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# The Effect of Capabilities on SMEs Performance with Competitive Advantage Mediating Variables: A Case Study in Medan City

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**Abstract**

The SMEs sector is very influential on economic growth in various countries, including Indonesia. During the Indonesian Covid-19 pandemic, SMEs were affected by social distancing policies, the implementation of community activity restrictions (PPKM) and other policies that disrupted SMEs operational activities. In order to overcome these problems, capabilities are needed that are able to help the performance of SMEs. There are four capabilities in this study, namely innovation capabilities, marketing capabilities, learning capabilities and managerial capabilities. This study examines the indirect relationship between the capability and performance of SMEs through competitive advantage as a mediating variable. Competitive advantage is considered capable of providing an important role in the relationship between the capability and performance of SMEs. Using a quantitative research approach, this study collected data with questionnaires to 107 SMEs actors in the city of Medan but only 101 were usable. This study proves that two of the four capabilities have a positive and significant effect on financial performance. This study also proves that the capabilities of the company must create a competitive advantage in order to be able to improve the performance of SMEs.

**Keywords:** Capability, Competitive Advantage, Performance, SMEs.

## INTRODUCTION

Micro, small and medium enterprises (SMEs) are one of the driving forces of economic development (World Bank, 2005). The SMEs sector has an important role not only in economic development, but also in poverty alleviation and job creation (Gharakhani & Mousakhani, 2012, Fawzeea et al., 2019). According to the Central Statistics Agency (BPS) in 2020 the number of Micro, Small and Medium Enterprises (SMEs) will reach 64 million. This figure reaches 99.9 percent of all businesses operating in Indonesia.

According to Pešalj et al. (2018) the success of SMEs depends on their capability to balance short-term and long-term goals, internal and external focus, control and creativity, implementation of current strategies and development of new ones. However, SMEs management processes and capabilities that are not well-practiced and lack of resources make it difficult for them to achieve this balance (Fuller-Love, 2006; Garengo et al., 2005; Smith & Smith, 2007, Sofiyah et al., 2018). To overcome this, SMEs need to have various capabilities such as innovation, marketing, learning capabilities and adequate managerial capabilities.

The development of the SMEs business during 2020 was also affected by the pandemic. The increase in positive cases of Covid-19 in various countries has triggered the implementation of social distancing and lockdown policies which have resulted in the closure of schools, campuses, houses of worship, and shopping centers (Fakhruroji et al., 2020). The Covid-19 pandemic has caused most SMEs to slump and have an impact on business closures due to production process delays, cash flow problems, closure of business activities/operations, layoffs of employees, and savings in company capabilities for future expansion (Ginting et al., 2019, Smith-Bingham & Hariharan, 2020). A survey conducted by the Indonesian Institute of Sciences (LIPI) through the Center for Economic Research (P2E) showed that more than 94 percent of MSMEs experienced a decline in sales due to the Covid-19 pandemic (LIPI, 2020).

These problems require stakeholders to work to maintain the sustainability of MSMEs and to structure and revitalize the SMEs sector with the aim of creating MSME commitment and trust (Hadi & Purwati, 2020). To reduce the decline in the performance of MSMEs during the pandemic, appropriate and fast innovation is needed to create new activities to ensure the sustainability of their business (Septina, 2020). SMEs are expected to be able to improve their performance by adapting to changes.

Sok et al. (2013) explained that there are three main capabilities that organizations must have to improve performance and maintain organizational sustainability, namely innovation, marketing and learning capabilities. Furthermore, companies need to develop a different set of capabilities in order to be able to win the global competition (P Sok & O'Cass, 2011). This study replicates the previous research, but adds one independent variable, namely managerial capability because it is based on the suggestion of Robbins et al. (2009) which states that if a manager wants to succeed in his business which is seen from his performance, then a manager must have and carry out, (1) management functions, (2) management roles, and (3) management expertise. Mahoney (1995) states that managerial capabilities will generate profits for companies involved in competition. In the context of SMEs, managerial skills will help business actors in managing their business,

such as managing their finances and resources. This is reinforced by the research of Haber & Reichel (2007) which concludes that the managerial ability of entrepreneurs has a positive effect on business performance.
Another study conducted by Holcomb et al. (2009) also found that managerial capability has a positive effect on organizational performance.

