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DOES PERFORMANCE IMPROVE SUSTAINABILITY? EMPIRICAL RESEARCH ON INDONESIAN MSMEs

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ABSTRACT

MSMEs (Micro, Small, and Medium Enterprises) is a business sector that plays an essential role in the economic growth in a country, especially in Indonesia. Nowadays, the creative industry is one of the fast-growing business sectors. Encouraging the growth of MSMEs in the creative industry sector is one form of government effort in promoting sustainable economic development. This research analyses the impact of financial literacy and market orientation on the MSMEs performance and sustainability. The research sample was 95 respondents. They are owners or managers of MSMEs in the creative industry in the Special Region (Province) of Yogyakarta. The hypothesis testing results show that financial literacy and market orientation positively impact performance and sustainability. Besides that, the performance of MSMEs also influences business sustainability. But, financial literacy has no significant impact on business sustainability. This research's implication is the need for government assistance to encourage MSMEs owners to increase knowledge about financial literacy and market orientation so that MSMEs can develop more optimally.

Keywords: Financial literacy; market orientation; performance; sustainability; MSMEs

I. INTRODUCTION

Micro, Small, and Medium Enterprises (MSMEs) have a crucial role in developing a country (Audretsch, Horst, & Thurik, 2009). MSMEs in Indonesia contribute to poverty alleviation by creating new employment to absorb labor, and then it becomes a contributor to the Gross Domestic Product (Budiarto, Prabowo, & Herawan, 2017). Central Statistics Agency (2019) states that there was an increase in employment until February 2019, reaching 94.99%, and the contribution of MSMEs to Gross Domestic Product (GDP) reached 65%.

Although MSMEs have a significant role in creating employment, MSMEs still struggle to compete with large industries. Some of the problems faced are HR capacity, technology, business, ownership, marketing, financing, and other business management issues (Abor & Quartey, 2010; Budiarto, Sari, Sudaryana, & Prabowo, 2018). A creative economy is a form of sustainable

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economic development efforts to catch up with the development of MSMEs because of the optimization of unlimited resources with ideas, talents, and creativity. Indonesia has 16 sub-sectors of creative industries such as applications and games, architecture, interior design, visual communication design, product design, fashion, film, animation and video, photography, crafts, culinary, music, publishing, performing arts, fine arts, television, radio (Ministry of Tourism and Creative Economy, 2019). The Indonesian government is currently driving SMEs' growth with creative economy programs to reduce unemployment since the creative industry has the most significant potential in achieving sustainable development (Mardiana, Warsiki, & Heriningsih, 2020; Dahles, Prabawa, & Koning, 2020). The creative industry has an essential role because, without creativity, the industry will die (Indriartiningtias, Subagyo, & Hartono, 2019).

MSMEs in the creative industries in business decision-making use short-term orientation so that there is no increase in long-term performance (Manurung & Barlian, 2012). Therefore, MSMEs owner must know about financial management to develop and manage their business (Karadag, 2015). Understanding of financial literacy is crucial for entrepreneur to improve business performance (Dahmen & Rodríguez, 2014). Financial literacy helps companies access financial resources to increase company growth (Adomako, Danso, & Ofori Damoah, 2016).

In addition to financial literacy, MSMEs owners must have a market orientation to improve business performance and sustainability. The entrepreneur is always required to find what is happening in the market. Also, understand the desire for the consumer to maintain business continuity. Owners must be able to increase their understanding of the importance of innovation and market orientation because this will boost the better performance of MSMEs, affecting business competitiveness and performance improvement (Tham, Ab Yazid, Khatibi, & Azam, 2017). Innovation is the key to the sustainability of MSMEs businesses so that the company is different from competitors (Klewitz & Hansen, 2014).

Although there have been many studies on MSMEs, this research is still interesting because 1) Sustainability of MSMEs in the creative industries sector always involves innovation and market orientation (Kraus, Burtscher, Niemand, Roig-Tierno, & Syrjä, 2017). 2. The existence of research inconsistencies which states that financial literacy and market orientation can improve business performance and sustainability (Dahmen & Rodríguez, 2014; Fatoki, 2014; Wise, 2013; Adomako et al., 2016; Eresia-Eke & Raath, 2013; Ozkaya, Droge, Hult, Calantone, & Ozkaya, 2015; Zhou & Tse, 2005). 3. There is limited literature that combines financial literacy and market orientation on performance and sustainability, so it is still an empirical question.

