized by a large number of buyers and a wide range of product differentiation.

4.2 Organizational Innovation

Organizational innovation in the consumer goods industry is revealed through the respondents' assessment of 4 (four) dimensions, namely product innovation, process innovation, administrative innovation, and marketing innovation. The results are presented in Table 4.

Table 4. Industry Perception towards Organizational Innovation

Dimensions	Mean
Product Innovation	3,9
Process Innovation	3,3
Administrative Innovation	3,6
Marketing Innovation	3,7

Table 4 shows that the level of product innovation in consumer goods industry companies is in good condition especially in several aspects, they are the authenticity of product designs, original designs of patterns/colors, and the authenticity of packaging designs. This happens because the SMEs have a high awareness that the authenticity of products will generate demand and loyalty from customers.

The uniqueness of product design in the form of products' pattern/color in consumer goods industry companies is also good. The companies create their own uniqueness, for example in determining the use or formula of raw materials (in the food industry) and in determining the model, style, and color of the product (in the fashion industry).

The process innovation in consumer goods industry companies is generally in a sufficient condition. This illustrates that the SMEs have replaced the existing equipment with newer and more sophisticated ones, and already have equipment that can minimize the use of raw materials.

The administrative innovation in consumer goods industry companies is also in good condition. It can be seen in their activities of making efforts to find errors in all units, for example in non-standard and inefficient production processes, and to follow up by giving improvements and responding to customers' complaints.

Last, the marketing innovation in consumer goods industry companies is in good condition. The companies have attempted to market their products to various regions with different segments. Unfortunately, they have not implemented the promotion mix properly and have not utilized marketing distribution channels optimally.

4.3 Company Performance

The performance of companies in the consumer goods industry is revealed through four performance indicators by Balance Scorecard, namely financial, customer, internal business processes, and human capital perspectives. The results are represented in Table 5.

Table 5. Industry Perception towards Company Performance

Dimensions	Average
Financial Perspective	3,9
Costumer Perspective	3,3
Internal Business Process Perspective	3,6
Human Capital Perspective	3,7

Table 5 shows that the company performance from a financial perspective is in good condition. It can be seen from the increase in profit from the last 5 years, the increase in sales volume in the last 5 years, and investment in office equipment.

From the customer's perspective, the company's performance is seen to be relatively good. It is indicated by a good level of customer satisfaction, the percentage of additional purchases by main customers, and an increasing number of new customers. Only the number of events/exhibitions is sufficient.

From the internal business perspective, the company's performance is seen to be in good condition. It is indicated by the percentage of production that can be fulfilled according to schedule. However, the number of equipment damage and the rate of defective/damaged products is still high.

Last, from the perspective of human capital, the company's performance is also seen to be in good condition. It is indicated by the very low number of employee turnover in the last 5 years which shows a high level of job satisfaction. In addition, to improve their skills, regular training is provided for employees both internally and externally.

4.4 Structural Model (Inner Model)

The structural model was measured using PLS by evaluating the R2 for dependent constructs. Then, path coefficient values or t-values of every path were evaluated to test the significance between constructs in the structural model. The path coefficient value or inner model presents the level of significance in testing the hypotheses. The path coefficient score or inner model indicated by the T-statistic value must be above 1.96 for the two-tailed hypothesis and above 1.64 for the one-tailed hypothesis (hypothesis testing at alpha 5% and 80% power) [28]. Table 6 describes the path coefficient value or inner model which shows the level of significance in hypothesis testing.

Table 6. Path Coefficient Value: Mean, Standard Deviation, T-Value, and P-Value

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Organization_Innovation -> Performance	0,653	0,628	0,163	4,019	0,000
Competition -> Organization_Innovation	0,685	0,698	0,086	7,986	0,000
Competition -> Performance	0,242	0,257	0,177	1,365	0,172

Table 6 is used to measure the support of the hypothesis. This measure can be used to compare the value of T-statistics and T-table. If the value of T-statistics is higher than T-table, it means that the hypothesis is supported. For the 95% confidence level (Alpha 5%), the T-table value for the one-tailed hypothesis is ≥ 1.66. From this table, it can be concluded that:

1. Organizational innovation has a positive effect on company performance, as indicated by the T-statistics value of 4.019; with a path coefficient of 0.653.
2. Industrial competition has a positive effect on organizational innovation, as indicated by the T-statistics value of 7,986; with a path coefficient of 0.685.
3. Industrial competition does not have a positive effect on company performance, as indicated by the T-statistics value of 1.365.

Figure 2 presents a complete path diagram of the influence model of industrial competition on organizational innovation and its impact on company performance using the PLS method.

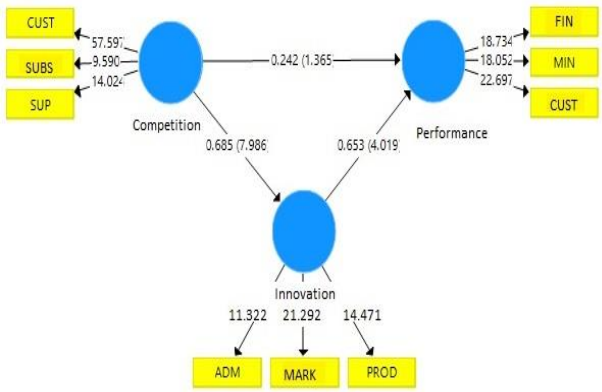

Figure 2 Model path diagram of the influence of industrial competition on organizational innovation and its impact on company performance

4.5 The Effect of Industrial Competition on Organizational Innovation

Based on SEM results, industrial competition has a positive effect on organizational innovation in Small and Medium Enterprises. This finding shows that if the industrial competition is getting tighter, the level of organizational innovation implementation will be better. A large number of industrial competitors, a high level of product differentiation, and a high level of customer loyalty from competitors in the industry are the causes of the increasingly fierce level of competition. SMEs that face fierce industrial competition will apply product innovation, process innovation, marketing innovation, and administrative innovation properly.

4.6 The Effect of Industrial Competition on Company Performance through Organizational Innovation

Industrial competition has no direct effect on company performance, but competitive conditions will affect company performance through organizational innovation. This finding indicates that competition causes organizational innovation in SMEs which then increases company performance.

Organizational innovation has a positive effect on company performance in Small and Medium Enterprises. This result shows that if the level of organizational innovation carried out by SMEs is higher, the company's performance will be better. Implementing product innovation from the side of uniqueness, novelty, authenticity; applying process innovations by using better machines and equipment; implementing marketing innovations by expanding the reach of the marketing area; and implementing administrative innovation will increase company performance through the level of profitability, sales turnover, satisfaction and customer loyalty, better internal business processes, and better human resource performance.

This finding is supported by previous studies which state that the most fundamental determinant of company

performance is implementing organizational innovation properly. Research that discusses the positive influence of organizational innovation on company performance has been conducted by several researchers [29]–[31].

5. CONCLUSION

In the small and medium-sized consumer goods industries, it happens that if the industrial competition is getting tighter, the numbers of competitors, new entrants, and substituted goods are getting bigger, the customer and supplier bargaining powers are getting weaker, then the organizational innovation is getting higher. Increasingly fierce industrial competition will improve company performance through a high level of organizational innovation. Increased company performance is obtained through increased profitability, sales turnover, and customer satisfaction as well as loyalty; better internal business processes, and better human resource performance.

Future research can investigate other possible variables that might affect company performance. In addition, a probability sampling method can be assigned to generalize the result.

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