Falahat et al., (2020) stated that the possible cause of the inconsistency of results in the capability-performance relationship was caused by omitted mediators such as competitive advantage. Therefore, further research is needed on the relationship between competitive advantage and capability (Falahat et al., 2020).

## LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

### Literature Review

### Resource-Based View Theory

This study uses the resource-based view (RBV) theory which states that the company's resources and capabilities are valuable and difficult for competitors to follow (Harts, 1995). According to RBV theory, firm capabilities are complex (Barney, 1991) and are accumulated and shaped by the interrelationships of internal and external resources of the firm that are difficult to imitate (Falahat et al., 2020). In other words, capabilities can be a source of competitive advantage if they are long-lasting, non- transparent, and difficult to imitate (Falahat et al., 2020). Based on the explanation above, it can be said that RBV theory provides impetus for companies to create competitive advantages (Barney, 1991), one of which is by having capabilities such as innovation, marketing capabilities, learning capabilities and managerial capabilities (Holcomb et al., 2009; P Sok & O'Cass, 2011).

### SMEs

Micro, small and medium enterprises (SMEs) are defined in the Law of the Republic of Indonesia No. 20 of 2008 concerning SMEs. The law regulates the criteria used to define SMEs as stated in Article 6. Such as net worth or asset value excluding land and buildings for business premises, or annual sales proceeds. With the following criteria:

(1) Criteria for Micro Enterprises are as follows: a. has a net worth of at most Rp. 50,000,000.00 (fifty million rupiahs) excluding land and buildings for business premises; or b. have annual sales of a maximum of Rp.300,000,000.00 (three hundred million rupiah).

(2) Small Business Criteria are as follows: a. has a net worth of more than Rp. 50,000,000.00 (fifty million rupiah) up to a maximum of Rp. 500,000,000.00 (five hundred million rupiah) excluding land and building for business; b. or have annual sales of more than Rp.300,000,000.00 (three hundred million rupiah) up to a maximum of Rp.2,500,000,000.00 (two billion five hundred million rupiah).

(3) The criteria for Medium Enterprises are as follows: a. has a net worth of more than Rp. 500,000,000.00 (five hundred million rupiahs) up to a maximum of Rp.

10,000,000.00 (ten billion rupiahs) excluding land and buildings for business; or b. have annual sales of more than Rp.2,500,000,000.00 (two billion five hundred million rupiah) up to a maximum of Rp.50,000,000,000.00 (fifty billion rupiah).

**SMEs Performance**

Organizational performance is the company's achievement from the established strategy, both in terms of financial and non-financial (Geng, Mansouri and Aktas, 2017). In the case of SMEs, performance refers to the "value" contributed to customers and owners (Porter, 1990). In addition, Laitinen (2002) defines company performance as "the ability of an entity/business/company to produce results within the dimensions that have been determined in relation to targets". Sefiani and Bown, (2013) observe that performance is an indicator used to measure the goals and objectives set. Usually, company performance can be measured by Return on Assets (ROA), Return on Equity (ROE) and Return on Investment (ROI) when archived data is available (Anwar, 2018). **Competitive advantage**

Competitive advantage is defined as the strategic advantage of a company over rival companies in the industry, which allows it to appear above competitors and rival companies (Porter, 1997). A company can achieve competitive advantage if it can create more value than its competitors (Njuguna, Karanja and Kihoro, 2015). SMEs cannot achieve their competitive advantage if they only prioritize their own tangible assets, without trying to increase their knowledge of resources (Gassmann and Keupp, 2007).

**Innovation Capability**

Innovation capability is defined as a comprehensive set of characteristics of an organization that supports and facilitates an innovation strategy (Burgelman, Chloupková and Wobbe, 2014). Innovation capability consists of the ability to create and bring about new technological possibilities through economic practices (Adelekan, 2016). In general, innovation capability is a collection of interrelated processes that companies have to facilitate and implement the development, evolution, and implementation of product innovation (Sok, O'Cass and Sok, 2013). The term covers a wide range of activities from the ability to discover to the ability to innovate and the ability to improve existing technologies beyond the original design parameters (Loewe and Dominiquini, 2006).