This study provides two implications for MSMEs. First, MSMEs improve their marketing orientation by expanding market share, especially with e-commerce. Second, a local brand image is needed for MSMEs so that the business name is easy for consumers to remember. These two implications will encourage MSMEs to maintain business sustainability in the future so that they are not easily affected by environmental changes.

II. THEORETICAL REVIEW AND HYPOTHESIS

2.1. MSMEs (Micro, Small and Medium Enterprises)

MSMEs are productive business activities that can realize development success, mainly in developing countries (Eniola, 2014). MSMEs play an essential role in driving the economy to create jobs to increase people's income. According to (Law of the Republic of Indonesia Number 20 the Year 2008), MSMEs in Indonesia are grouped into three categories: Microbusiness, small business, and medium-sized business. These three categories are generally differentiated based on

net assets, annual sales income, and employees' numbers. Microbusiness has net assets <IDR 50,000,000.00; IDR 50,000,000.00-500,000,000.00 for small business and> IDR 500,000,000.00 for Medium-size. Microbusinesses have annual sales of <IDR 300,000,000.00; IDR 300,000,000.00-2,500,000,000.00 for small business and> IDR 2,500,000,000.00 for medium-size. According to the Central Statistics Agency, the number of net assets excluding land and buildings is categorized based on the number of employees. The number of employees for micro-businesses is <4, and small businesses are 5-19 while medium-size businesses have 20-300 employees.

2.2. Financial Literacy

The lack of financial literacy levels of MSMEs entrepreneurs will have an impact on business performance. Financial literacy is a skill in managing and using the money owned to increase future living standards (Lusardi, 2012). According to (Financial Services Authority, 2014), financial literacy is knowledge, skills, and beliefs that influence attitudes and behavior to improve the quality of decision making and business management to prosper.

According to Eresia-Eke & Raath (2013) there are several financial literacy perspectives: consumers, commercial service providers, the government, and individuals or families. A consumer point of view explains that functional financial literacy can create purchase decisions of goods and services that prioritize quality. Commercial service providers' perspective suggests that proper financial literacy management will produce adequate information about the product being sold in terms of understanding risk and cost efficiency to customers. The government perspective explains that the government will get maximum tax revenue to develop infrastructure and public service facilities. Meanwhile, from individuals' or families' perspectives, the right level of financial literacy can improve one's ability to have long-term savings or investments.

2.3. Market Orientation, Business Performance & Sustainability

MSMEs are one of the most popular business types for entrepreneurs, so to maintain their businesses businesses must cross the market to survive among the many competitors. Market orientation is a strategy used by companies to achieve a sustainable competitive advantage based on the generation, the information in organizations, and markets' selection to be addressed (Maydeu-Olivares & Lado, 2003). Companies must understand the needs, desires, and market demands to improve business performance (Octavia et al., 2020). According to Azam, Ferdous S, Aque, Abdullah, & Anwar (2014); Tham et al. (2017); Udriyah, Tham, & Ferdous Azam (2019), market orientation becomes three dimensions: customer orientation, competitor orientation, and coordination inter-functional.

Business performance is a concept to measure company performance to achieve business success in the market competition (Mahmoud, Blankson, Owusu-Frimpong, Nwankwo, & Trang, 2016). The MSME's performance is an achievement from an individual's effort doing his role in the company for a certain period (Mutegi, Njeru, & Ongesa, 2015). According to (Budiarto et al., 2017), MSME's performance measurement uses self-measures to quantify financial and non-financial performance.

Business sustainability is a consistent business condition in achieving business growth and development. Business sustainability is influenced by several factors, such as a regular updating of a business plan, the compilation of business plans, routine competitor analysis, the ease of entering into a new business, and the ability to calculate risk (Ligthelm, 2010). Business continuity is shown by business owners' ability to innovate and sustain the business in the long term. The

ability to innovate is proof that the business has a guidance for building and reading the future chance (Kaswuri, 2016). Innovation is the key to the sustainability of MSMEs so that companies are different from competitors (Wahyuni, 2019).

