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The Effect of Intellectual Capital on MSME Performance Through Innovation as an Intervening Variable

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ABSTRAK

Usaha Mikro, Kecil, dan Menengah (UMKM) memegang peranan penting dalam perekonomian Indonesia. Penelitian ini bertujuan untuk mengeksplorasi pengaruh modal intelektual terhadap kinerja UMKM melalui inovasi. Dengan menggunakan metode purposive sampling, kuesioner disebarkan kepada 98 pemilik UMKM di Indonesia. Analisis data dilakukan menggunakan Structural Equation Modeling (SEM) *dengan aplikasi SMART PLS. Hasil analisis SEM menunjukkan bahwa modal intelektual berpengaruh positif terhadap inovasi (t-statistik = 120,105) dan kinerja UMKM (t-statistik = 18,863). Selain itu, inovasi juga berpengaruh positif terhadap kinerja UMKM (t-statistik = 12,010). Temuan ini menegaskan bahwa peningkatan kinerja UMKM memerlukan modal intelektual yang kuat dan didukung oleh inovasi yang efektif. Dengan demikian, peningkatan inovasi dapat menjadi kunci dalam meningkatkan kinerja UMKM. Penelitian ini memberikan kontribusi penting dalam pemahaman tentang hubungan antara modal intelektual, inovasi, dan kinerja UMKM. Implikasi dari temuan ini dapat membantu pemilik UMKM dan pemangku kepentingan terkait untuk meningkatkan strategi pengelolaan modal intelektual dan inovasi guna meningkatkan kinerja UMKM di Indonesia.*

ABSTRACT

Micro, Small and Medium Enterprises (MSMEs) play an important role in the Indonesian economy. This study aims to explore the influence of intellectual capital on MSME performance through innovation. Using the purposive sampling method, questionnaires were distributed to 98 MSME owners in Indonesia. Data analysis was performed using Structural Equation Modeling (SEM) with the SMART PLS application. The results of SEM analysis show that intellectual capital has a positive effect on innovation (t-statistics = 120,105) and MSME performance (t-statistics = 18,863). In addition, innovation also has a positive effect on the performance of MSMEs (t-statistics = 12,010). This finding confirms that improving the performance of MSMEs requires strong intellectual capital and is supported by effective innovation. Thus, increasing innovation can be key in improving the performance of MSMEs. This research makes an important contribution in the understanding of the relationship between intellectual capital, innovation, and MSME performance. The implications of these findings can help MSME owners and related stakeholders to improve intellectual capital management strategies and innovations to improve the performance of MSMEs in Indonesia.

1. INTRODUCTION

Along with the rapid development of the economy, it creates increasingly fierce competition among business actors (Ariyani et al., 2021; Faizah, 2019; Feyen et al., 2021; Grant, 2017; Gunawan et al., 2023; Rahayu & Hidayah, 2023; Wu, 2020). Knowledge-based Human Resources (Knowledge-based resources) include tactics for competing, which are indicators of success when competing with fellow companies (Indriastuti & Kartika, 2021; Martínez-Sánchez et al., 2020). A company can be superior if it has added value compared to its competitors (Islami et al., 2020; Weinstein, 2020). Good intellectual capital will indicate added value for a business entity (Dewi et al., 2020; Sunarsih & Dewi, 2019). Intellectual capital is said to

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be good if the company can develop the ability to motivate its employees to be able to innovate and increase their productivity, as well as having a system and structure that can assist the company in maintaining and even increasing its profitability and existence (Abdulaali, 2018; Igielski, 2018; Indriastuti & Kartika, 2021; Rajapathirana & Hui, 2018; Yousef Obeidat et al., 2017). Intellectual capital is a vital asset in an economy built on knowledge. Knowledge related to employees and information about the organization are the three components that usually form intellectual capital (Hatane et al., 2022; Li et al., 2019; Mukaro et al., 2023; Pulungan & Koto, 2017; Soewarno & Tjahjadi, 2020). Improved financial performance is one of the benefits derived from investing in intellectual capital, which also generates a competitive advantage. Determines the overall health of a company based on its financial performance in the market. Intellectual capital is an intangible potential that can make an impression on the achievements of micro and small companies (Absah et al., 2018; Beltramino et al., 2020; Gallardo-Vázquez et al., 2019; Muda et al., 2020; Natsir & Bangun, 2021; Sunarto & Fanani, 2020).