**Marketing Capability**

Marketing capability refers to the company's ability to implement marketing activities such as market research, advertising, promotion, customer relations, sales efforts and so on (Dutta, Narasimhan and Rajiv, 1999; Vorhies and Morgan, 2005). Marketing capabilities represent the company's ability to understand and forecast

customer needs better than its competitors and effectively connect its offerings with customers (Mu, 2015).

**Learning Capability**

Learning capability can be defined as an organization's ability to create, transfer and integrate knowledge and modify its behavior with a view to improving its performance (Gomez, Lorente and Valle, 2005). It includes organizational and managerial factors including managerial commitment, openness, sense of belonging to the organization, experimentation, knowledge transfer, and integration, all of which facilitate the learning process (Goh and Richards, 1997).

**Managerial Capability**

Managerial capability is defined by Kroeger (1974), Acquaah (2003) Graves and Thomas (2006) as an inherent and heterogeneous management capacity, experience, expertise and process used for the implementation of strategies and productive activities. Fernández and Nieto, (2005) argue that existing managerial capabilities can be utilized to ensure quality management and company performance.

**Hypothesis Development**

**Relationship Between Innovation Capability and Performance of SMEs with Competitive Advantage as a Mediation Variable**

The ability to develop and produce innovative and unique products determines the competitiveness of a company (Falahat et al., 2020). Innovation capability is defined as a set of interrelated processes that companies have to facilitate and implement the development, evolution and successful implementation of product innovations (Sok, O'Cass and Sok, 2013). Product innovation capabilities increase time to market when introducing new products (Sok, O'Cass and Sok, 2013). As a result, Kaleka (2002) found that innovation capability leads to competitive advantage. Therefore, innovation capabilities can be both valuable and rare and, therefore, can bring competitive advantage when supporting companies in adapting to changing customer needs (Yang and Ju, 2018).

Then the proposed hypothesis is:

**H1: Innovation capability has a positive effect on SMEs performance through competitive advantage.**

**The Relationship Between Marketing Capability and Performance of MSMEs with Competitive Advantage as a Mediation Variable**

Marketing capability is the company's ability to plan, manage, and launch its marketing program (Zou, Fang and Zhao, 2003; Pham and Monkhouse, 2017).

According to Kamboj, Goyal and Rahman (2015) companies with marketing capabilities produce superior financial performance compared to companies that only focus on operational capabilities. Ahmadi, O'Cass and Miles (2014) found that marketing helps new technology ventures in India to demonstrate the competitive advantage of their products. In the context of MSMEs, marketing capabilities are often faced with poor resources such as cash flow and market expertise as well as tactical and strategic problems related to customers (Doole, Grimes and Demack, 2006; O'Dwyer, Gilmore and Carson, 2009). Although these obstacles are also faced by SMEs, O'Dwyer, Gilmore and Carson (2009) argue that SMEs always prioritize marketing capabilities as the key to competitiveness. With the characteristics of being small, agile and targeting small market segments, SMEs are able to pay great attention, offer friendly and outstanding services and provide products tailored to the specific needs of customers, all of which form the basis for achieving SMEs performance (Sok, O'Cass and Sok, 2013). Then the proposed hypothesis is:

**H2: Marketing capability has a positive effect on SMEs performance through competitive advantage.**

**The Relationship Between Learning Capability and Performance of MSMEs with Competitive Advantage as a Mediation Variable**

Learning capabilities are considered important to develop competitive advantage and improve financial performance over time (Ratnawati et al., 2018). Calantone, Cavusgil and Zhao (2002) found a direct relationship between learning capabilities and financial performance. Nybakk (2012) states that learning has a positive effect on company performance so companies must be directly involved in developing the knowledge of their employees. The relationship between factors that facilitate organizational learning, innovation and organizational performance has also been recognized. (Lopez, Peón and Ordás, 2005; Wang, 2008; Gunday et al., 2011; Alegre and Chiva, 2013). Then the proposed hypothesis is:

**H3: Learning capability has a positive effect on MSME performance through competitive advantage.**

**The Relationship Between Managerial Capability and Performance of MSMEs with Competitive Advantage as a Mediation Variable**