2.4. Hypotheses Development

Financial literacy is knowledge about managing finances to achieve a more prosperous in the current time and future (Karadag, 2015). Business owners need financial literacy in making strategic financial decisions to achieve company goals in improving business performance and sustainability (Drexler, Fischer, & Schoar, 2014). Sound financial knowledge by the owner can improve business sustainability (Fatoki, 2014).

MSMEs are a type of productive business owned by individuals and communities to reach economic development success. MSMEs owners need financial literacy and market orientation to improved performance and business sustainability (Udriyah et al., 2019). To maintain business sustainability, companies need to improve performance (Wise, 2013; Dahmen & Rodríguez, 2014). Adomako et al. (2016), in their research, stated that there is a mutually influential relationship between financial literacy and business performance. Businesses with good functional financial literacy will anticipate environmental changes in terms of trade, economy, and finance to improve business performance and sustainability. The results of this study contradict the findings Eresia-Eke & Raath (2013), which states that there is no influence on financial literacy and business performance. However, in his research, (Adomako et al., 2016) say that with proper financial literacy, the company can survive during economic crises so that business performance continues to increase and has long-term sustainability. Based on some findings above, the following hypotheses are proposed:

H_{1a}: Financial literacy positively impact the performance of MSMEs.

H_{1b}: Financial literacy positively impact the sustainability of MSMEs.

Market orientation increases competitiveness and directly influences company performance (Udriyah et al., 2019). Market orientation is essential because, with market orientation, business owners can collect and manage information to understand market needs. Understanding market needs will drive the innovation process that exists in the company. The company must improve the sustainability of its business by innovating and increasing employee and customer satisfaction (Hudson, Smart, & Bourne, 2001).

Research conducted by Dubihlela & Sandada (2014); Šályová, Tábořecká-Petrovičová, Nedelová, & Ďad'o (2015); Lee, Kim, Seo & Hight (2015); Kaswuri (2016) states that market orientation has a significant effect on performance and innovation. Innovation is a business owner's strategy to maintain business sustainability (Mahmoud et al., 2016). Based on the theoretical study, the following hypotheses are proposed:

H_{2a}: Market orientation positively impact the performance of MSMEs.

H_{2b}: Market orientation positively impact the sustainability of MSMEs.

MSMEs plays a significant role, not only create of employment but potentially as generate of economic development. If the performance of MSMEs is excellent, it will survive amid increasingly fierce business competition. The company's ability to create innovation will be in line with performance because a lack of creativity will be detrimental to business continuity

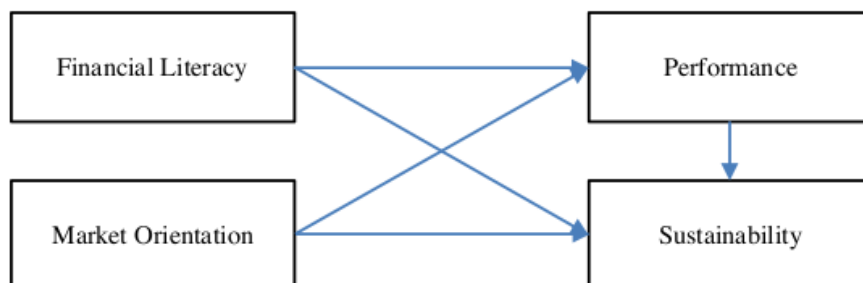
(Tambunan, 2011). According to Mckague, Wheeler, Corrine, Comeault, & Ray (2011), companies need to innovate to develop business performance to create long-term business sustainability. Research conducted by (Pramudiati, Putri, & Basri, 2019) states that performance positively impact business sustainability. Based on the findings, the following hypothesis is proposed:

H₃: Performance positively impact the sustainability of MSMEs.