The state prioritizes the growth of Micro, Small and Medium Enterprises (MSMEs) in Indonesia during national economic development (Broto Legowo et al., 2021; Nursini, 2020). This is because the MSME sector is one of the pillars of economic growth, which aims to reduce inequality between social groups and alleviate poverty and employment problems. However, its development will broaden the monetary base and significantly contribute to accelerating structural changes, such as strengthening regional and national economic resilience. The role of MSMEs in the Indonesian economy is reflected in the population as the most significant economic actor and in employment, the formation of the Gross Domestic Product (GDP), the value of exports and their contribution to capital or investment (Broto Legowo et al., 2021; Nursini, 2020).

Micro, Small and Medium Enterprises are organizations with valuable properties owned by people or business elements regulated in Law No. 20 2008 concerning MSMEs. According to Iqbal, in short, MSMEs are businesses run by companies or entities that have met the criteria for micro-enterprises (Iqbal, 2022; Mulachela, 2021). One of the pillars of the economy is MSMEs. Micro, Small and Medium Enterprises are one of the efforts to improve the country's economy, whose contribution is already visible. According to Mulachela, Micro, small and medium enterprises (MSMEs) are one of the popular business practices in the community (Iqbal, 2022; Mulachela, 2021). With few MSME business actors, this business sector has become one of the drivers of the Indonesian economy. MSMEs are businesses managed by individuals, households or small business entities. This classification is grouped based on the amount of turnover, the number of employees employed, and the amount of wealth or assets. One of the obstacles SMEs face is the lack of understanding and not making good use of intellectual capital. Besides that, SMEs also have not paid attention to human capital, customer capital, and capital structure. In that case, it is an element of developing MSME intellectual capital. If the MSME refers to knowledge-based management, the MSME can compete with the competitive advantages obtained by the invasion generated by the intellectual capital owned by the MSME. Managing small and medium enterprises requires management skills different from working with already complex companies. Financial performance is an indicator that can show the efficiency of an organization in achieving company goals. The company is successful if it has met its previous targets. So financial performance is critical for every company in fighting business competition. According to Atmoko et al., economic performance is the level of success achieved either in terms of quantity or quality of achievement that has been targeted. Financial performance for MSMEs is a subjective measurement tool that embodies the use of assets in the continuity of the income cycle (Atmoko et al., 2022; Trumpp & Guenther, 2017).

Performance is a crucial thing that every business organization must own because performance represents a business entity's capability to manage and provide resources (Abubakar et al., 2019; Mikalef et al., 2019). In addition, the organization's main target is to meet predetermined behavioral benchmarks to meet the desired results and actions. Behavioral barometers can be manifested as formal plans or management policies outlined in budgets. According to Milena Ariyati et al., Financial performance measurement is essential for a company to compete. Financial performance analysis is a series of details related to reviewing data, calculating, measuring, providing and interpreting financial solutions for business entities within a certain period. Return On Assets is the capability of a business entity to gain profits by implementing its resources (Mahardini, 2019; Milenia Ariyati et al., 2022).

Innovation is also needed to improve employee performance, apart from intellectual capital. Innovation is considered one of the economy's main drivers (Maradana et al., 2017; Marsiglio & Tolotti, 2018). Innovation affects employment, trade openness, economic development, global competition, financial systematics, quality of life, and infrastructure improvement. In this case, MSMEs should constantly innovate to improve employee performance, which is further essential for increasing MSME profits and economic growth.