Managerial capabilities that function as structures, systems, and frameworks to produce measurable performance results (Aidoo, Agyapong and Mensah, 2020). In the context of MSMEs, the managerial role has the function of compiling an activity program, compiling a budget, establishing procedures, evaluating performance, and

monitoring the implementation of work programs in order to achieve its business strategy (Aisha et al., 2016). Several managerial competencies are very important for business such as industrial sector knowledge, creativity, innovation and risk taking (Aisha et al., 2016). Man, Lau and Chan (2002) identify the influence of different countries on managerial competence. The results of the study indicate that there are fundamental differences in trait competencies, based on differences in how to manage MSMEs. Bilkey (1978) which states that there is a positive and significant relationship between managerial ability-performance and to achieve superior performance, unique management abilities are needed as evidenced by Carmeli and Tishler (2004). Then the proposed hypothesis is:

**H4: Managerial capability has a positive effect on MSME performance through competitive advantage.**

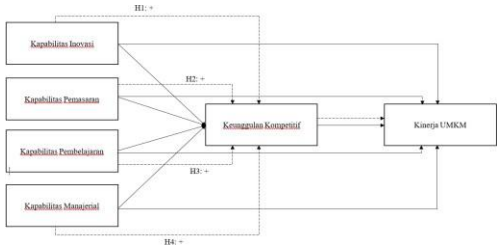


**Figure 1 Research Framework**

## RESEARCH METHODS

### Research design

This research is a hypothesis testing study that will explain the phenomenon of causal relationships between variables (Indriantoro and Supomo, 1999). A causal study is a causal relationship by analyzing the relationship between the independent variable and the dependent variable (Indriantoro and Supomo, 1999). To test this effect, the approach used is a quantitative approach with survey data collection methods.

### Population and Sample

The population of this research is SMEs in the city of Medan, North Sumatra. The total population of this study amounted to 1,293 SMEs recorded in the Medan City Cooperatives and SMEs Office report in 2019. The proportion of micro, small and medium entrepreneurs reached 99.8% of the total economic enterprises in the city of Medan (Central Bureau of Statistics, 2014) . This study used a sample collection technique with purposive sampling. Purposive sampling technique is the selection of samples based on the consideration of certain criteria (Cooper and Schindler, 2014). The sample criteria in this study are:

1. Have a net worth of more than Rp. 50,000,000.00 (fifty million rupiah) up to a maximum of Rp. 10,000,000.00 (ten billion rupiah) excluding land and building for business; or have annual sales of more than Rp.300,000,000.00 (three hundred million rupiah) up to a maximum of Rp.50,000,000,000.00 (fifty billion rupiah).

The sample in this study were entrepreneurs registered with the Medan City Cooperatives and SMEs Service who were still operating. The number of samples taken in this study were 100 respondents, because they were considered able to represent the existing population based on the estimation model using the maximum likelihood (ML) a minimum sample of 100 was required (Ghozali, 2008:64).

**Data collection technique**

The data collection technique used in this research is to conduct a survey through questionnaires to conduct a pilot test. Then in the pilot test, validity and reliability tests will be carried out for each variable. After the pilot test is completed and the construct is declared to have passed the validity and reliability test, the questionnaire is ready to be distributed.

**Data analysis technique**

This study uses Structural Equation Modeling (SEM) as a data analysis method. SEM is a type of multivariate analysis in the social sciences that includes multiple regression, factor analysis (CFA/EFA) and path analysis (path analysis) which explains the relationship between latent constructs or variables and their manifestations in a complex model, which can be estimated or tested simultaneously (Hair et al., 2013; Kock, 2018). Thus, this analytical method makes it possible to use variables that cannot be observed or measured directly by the manifestation variable or indicator (Hair et al., 2013).

**Measurement model (Outer Model)**

The measurement model is a component of the theoretical path model that contains indicators and their relationship to constructs (Kock, 2018). The following is a test of the measurement model, namely:

a. Validity test

Validity test was conducted to ascertain whether the statements used in the questionnaire were actually able to measure the object under study. When it is valid, the questionnaire can be distributed to respondents.

b. Reliability Test

Reliability is defined as reliability or consistency which indicates that repeated measurement of the same attribute will give identical or very similar results (Neuman, 2014). Measured by Composite reliability and Cronbach alpha, which reflects the internal consistency of the measuring instrument (Hair et al., 2013).