2.5. Research Model

It has become a consensus that MSMEs have an essential role in economic growth in developing countries (Alzougool, 2019). Even though they have a strategic position, MSMEs cannot compete with large companies (Adomako et al., 2016); therefore, a particular strategy is needed to maintain MSMEs' growth performance. In line with these problems, inappropriate performance measurement is still a primary problem for MSMEs (Maduekwe & Kamala, 2016). MSMEs can use various strategies to improve their performance, such as marketing strategies or increasing their owners' ability through financial literacy (Indriartiningtias et al., 2019; Virtanen, Björk, & Sjöström, 2017). Financial literacy is the skills of MSMEs owners in various economic contexts that are useful for decision-making. The owner's financial literacy ability will understand various financial problems to improve small firms' financial well-being (Mutegi et al., 2015). Market orientation is a strategy that makes consumers a vital factor affecting all organizational activities. This market orientation will always be associated with MSMEs' progress because organizations will easily learn about market developments and adapt quickly to market changes (Octavia et al., 2020). Based on some of these research perceptions, a research model is proposed, as shown in Figure 1.

Figure 1: Research Model



III. RESEARCH METHODOLOGY

This research was conducted in Yogyakarta province, which consists of 1 city, namely Yogyakarta, and four regencies, namely Sleman, Kulon Progo, Bantul, and Gunungkidul since 1: In Indonesia, Yogyakarta Province is known as the city of education, culture, and tourism so that creative business experiences growth (Umami, 2015; Suarman, 2015; Sugandini et al., 2018); 2 previous research on MSMEs area was only conducted in 1 location, such as Bantul Regencies (Muafi, 2015); Sleman Regencies (Mardiana et al., 2020; Rachmawati, Hapsari, & Cita, 2018); Yogyakarta

City (Dahles et al., 2020), Gunungkidul Regencies (Probosari, Wijayani, & Paryati, 2020) while this research expands the object of study to make it easier to generalize (Alharbi & Drew, 2014). This study's population is the creative owners of micro, small, medium enterprises (MSMEs) in the creative, culinary, fashion, TV, and radio sectors in the Special Region of Yogyakarta. The sampling method used was purposive sampling, with the following criteria: 1) The business is still operating, 2) Having at least one employee. The number of samples taken in this study was 95 respondents. Respondents in this study are the owners and managers who act like people in charge at MSMEs. This sample size follows the rule of thumb, which states that the sample size is between 30 and 500 are appropriate for most research Roscoe (1975); Sekaran & Bougie (2014).

This study uses a local language questionnaire (Indonesian) because the research location is in Yogyakarta Province. The questions on the questionnaire were adopted and developed from previous research. Before distributing questionnaires both on-line and off-line, a pre-test was conducted on research students and MSMEs owners to ensure that the questions were easy to understand. Several questions were then modified to suit the real conditions of the organization. The financial literacy variable is measured with five questions modified from (Aribawa, 2016), such as identifying the company, potential savings, calculating credit interest, and the effect of inflation.

Market orientation variables are measured by three indicators: customer orientation, which is developed into four questions. Competitor orientation, which is developed into two questions, and inter-function coordination becomes one question (Udriyah et al., 2019). Performance variables are measured with four questions: the existence of planned work, the ability to anticipate products when demand increases, guarantee the timeliness to customers, and the suitability of products with specifications offered (Octavia et al., 2020).

Sustainability variables are measured with eight questions which modified from previous research, such as willingness to try new ideas, introducing more new products, increasing product design capacity, modifications the products, improving work practices, employee training, developing management involvement, technological updates (Klewitz & Hansen, 2011; Aribawa, 2016).

The measurement scale used is 1 to 5, where 1 (Strongly Disagree), 2 (Disagree), 3 (Neutral), 4 (Agree), 5 (Strongly Agree). Testing instruments in this study used validity and reliability tests. Meanwhile, to analyse the impact of independent variables on the dependent variable using bootstrapping techniques on the Smart PLS.

IV. RESULT AND DISCUSSION

In this study, researchers collected data for three months, starting from mid-October to December 2019, by distributing 120 questionnaires. Based on the results of the distribution of questionnaires, only 100 returned questionnaires, 95 questionnaires could be analysed, while five questionnaires could not include because of incomplete. The results of the analysis of 95 questionnaires are shown in Table 1.

