

The Role of Business External Environment as a Moderation of the Effect of Entrepreneurial Orientation on Business Performance that is Mediated in Flexibility of Strategy

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Abstract: This study aims to examine the entrepreneurial orientation associated with business performance by incorporating flexibility strategies as mediation and the external environment of the business as moderation by taking studies in the small handicraft industry sector in East Java Indonesia. Data collection techniques used questionnaires distributed to UKM owners or managers of the craft sector as many as 198 entrepreneurs. The results of testing structural equation modeling with WarpPLS show that entrepreneurial orientation does not have a significant positive effect on business performance while entrepreneurial orientation on flexibility strategies has a significant positive effect. The results of the verification of the flexibility strategy mediate the relationship between entrepreneurial orientation to performance while the external business environment is not able to moderate the relationship between entrepreneurial orientation and performance.

Key words: Entrepreneurial orientation, flexibility strategy, business external environment, business performance, positive effect, WarpPLS

INTRODUCTION

Recent discussions and studies of entrepreneurial orientation are increasingly dynamic in various circles both academics and practitioners. Entrepreneurial orientation is seen as a strategy that must be possessed by entrepreneurs in order to win business competition Hitt *et al.*, 2009; Kuratko *et al.*, 2001; Lumpkin and Dess, 2001; Wiklund and Shepherd, 2005; Zahra and Garvis, 2000). Existing resources regardless of the various strengths or weaknesses that have become self-evaluation material to then be able to organize and take advantage of market opportunities (Barringer and Bluedorn, 1999; Brown and Eisenhardt, 2000; Ireland *et al.*, 2003; McCline *et al.*, 2000; Shane and Venkataraman, 2000; Teece, 1998; Wiklund and Shepherd, 2003; Zahra and Garvis, 2000.

The development of the concept of entrepreneurial orientation was also carried out by several previous researchers who viewed that entrepreneurial orientation consisted of three components, namely innovativeness, proactiveness and risk taking while other researchers viewed that entrepreneurial orientation is formed through five dimensions including autonomy, innovativeness, risk taking, proactiveness and competitive aggressiveness (Lumpkin and Dess, 1996). The dimensions developed by previous researchers are indicators that can translate

that entrepreneurial orientation can achieve extraordinary performance for the company (Lumpkin and Dess, 2001; Wiklund and Shepherd, 2003, 2005; Zahra and Covin, 1995; Zahra and Garvis, 2000).

The point of view in the context of entrepreneurship by making it into a business is a process and is a fundamental problem for entrepreneurs (Lumpkin and Dess, 1996). These problems occur mostly for beginners or novice business people because of their presence in the business arena from various reasons. Market misunderstanding is the next problem faced by novice entrepreneurs, business focus is based only on the ability to make products rather than looking at the needs and desires of the market, meaning that it is not preceded by looking at the market situation. The low ability to reduce the inability is still weak given the majority of the beginner's educational background is not high.

Various abilities that must be possessed by novice entrepreneurs are the ability to develop strategies in the face of competition including how an entrepreneur has an extensive network has good resources and organization has high innovation ability and internalization as a good work culture (Hitt *et al.*, 2001). The entry of the global era like this, the development of technology is a very decisive role for business conditions. The external business environment that is constantly evolving and full of

uncertainty requires a careful strategy, however there are still opportunities in uncertainty, the company must focus on identifying and exploiting these opportunities (Shane and Venkataraman, 2000). Entrepreneurship involves the process of identifying and exploiting opportunities in the external environment (Kuratko *et al.*, 2001; Zahra and Dess, 2001), the entrepreneurial mindset is very useful in photographing profits in uncertainty (McGrath and MacMillan, 2000).

Environmental uncertainty that occurs and is experienced by business people makes them increasingly depressed how to overcome such conditions. This means that such complex demands must be addressed immediately by business people through how to see existing resources in the organization and develop appropriate strategies to overcome the environmental uncertainty. Strategies for dealing with environmental change may be short-term which means that they only adjust to existing conditions but strategies can also be long-term when the strategy is prepared through information obtained both internally and externally by assessing the strengths that are owned.

Entrepreneurship orientation: Entrepreneurial orientation is defined as the process of developing an entrepreneurial strategy as a key decision maker by utilizing existing resources in order to achieve the objectives of its business organization (Rauch, 2010). In relation to individual abilities, entrepreneurial orientation is seen as an individual characteristic both as a company leader (manager) and as an owner who is able to overcome conditions of environmental uncertainty by innovating quickly. When viewed from the intrinsic point of view of an entrepreneur, it can be said that entrepreneurial orientation is a characteristic, trait and character that is inherent in a person as an individual who has a strong will to realize innovative ideas into real business and is able to develop it (Peter, 1994).

The definitions above are a small part of all components that are inherent in an entrepreneur. A successful entrepreneur is seen as a creative person, able to see and take advantage of business opportunities have a passion and be energetic, able to manage risk have broad insight, adaptable or flexible and not easily give up.