**Structural Model (Inner Model)**

The structural model (inner model) shows how the constructs relate to each other based on the theories used which are based on a fairly well-established theory. This structural model has several assessments, namely: path coefficient (β) and p-value, coefficient of determination (adjusted r-squared), predictive relevance (Q-Squared), and Variance Inflation Factor (VIF) (Hair et al., 2013 ).

**Hypothesis test**

Hypothesis testing aims to determine the level of significance of the influence of the independent variable on the dependent variable. In SmartPLS, the hypothesis is tested using the path coefficient. The path coefficient value shows the level of significance in hypothesis testing. The significance value is indicated by the T-statistic value which must be >1.96 and the P-value <0.05 to get significant results (Abdillah & Hartono., 2015:197).

**ANALYSIS AND RESULT**

**Characteristics of Research Data**

This study is a questionnaire survey whose questions use a Likert scale of 1-5.

**Table 1 Descriptive Statistics**

| Variable | Minimum | Maximum | Average |
|---|---|---|---|
| **KI** | 3 | 5 | 4,17 |
| **KP** | 3 | 5 | 4,19 |
| **KPL** | 3 | 5 | 4,14 |
| **KM** | 3 | 5 | 4,25 |
| **KK** | 3 | 5 | 4,28 |
| **KIN** | 3 | 5 | 4,28 |

**Analysis of the Measurement Model (Outer Model)**

**Construct Validity Test**

Convergent validity is said to be valid if the standard value of loading is at least between 0.4 - 0.7 and better if 0.7 (Hair et al., 2013). Furthermore, the discriminant validity test was tested based on the value of the cross loading measurement with its construct (Abdillah and Hartono, 2015: 195).

**Tabel 2 Nilai *Outer Loading***

| | KI | KP | KPL | KM | KK | KIN |
|---|---|---|---|---|---|---|
| **KI1** | **0,779** | | | | | |
| **KI2** | **0,805** | | | | | |
| **KI4** | **0,757** | | | | | |
| **KI5** | **0,813** | | | | | |
| **KIN1** | | | | | | **0,853** |

| | | | | | | |
|---|---|---|---|---|---|---|
| **KIN2** | | | | | | **0,857** |
| **KIN3** | | | | | | **0,848** |
| **KK1** | | | | | **0,819** | |
| **KK2** | | | | | **0,804** | |
| **KK3** | | | | | **0,824** | |
| **KK4** | | | | | **0,835** | |
| **KK5** | | | | | **0,838** | |
| **KM1** | | | | **0,832** | | |
| **KM2** | | | | **0,798** | | |
| **KM3** | | | | **0,829** | | |
| **KM4** | | | | **0,849** | | |
| **KP1** | | **0,696** | | | | |
| **KP2** | | **0,668** | | | | |
| **KP3** | | **0,694** | | | | |
| **KP4** | | **0,738** | | | | |
| **KP5** | | **0,708** | | | | |
| **KP6** | | **0,814** | | | | |
| **KP7** | | **0,823** | | | | |
| **KP8** | | **0,808** | | | | |
| **KPL1** | | | **0,747** | | | |
| **KPL2** | | | **0,730** | | | |
| **KPL3** | | | **0,793** | | | |
| **KPL4** | | | **0,780** | | | |
| **KPL5** | | | **0,701** | | | |

The measurement results of the above model after eliminating the KI3 indicator, show that the correlation between the indicators and their variables is discriminantly valid. The loading factor value of each indicator has met the requirements above 0.4, which can be seen in table 4.4.

**Table 3 Cross Loading Value**

| | **KI** | **KP** | **KPL** | **KM** | **KK** | **KIN** |
|---|---|---|---|---|---|---|
| **KI1** | **0,779** | 0,52 | 0,461 | 0,414 | 0,517 | 0,476 |