Table 1: Respondent's Characteristic

		Sleman	Yogyakarta	Bantul	Kulon Progo	Gunung kidul	Total
Size	Micro	18	7	12	5	39	81
	Small	3	-	1	2	4	10
	Medium	2	-	2	-	-	4
Role	Owner	20	6	12	7	29	74

	Manager	3	1	3	-	14	21
Gender	Male	6	7	7	4	39	63
	Female	17	-	8	3	4	32
Education	Non-bachelor	16	7	12	7	41	83
	Bachelor	7	-	-	-	2	12
Business's Age	< 3 years	4	-	-	1	2	7
	3 - 5 years	2	-	2	-	3	7
	6 - 10 years	5	1	2	2	16	26
	> 10 years	12	6	11	4	22	55
Number of Employee	1-10	18	7	12	5	41	83
	11-20	2	-	1	2	2	7
	21-30	3	-	1	-	-	4
	>30	-	-	1	-	-	1
Type of Business	Craft	11	7	8	2	42	70
	Culinary	8	-	2	2	-	12
	Fashion	4	-	5	2	-	11
	Multimedia	-	-	-	1	1	2

The measure ¹³ of model quality is a test used convergent validity test and reliability test. An indicator will meet convergent validity if it has an outer loading value > 0.5. Table 2 shows the results of convergent validity tests, while Table 3 shows the reliability test results. The test of structural model (inner model) in this study using the coefficient of determination. Table 4 shows that the results of R square for the performance and sustainability variables. The low R square indicates that the variation in performance and sustainability can only be explained by small market orientation and financial literacy. The low value of R square in social research is not a problem because it is used to test the theory, not to predict (Moksony, 1999). Also, there are many other factors related to the growth of MSMEs, such as access to finance & capital (Adomako et al., 2016); organizational creativity (Indriartiningtias et al., 2019); social media (Konstantopoulou, Rizomyliotis, Konstantoulaki, & Badahdah, 2019); environment (ByoungHo Jin, 2010) which is an opportunity for further research.

Table 2: Cross Loading Value

Variable	Question	Cross Loading
Financial Literacy	1. Identification of the company at the time of opening an account	0.655
	2. Understanding of potential savings yields in one year	0.765
	3. Understanding of potential savings yields in multi-years	0.755
	4. Understanding of calculating credit interest per year	0.713
	5. Knowledge of the effect of inflation on company growth	0.701
Market Orientation	1. Have a strong focus on understanding customer needs.	0.751
	2. Always provide value-added products for customer satisfaction.	0.698
	3. Pay attention to the after-sales service of our products.	0.740
	4. Always try to give the best quality products to our customers.	0.820
	5. Quick to respond to changes in prices or strategies made by competitors	0.624
	6. Competitive price comparison	0.648
	7. Encourage staff to bring in new ideas	0.694
Performance	1. The existence of planned work	0.720

	2. The ability to anticipate products when demand increases	0.747
	3. Guarantee the timeliness to customers	0.733
	4. The suitability of products with specifications offered	0.724
Sustainability	1. Willingness to try new ideas	0.792
	2. Introducing more new products than competitors	0.679
	3. Increasing product design capacity	0.737
	4. Introducing modifications to existing products	0.741
	5. Continually improving work practices	0.738
	6. Employee training	0.740
	7. Developing management involvement	0.686
	8. Technological updates for service quality	0.575

10

Table 3: Construct Reliability and Validity

	Cronbach's Alpha	Rho_A	Composite Reliability	Average Variance Extracted (AVE)
Financial Literacy (FIN)	0.769	0.772	0.842	0.517
Market Orientation (MAR)	0.838	0.884	0.878	0.509
Performance (PER)	0.711	0.712	0.821	0.535
Sustainability (SUS)	0.861	0.865	0.892	0.509

19

Table 4: R Square Value

	R Square	Adj. R Square
Performance	0.396	0.383
Sustainability	0.407	0.387

All of the Hypothesis testing in this study use smart PLS—the test of all hypotheses, affecting financial literacy on performance and sustainability using bootstrapping techniques. Table 5 shows the results of hypothesis testing using bootstrapping techniques.