The aim of this research is to investigate the relationship between intellectual capital, innovation,

and the performance of Micro, Small, and Medium Enterprises (MSMEs) in Indonesia. In the context of increasingly fierce business competition, this research aims to understand how intellectual capital and innovation can influence the performance of MSMEs. It is hoped that this research will provide a deeper understanding of how intellectual capital management and innovation can help MSMEs improve their performance. It is hoped that the results of this research will provide valuable insight for MSMEs business owners, related stakeholders, and the government in developing effective strategies to improve the competitiveness and performance of MSMEs in Indonesia.

2. METHODS

This research is a type of quantitative research. Quantitative study is research based on the philosophy of positivism, which is used to study specific populations or samples. The people in this study are SMEs in Indonesia. The model in this study was 98 MSME respondents using a purposive sampling technique. This study uses primary data types. Questionnaires were given to MSME owners. The data analysis technique in this study is the SEM calculation using the SMART PLS application. The variables used are intellectual capital as the independent variable, employee performance as the dependent variable, and innovation as the intervening variable.

3. RESULTS AND DISCUSSIONS

Results

Measurement Model Analysis

This measurement model analysis aims to determine which research indicators can be used as a measuring tool according to the latent results that are reliable and valid. After that, the model is calculated based on the existing PLS algorithm in the SmartPls program. The following criteria are used to form an opinion about the model:

Loading Factor Question Items Against Dependent Variables

The loading factor is a composite indicator and estimated factor value. When the loading factor produces a value of 1 or is very close to 1, the weighted value is considered much stronger than the standard, which ranges between 0 and 1. This evaluation is also known as a discriminant validity test related to several construct measurement principles, where basically what is not the same will not correlate. The concurrent validity test is calculated based on the value of the loading factor or outer loading. Where is a valid indicator if the external loading value is > 0.5. Thus, the results in Table 4.5 for all variables state that all items have a value of > 0.5, meaning that all indicators are valid or feasible in preparing first order and second order in the SEM model construct.

Determination Test (R square)

Calculation of "R square" is used to determine the extent of the independent variables, in the form of brand marketing and viral marketing on purchase decisions, as well as mediation of Consumer trust. The percentage of the dependent variable that the independent variables can represent is determined through this test. The value of 0 for R2 indicates that there is no effect of the independent variable on the dependent variable; consequently, none of the variables examined managed to translate a variety of dependent variables. However, suppose the value of R2 is 1. In that case, this indicates that the influence exerted by the independent variable on the dependent variable is perfect, meaning that the independent variable can translate 100% (fully) of the variation in the dependent variable. If the value of R2 is less than 1, this indicates that the independent variable cannot translate 100% (fully) of the variation in the dependent variable. The statistical output above shows that the magnitude of R Square on MSME performance is 0.923, meaning that 92.3% of MSME performance can be explained by intellectual capital and innovation. The innovation model has an R2 value of 0.904, indicating the intellectual capital indicator can explain 90.4% of the innovation variable.

Composite Reliability, Cronbach Alpha, Average Variance Extracted

The outer model can also be measured based on the results of the construct reliability or the composite reliability value, which is the choice for the Cronbach Alpha test to determine convergent validity in the reflective model. The variation in the combined reliability value itself is around 0–1. The deal was 0.6–0.7 in an exploratory study with confirmatory research. Meanwhile, the composite reliability value > 0.9 indicates a small error. In addition, there is also an AVE test, which is known based on convergent value and convergent validity. The results of the AVE test itself will explain each latent factor in the model, and it