| | | | | | | |
|---|---|---|---|---|---|---|
| **KI2** | **0,805** | 0,598 | 0,5 | 0,505 | 0,495 | 0,431 |
| **KI4** | **0,757** | 0,556 | 0,535 | 0,451 | 0,515 | 0,474 |
| **KI5** | **0,813** | 0,589 | 0,467 | 0,641 | 0,693 | 0,559 |
| **KIN1** | 0,514 | 0,629 | 0,527 | 0,496 | 0,732 | **0,853** |
| **KIN2** | 0,603 | 0,592 | 0,461 | 0,497 | 0,714 | **0,857** |
| **KIN3** | 0,473 | 0,54 | 0,424 | 0,471 | 0,717 | **0,848** |
| **KK1** | 0,573 | 0,574 | 0,464 | 0,549 | **0,819** | 0,681 |
| **KK2** | 0,617 | 0,578 | 0,425 | 0,454 | **0,804** | 0,743 |
| **KK3** | 0,544 | 0,558 | 0,399 | 0,445 | **0,824** | 0,722 |
| **KK4** | 0,578 | 0,555 | 0,558 | 0,524 | **0,835** | 0,67 |
| **KK5** | 0,63 | 0,578 | 0,49 | 0,593 | **0,838** | 0,664 |
| **KM1** | 0,591 | 0,651 | 0,549 | **0,832** | 0,48 | 0,458 |
| **KM2** | 0,467 | 0,537 | 0,549 | **0,798** | 0,502 | 0,446 |
| **KM3** | 0,492 | 0,577 | 0,572 | **0,829** | 0,559 | 0,516 |
| **KM4** | 0,598 | 0,649 | 0,588 | **0,849** | 0,512 | 0,469 |
| **KP1** | 0,561 | **0,696** | 0,565 | 0,498 | 0,687 | 0,612 |
| **KP2** | 0,519 | **0,668** | 0,576 | 0,498 | 0,392 | 0,4 |
| **KP3** | 0,556 | **0,694** | 0,571 | 0,539 | 0,577 | 0,513 |
| **KP4** | 0,584 | **0,738** | 0,486 | 0,511 | 0,468 | 0,424 |
| **KP5** | 0,45 | **0,708** | 0,555 | 0,508 | 0,351 | 0,409 |
| **KP6** | 0,55 | **0,814** | 0,652 | 0,631 | 0,531 | 0,531 |
| **KP7** | 0,515 | **0,823** | 0,717 | 0,571 | 0,514 | 0,559 |
| **KP8** | 0,524 | **0,808** | 0,666 | 0,576 | 0,477 | 0,57 |
| **KPL1** | 0,376 | 0,662 | **0,747** | 0,458 | 0,389 | 0,391 |
| **KPL2** | 0,437 | 0,554 | **0,73** | 0,462 | 0,348 | 0,399 |
| **KPL3** | 0,541 | 0,648 | **0,793** | 0,532 | 0,419 | 0,433 |
| **KPL4** | 0,538 | 0,658 | **0,78** | 0,552 | 0,525 | 0,497 |
| **KPL5** | 0,407 | 0,492 | **0,701** | 0,553 | 0,418 | 0,332 |

Furthermore, for discriminant validity the table above shows that the correlation of the innovation capability variable with its indicators is higher than the correlation of the innovation capability indicator with other variables. This also applies to other construct-forming indicators, the correlation value is always higher than the correlation

of indicators with non-forming variables. This means that it can be said that each latent variable is able to predict the size of each block better than the size of the other blocks.

**Reliability Test**

The requirement to meet the reliability test is the value of Composite reliability 0.7 and Cronbach alpha 0.7. However, the value of Cronbach's alpha 0.6 is still acceptable (Hair et al., 2013).

**Tabel 4 *Composite Reliability* dan *Cronbach Alpha***

| Variabel | *Composite Reliability* | *Cronbach Alpha* |
|---|---|---|
| **KI** | 0,868 | 0,799 |
| **KP** | 0,909 | 0,886 |
| **KPL** | 0,866 | 0,807 |
| **KM** | 0,897 | 0,846 |
| **KK** | 0,914 | 0,882 |
| **KIN** | 0,889 | 0,812 |

Based on table 4.6 above, the value of Composite reliability for all constructs 0.7 and the value of Cronbach alpha for all constructs 0.7. Therefore, it can be concluded that all constructs have met the reliability requirements.

**Structural Model (inner model)**

**Variance Inflation Factor (VIF)**

The recommended VIF value is <10 or <5 and the recommended tolerance value is >0.10 or >0.20 to avoid multicollinearity (Ghozali & Latan., 2015:78).