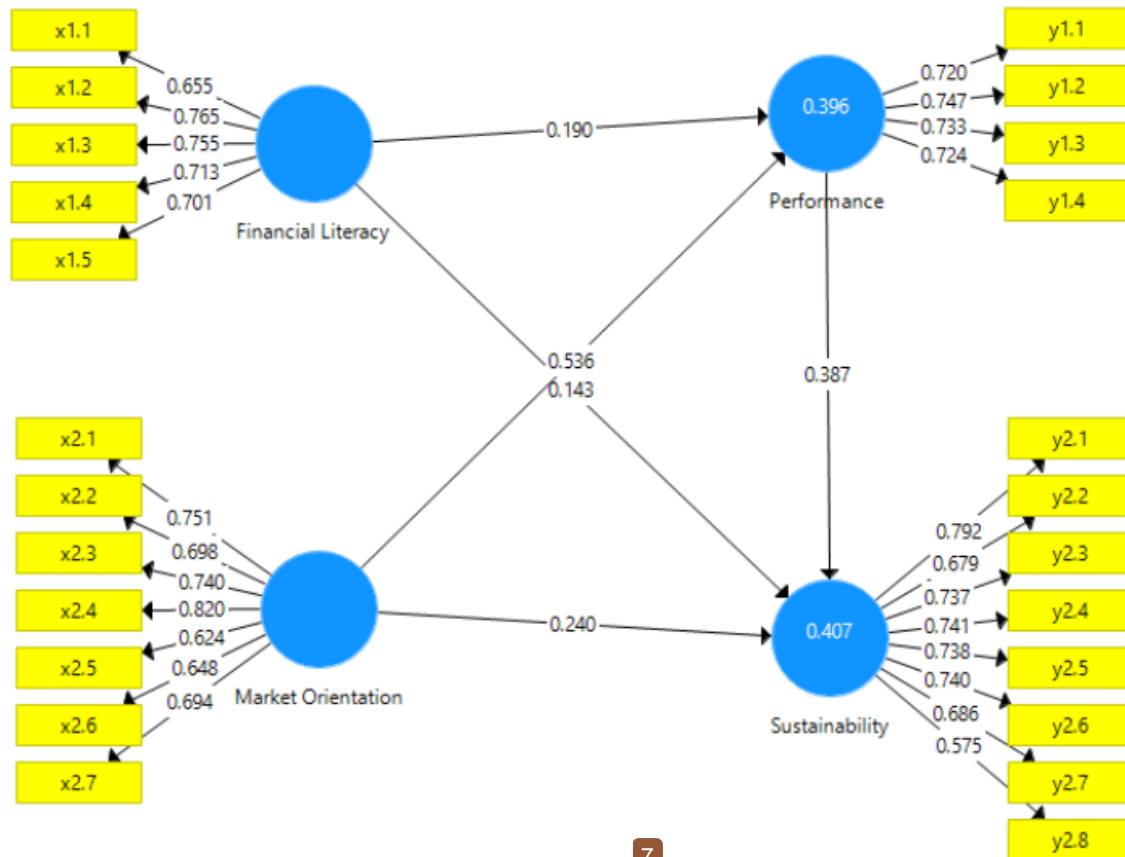
Table 5: Path Coefficients

	Beta	Mean	SD	T Statistics	P Value	Result
FIN → PER	0.190	0.194	0.103	1.844	0.066*	H _{1a} : Accepted
FIN → SUS	0.143	0.157	0.115	1.245	0.214	H _{1b} : Rejected
MAR → PER	0.536	0.555	0.086	6.215	0.000***	H _{2a} : Accepted
MAR → SUS	0.240	0.254	0.104	2.319	0.021**	H _{2b} : Accepted
PER → SUS	0.387	0.371	0.112	3.464	0.001**	H ₃ : Accepted

*Sig < 10%, ** sig < 5%, *** sig < 1%

The hypothesis testing using the bootstrapping technique reveals that financial literacy positively impact MSMEs' performance. Some research shows that financial literacy plays an essential role in helping business actors make financial decisions to maintain business performance (Adomako et al., 2016). MSMEs have unique characteristics so that in running their business, it is necessary to have cooperation to complement each other's limitations to compete globally.