can be stated to be vital if the AVE is > 0.5 and the AVE value is required > the cross-loading correlation value. If the magnitude of AVE < 0.5 means it has a high error rate. The Cronbach Alpha test can explain convergent validity, with Cronbach Alpha criteria > 0.8 included in a reasonable scale, and> 0.7 means that it is included in the scale that has been accepted. More significant than 0.6 is included in a low estimate scale. Discriminant validity is a way to compare the AVE value of each part with the correlation of other constructs in a model. If the AVE value > the correlation of all other constructs, it means that there is good discriminant validity. It is recommended for the magnitude of the measuring value > 0.5. As per the table above, all construct variables yield values > 0.5, meaning that all indicators in the construct are valid or in accordance with the discriminant and convergent validity requirements in establishing SEM modeling. Composite reliability is part of an indicator that calculates variables with good composite reliability if the value is ≥ 0.7. As for testing the reliability of the mixed, evaluation can be carried out through two types of measurements, namely Cronbach's Alpha and internal consistency. Refers to the results of the table above, the magnitude of the composite reliability of all constructs, namely > 0.7, is in perfect criteria. This means that all the variables in constructing the construct model are reliable. Meanwhile, the Cronbach Alpha test results on all constructs yielded > 0.8, which means that all constructs are by the reliability test requirements with Cronbach Alpha.

Test the Hypothesis with the Bootstrapping Method

The bootstrap procedure calculates the correlation between the latent variable values that have been generated, described through the correlation coefficient, R2 path analysis, and the significant impact of the variable. As for the emphasis on variance based in PLS, it changes the form of research from causality testing to predictive components.

Path Coefficient Hypothesis Test

Hypothesis testing is calculated in line with the pattern test to select whether a hypothesis is accepted or rejected based on construct significance, p-value, and t-test. The value of the t statistic used is > 1.96, and the magnitude of force is 0.05. The following are the results of the research hypothesis test: The consistency of the model used in the population is known based on the magnitude of the correlation between variables or by using the importance of the rho (path) coefficient by understanding the value of O (original statistic) and the t statistic, which states the magnitude of the significance of the relationship of a variable.

Hypothesis Test Results

The Effect of Innovation on MSME Performance

With a significant level (α) < 5% = 0.05 and the results of Structural Equation Modeling (SEM) calculations, the value of t-statistic = 12.010 is obtained with probability-statistic = 0.000. Thus, the H1 hypothesis, which proves that innovation has a significant positive effect on MSME performance, is significantly acceptable.

The Influence of Intellectual Capital on Innovation

With a significant level (α) < 5% = 0.05 and the results of Structural Equation Modeling (SEM) calculations, the t-statistic value = 120.105 with probability-statistic = 0.000. Thus, hypothesis H2, which states that intellectual capital has a significant positive effect on innovation, is significantly acceptable.

The Effect of Intellectual Capital on MSME Performance

With a significant level (α) < 5% = 0.05 and the results of Structural Equation Modeling (SEM) calculations, the t-statistic value = 18.863 with a probability-statistic = 0.000. Thus, hypothesis H3, which states that intellectual capital significantly affects MSME performance, is quite acceptable.

The Effect of Intellectual Capital on MSME Performance through Innovation

With a significant level (α) < 5% = 0.05 and the results of Structural Equation Modeling (SEM) calculations, the t-statistic value = 11.582 is obtained with a probability-statistic = 0.000. Thus, the H4 hypothesis, which states intellectual capital's vibrant and significant influence on the performance of MSMEs through innovation, can be accepted.

Discussion

Innovation Affects MSME Performance

The results are supported by previous study, which proved that the innovation variable significantly affects the performance of MSMEs (Hadi & Purwati, 2020; Wardana et al., 2022). Besides that,

other research views state that innovation is one of the Keys to Organizational Success in Competition (Chow, 2017; Ghosh, 2015; Johannessen & Skaalsvik, 2015). Inventions carried out by business managers can control fluctuations in business performance. The better entrepreneurs create innovation, the more the business performance will increase (Ayu & Suryaningrum, 2019; Ludiya & Mulyana, 2020). It can be concluded that MSMEs need to continue to innovate to improve their performance so that they have a positive influence on performance. The better the innovation provided, the higher the performance of MSMEs. Innovation affects organizational performance and is beneficial for companies to create new value propositions through several activities, such as offering new services or goods, implementing new administrative and operational practices, providing technology-related solutions or providing new skills and capabilities. Besides that, innovation can also encourage the insights and skills needed to be effectively implemented, mastered and enhanced with existing technology and to create something new (Fatimah & Azlina, 2021; Hasanah & Siregar, 2021).