**Tabel 5 Nilai VIF**

| | |
|---|---|
| **KI1** | 1,586 |
| **KI2** | 1,791 |
| **KI4** | 1,542 |
| **KI5** | 1,573 |
| **KIN1** | 1,745 |
| **KIN2** | 1,841 |
| **KIN3** | 1,771 |
| **KK1** | 2,158 |
| **KK2** | 1,906 |
| **KK3** | 2,155 |

| | |
|---|---|
| **KK4** | 2,247 |
| **KK5** | 2,340 |
| **KM1** | 2,216 |
| **KM2** | 1,879 |
| **KM3** | 2,003 |
| **KM4** | 2,333 |
| **KP1** | 1,727 |
| **KP2** | 1,633 |
| **KP3** | 1,989 |
| **KP4** | 1,952 |
| **KP5** | 2,080 |
| **KP6** | 2,462 |
| **KP7** | 3,697 |
| **KP8** | 3,284 |
| **KPL1** | 1,875 |
| **KPL2** | 1,932 |
| **KPL3** | 1,780 |
| **KPL4** | 1,809 |
| **KPL5** | 1,574 |

Based on the VIF value in the table above, there is no VIF value> 5, so there is no multicollinearity problem between research variables.

**Coefficient of Determination ($R^2$)**

**Table 6 Coefficient of Determination (R2)**

| **Variabel** | $R^2$ |
|---|---|
| Competitive Advantage | 0,586 |
| Performance | 0,739 |

Based on the table above, it can be explained that 58.6% of the competitive advantage variables can be explained by the variables of innovation capability, marketing capability, learning capability and managerial capability. Then, 73.9% of the MSME performance variables can be explained by the variables of innovation capability,

marketing capability, learning capability, managerial capability and competitive advantage. A high R2 value indicates that the predictive model of the research model is getting better (Abdillah and Hartono, 2015: 193).

**Predictive Relevance (Q2)**

According to Ghozali & Latan (2015:79), predictive relevance aims to validate the predictive ability of the model. The value of Q2 > 0 indicates that the exogenous latent variable is good or appropriate as an explanatory variable capable of predicting the endogenous variable, while the value of Q2 < 0 indicates that the model lacks predictive relevance. In this study, the value of Q2 is as follows.

**Table 7** ***Predictive Relevance***

| **Variabel** | **$Q^2$** |
|---|---|
| Competitive Advantage | 0,380 |
| Performance | 0,512 |

The table above shows the value of Q2 > 0 so it can be concluded that the model has predictive relevance or shows that the structural model designed to explain competitive advantage and performance in MSMEs is proven to be good or relevant.

**Hypothesis test**

Hypothesis testing aims to determine the level of significance of the influence of the independent variable on the dependent variable. In SmartPLS, the hypothesis is tested using the path coefficient. The path coefficient value shows the level of significance in hypothesis testing. The significance value is indicated by the t-statistic value which must be >1.96 and the P-value <0.05 to get significant results (Abdillah & Hartono., 2015:197).

**Tabel 8 Nilai** ***Path Coefficient***

| | *T Statistics* | *P Values* | Conclusion |
|---|---|---|---|
| KI → KIN | 0,531 | **0,593** | No direct effect |
| KI → KK | 3,657 | **0,000** | Direct effect |
| KP → KIN | 1,831 | **0,076** | No direct effect |
| KP → KK | 2,331 | **0,022** | Direct effect |
| KPL → KIN | 0,137 | **0,894** | No direct effect |
| KPL → KK | 0,421 | **0,682** | No direct effect |
| KM → KIN | 0,134 | **0,891** | No direct effect |

| | | | |
|---|---|---|---|
| KM → KK | 1,044 | **0,291** | No direct effect |
| KK → KIN | 7,765 | **0,000** | Direct effect |

The table above explains that with the t-statistical requirements > 1.96 and P <0.05 (significance 5%) then the direct relationship between innovation capability and marketing capability on MSME performance has no effect. In contrast to innovation capability and marketing capability to competitive advantage, these variables have a direct effect.

Different results were found in learning capabilities and managerial capabilities, the two variables did not have a direct effect on the performance of SMEs and on competitive advantage. The last variable, namely competitive advantage, is proven to directly affect the performance of MSMEs. Furthermore, to test the hypothesis is in the following table.