Figure 2: Hypotheses Testing



7

However, research cannot prove the significant effect of financial literacy on business sustainability because one of MSMEs' problems is a lack of financial knowledge (Adomako et al., 2016) These results are in line with Eresia-Eke & Raath (2013), which states that financial literacy does not affect MSMEs performance and growth. Furthermore, research Fatoki (2014) it also finds evidence that the financial literacy of MSMEs owners is at a weak level. This study allegedly because many respondents did not understand financial literacy due to low levels of education. The majority owner's level of education is non-bachelor (80%), while a few people only pursue the degree of education of the Bachelor. Such as research conducted by Abor & Quartey (2010) states that SMEs' development is experiencing a bottleneck due to the owner's low managerial ability. The correlation between financial literacy on sustainability is the indirect impact through the performance. The coefficient test results show a significant influence between financial literacy and performance, then a significant impact between performance and sustainability. This result is a challenge for further studies to analyse the relationship between financial literacy and sustainability through performance mediation.

The level of education affects one's understanding of financial literacy; MSME owners with higher education levels will have a deeper understanding of financial literacy to influence the orientation of long-term efforts to make business decisions (Dahmen & Rodríguez, 2014). MSMEs owners can use external expertise if they experience problems in understanding financial literacy to continue to run. Individuals with business management knowledge can reduce the impact of financial mismanagement (Kotze & Smit, 2008).

Market orientation has a positive impact on the performance of MSMEs. Companies with market orientation will improve business performance, so business owners are expected to establish good relationships with suppliers because it can help maintain business performance by having appropriate and adequate material availability (Udriyah et al., 2019). Companies with a market orientation focusing on customers and always observing competitors will make it easier for companies to innovate to create products needed by the market (Mahmoud et al., 2016). Companies' success in innovating to develop and see business opportunities can describe sustainable businesses (Hudson et al., 2001).

Besides, a local brand is needed to believe in the quality of the products produced that have value in consumers. Consumers who believe that the company has the right product will increase customer loyalty and make purchases (Wibowo, Udasmoro, & Noviani, 2020). Furthermore, MSMEs' problem is how to sell their products because the costs for promotion in a conventional way are costly (Alzougool, 2019). Therefore, social media is expected to be an efficient means of opening product marketing channels with relatively low cost, fast response, and a much wider reach, popularly known as e-commerce (Rachmawati et al., 2018). This online media is beneficial since it significantly influences consumer behavior. (Kim & Ko, 2012).

Furthermore, to test the mediation effect, a coefficient test is carried out on financial literacy, performance, and sustainability. The direct impact between market orientation and sustainability is 0.240, more significant than the indirect effect through the mediation of performance 0.207 ($0.536 * 0.387$). Therefore performance is not a mediating variable between market orientation and sustainability.

Finally, the findings suggest that performance has a positive impact on business continuity. The performance of SMEs can be seen from the innovations made to maintain business long term. Innovation of the company will be able to improve product quality, increase sales, and profitability. Therefore, improving the performance of MSMEs will create sustainability and become a guarantee for the business (Pramudiati et al., 2019).

V. CONCLUSION AND RECOMMENDATION

Based on the hypothesis testing, we can conclude that market orientation positively impacts the performance and sustainability of MSMEs. Subsequently, performance has a positive impact on business sustainability. Besides, financial literacy has a significant impact on performance but has no significant impact on MSMEs sustainability.

This research has limitations because it only takes samples in 4 creative industries MSMEs subsectors from a total of 16 subsectors. The next examination is expected to expand the sampling that involves the entire MSMEs subsector in the creative industry because the more samples, the better the study results (Alharbi & Drew, 2014). Further research is also suggested to add financial

decision-making variables because it provides many benefits, mainly for financial decision-making and develops a new market (Lusardi, 2012).

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