Intellectual Capital Influences Innovation

This research results align with the similar study, which proved that intellectual capital has a significant effect on innovation (Almutirat, 2022; Kekskin et al., 2018). Then, previous research states that intellectual capital significantly impacts innovation. This is due to the increasing number of competitors and demand; MSME entrepreneurs must be able to fulfill the wishes of their customers by creating several innovations. In addition, intellectual capital is a crucial source of innovation, including experience, creativity, and skills (Nasih, 2011; Shabiya, 2022). Intellectual capital is the primary key to the organization and is responsible for innovation (Delgado-Verde et al., 2014; Gomezelj Omerzel & Smolčić Jurdana, 2016). Intangible assets such as intellectual capital are an essential indicator in creating competitiveness, and this states that the ability of MSMEs to innovate is closely correlated to intellectual capital or the ability to utilize knowledge resources. This is because innovation is closely related to knowledge. In addition, intellectual capital is the main asset that needs to be owned by an organization in a knowledge-based economy to create a competitive advantage and improve organizational performance to trigger innovation.

Intellectual Capital Influences MSME Performance

Intellectual capital, which consists of human capital, customer capital, and structural capital, has a positive and significant effect on the performance of MSMEs. This is due to how vital intellectual capital is in developing the business world for the future. Because it is intangible and unique, it is also considered the primary business driver (Hermawan et al., 2017; Kurniawan, 2019). Therefore, MSMEs are required to maximize their intellectual capital, which later is expected that MSMEs will be able to focus on efforts to manage intellectual capital. Research by Rahayu states that intellectual capital, either partially or as a whole, positively impacts the performance of MSMEs. The more MSMEs improve their skills and capabilities accompanied by operational standards aligned with the MSME vision and mission, build harmonious relationships with each customer, and implement a good work culture. More MSME business performance will be added to fulfill MSME goals (Hermawan et al., 2017; Kurniawan, 2019).

Intellectual Capital Influences MSME Performance Through Innovation

The results of this research are supported by Shabiya's research, which proves that intellectual capital affects the performance of MSMEs through innovation. Intellectual capital is the basis for MSME entrepreneurs to improve their performance in managing or enhancing management-related businesses. By developing innovations, customers will not feel bored and satisfied with the products offered. Therefore, intellectual capital management can benefit MSME entrepreneurs by increasing innovation to improve the performance of the MSMEs themselves (Dristianto & Rodhiyah, 2016; Hermawan et al., 2017). In addition, Dristianto & Rodhiyah's research also proves that there is a significant influence between intellectual capital and MSME performance through innovation. In an economic change characterized by an economy based on knowledge, a business will always be required to carry out knowledge management so that it can compete with other MSMEs by cultivating creative ideas so that innovation emerges that will have an impact on the performance of the MSMEs themselves (Dristianto & Rodhiyah, 2016; Hermawan et al., 2017). The results of this research provide an important contribution in understanding the relationship between innovation, intellectual capital and MSME performance. The implication of these findings is that MSMEs need to pay attention to the importance of innovation and intellectual capital management to improve their performance. Therefore, MSMEs are advised to focus on developing sustainable innovation and effectively utilizing intellectual capital to achieve competitive advantage. Apart from that, it is important to know that good intellectual capital management can be the key to creating added value and improving the performance of MSMEs amidst increasingly fierce competition. However, this research has limitations in terms of sample size and data collection methods. Therefore, it is recommended to conduct further research

with a larger sample and use more diverse data collection methods to gain a more comprehensive understanding of the relationship between innovation, intellectual capital and MSME performance.

4. CONCLUSION

Based on the discussion, it can be concluded that intellectual capital influences MSME performance through innovation. This is because a business will always be required to carry out knowledge management to compete with other MSMEs by creating creative ideas so that innovation arises that will impact the MSMEs' performance. The advice is to increase the number of research samples, so that the research results can be better and applied to many MSMEs in Indonesia to improve their performance.

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