**Tabel 9** ***Specific Indirect Effect***

| | **T Statistics (\|O/STDEV\|)** | **P Values** | Conclusion |
|---|---|---|---|
| KI → KK → KIN | 3,489 | **0,001** | Supported |
| KP → KK → KIN | 2,258 | **0,029** | Supported |
| KPL → KK → KIN | 0,411 | **0,689** | Not supported |
| KM → KK → KIN | 0,981 | **0,317** | Not supported |

The test results on the first hypothesis show that the t statistic is 3.489 and the p value is 0.001. This result is declared to have a significant effect because the value meets the t statistic requirements > 1.96 and P < 0.05, **so the first hypothesis is accepted**. Then the results of testing the second hypothesis show that the t statistic is
2.258 and the p values are 0.024. In other words**, the second hypothesis is accepted** because the value meets the t statistic requirements > 1.96 and P < 0.05 so that it is declared to have a significant effect.

The test results on the third hypothesis show that the t-statistical value is 0.411 and the p-value is 0.681. In other words, the statistical requirements >1.96 and P<0.05 could not be met, so it was declared to have no significant effect. **So, the third hypothesis is rejected**. This proves that competitive advantage is not able to mediate the relationship between learning capability and SMEs performance. Finally, the fourth hypothesis shows that the t-statistical value in this test is 0.981 and p-value is 0.327, so it is declared not to have a significant effect because the statistical requirements >1.96 and P<0.05 cannot be met. **So, the fourth hypothesis is rejected**.

## CONCLUSION

This study aims to see whether the four capabilities of MSMEs have an influence on the performance of MSMEs with competitive advantage as a mediating variable. In this research, the capabilities studied are innovation capability, marketing capability, learning capability and managerial capability. This study uses competitive advantage as a mediator linking capability with performance. Replication of previous research, this study adds managerial capabilities that have not been explored in the context of MSMEs.

The results of this study provide evidence that the capability of SMEs to innovate is able to increase competitive advantage so that it affects performance. After testing the direct influence between innovation capability and MSME performance, it does not have a significant effect. That is, competitive advantage in this study is able to fully mediate the relationship between innovation capability and performance. This research is in line with research by Ratnawati et al (2018) which explains that the innovation process carried out by MSMEs that goes well will have an impact on competitive advantage and supports the resource based view (RBV) theory which emphasizes increasing competitive advantage that comes from the organization's strategic resources ( Dierickx and Cool, 1989). Competitive advantage allows companies to achieve superior performance over a certain period of time (Lei, Slocum and Pitts, 1999).

The result of further research is that marketing capability indirectly affects the performance of MSMEs through competitive advantage. After testing the direct influence between marketing capability and MSME performance, it turns out that marketing capability also does not have a significant effect. That is, competitive advantage in this study is able to fully mediate the relationship between marketing capabilities and performance. In market-oriented companies, the connected capabilities to understand the market and customers are at the core of creating competitive advantage (Day, 1994). Competitive advantage allows companies to achieve superior performance over a certain period of time (Lei, Slocumm and Pitts, 1999).

It should be remembered that the innovation and marketing capabilities that will affect the performance of MSMEs are those capable of generating competitive advantage. The results of this study prove that innovation capabilities and marketing capabilities do not directly affect performance, but through competitive advantage.

Furthermore, different research results were found in the third hypothesis. Learning capabilities have no effect on the performance of MSMEs either directly or through competitive advantage. Learning capabilities may not be so important in determining competitive advantage. Hooi's research (2020) found that learning capabilities are more

effective indirectly as an enabler that results in company performance through increasing learning orientation (Hooi, 2020). Thus, when using competitive advantage as a mediator, it has no effect on the relationship between learning capabilities and performance. Another factor that causes learning capability does not affect the performance of MSMEs, among others, the performance used in this study is financial performance. Prieto and Revilla (2006) show that learning capability has a positive effect on the non-financial performance of organizations.

Lastly, managerial capability also does not affect the performance of MSMEs either directly or through competitive advantage. Several studies consider managerial performance to play an important role in improving performance (Haber and Reichel, 2007), but in this study with the context of MSMEs in the city of Medan, most of the entrepreneurs still focus their efforts on product innovation and product marketing. This makes managerial capability in an MSME not yet considered important and takes a major role in business continuity.

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