Various literature that empirically addresses entrepreneurial orientation questions such as Miller and Friesen (1982) that construct entrepreneurial orientation into five dimensions including adaptability, analytical ability, integration, ability to manage risk and the ability to produce innovative products. Meanwhile the view of entrepreneurial orientation as a personality (Littunen,

2000; Lee and Tsang, 2001; Olson, 2000), the view of entrepreneurship as achievement motivation (Littunen, 2000; Lee and Tsang, 2001) including ethical work, pursuit of excellence, mastery in business and dominance. Covin and Slevin (1989) construct three dimensions of entrepreneurship including proactive, risk-taking and innovative. Meanwhile, Lumpkind and Dess (1996) constructs entrepreneurial orientation into five dimensions including autonomy, proactiveness, risk-taking, competitive aggressiveness and innovativeness.

Empirical studies conducted by previous researchers by taking the setting of research objects in large-scale companies (Covin and Slevin, 1989) on SMEs and in other types of manufacturing, services or trade businesses. From various research results that have been done by previous researchers, different results are obtained, some of which prove that entrepreneurial orientation has a positive effect on the business performance of companies, some are not proven that entrepreneurial orientation positively influences business performance. Seeing these conditions, the authors developed the following hypothesis:

- H_1 : the higher the degree of entrepreneurial orientation, the higher the business performance of SMEs

Flexibility: Philosophical review in general from the strategists explained strategic that the company's strategic planning is reflected in the mission that is implementative and able to be translated into a defined business strategy. Some experts also mention that the strategy is a plan that is integrated, comprehensive and integrated by linking the company's advantages with a dynamic environment and is designed to ensure that the company's main objectives can be achieved through proper implementation (Jauch and Glueck, 1999). A dynamic and potentially changing environment requires hard thinking from the company to always adjust to changes. For some companies, flexibility in dealing with change can be adjusted while for some other companies, especially, small-scale changes that occur are a daunting challenge.

Some literature that examines the flexibility of strategy explains that the flexibility of strategy is the ability of a professional company leader, manager, educator, human resource development who has flexibility in decision making based on limited targets and time (Yawson and Greiman, 2017), even further Yawson and Greiman (2017) constructing strategic flexibility as a scenario tool and application tool for leaders in decision-making called the Strategic Flexibility Framework (SFF).

In the context of developing countries with the rapid dynamics of change, the quantity growth of companies both technology-based and non-technology, requires a leader to be able to see the situation. In the perspective of dynamic capability theory that the flexibility of strategy is defined as the company's ability to place and reformulate available resources, the implementation process and strategies in dealing with environmental changes (Yang *et al.*, 2015). The rapid ability of existing resources in responding to existing and effective and efficient environmental changes is strategic flexibility (Bock *et al.*, 2012; Sanchez, 1995, 1997; Yang *et al.*, 2015). The company's ability is not only based on merely adjusting strategies that are external to anticipation but also requires redefinition, strategy formulation (Sanchez, 1995), rotation of human resources, reviewing the budget and allocation and the required technology.

When observed small and medium scale companies that are not optimal in formulating strategies but the majority of them are able to anticipate change even though its nature is still for short-term needs to survive. Such a situation is identical with what happens to companies in developing countries, the conditions that exist in small and medium enterprises are still limited in the resources they have. Indeed the potential of small and medium-sized companies is very large and is able to improve business performance to be even higher. The existence of strategic flexibility can help companies overcome routines that make organizational performance dynamic (Gilbert, 2005; Sanchez, 1995; Yang *et al.*, 2015).

The ability to identify external conditions becomes important information material for later adapting to strategizing (Chakravarthy, 1982; Hanan and Freeman, 1977; Richard and Winter, 1982; Teece *et al.*, 1997). Considering the strategy is very closely related to the impact of both the company's performance and the risks arising from managerial and organizational decision making (Greve and Salaff, 2003); March and Shapira, 1987) regardless of whether the company is large, medium or small. Strategic flexibility carried out by the company is also a strategic step to achieve previously set goals in order to improve its business performance in accordance with the business philosophy (Covin and Slevin, 1989; Mu *et al.*, 2017; Mu and Benedetto, 2011; Theodosiou *et al.*, 2012; Venkatraman, 1989).

Strategic flexibility approach, according to some experts can be divided into two approaches among them are understood as manufacturing flexibility (operational approach) and strategic flexibility (strategic approach) (De Toni and Tonchia, 2005). Operational or manufacturing flexibility approaches are defined as the ability of the

manufacturing system of the company in adapting changes in the state of the environment, its processes and its needs (De Toni and Tonchia, 2005; Zhang *et al.*, 2003).

The above understanding is reinforced by Newman's *et al.* (1993) statement which states that manufacturing flexibility as a fundamental instrument for dealing with strong uncertainty. Balance in the context of flexibility against uncertainty can be represented through flexibility itself and the other is uncertainty (external: demand and supply, internal failure, lack of material and delay). Conceptually strategic flexibility is a consequent variable (effect) arising from an operating process and innovation.

The results of studies that develop the concept of flexibility strategy into three dimensions, among others, cost, time and quality with explicit visualization as a capacity of the company related to these three dimensions (Corbett and van Wassenhove, 1993). Meanwhile, other researchers developed into five dimensions including speed, consistency, sharpness, agility and innovation (Stalk *et al.*, 1992) explained that the flexibility strategy is a strategy configuration that is chosen from several existing options by looking at the level of competition and market space that can targeted according to specific competencies, knowledge and abilities.

The ability to adapt the flexibility strategy is also determined by how high the entrepreneurial orientation degree of an entrepreneur or company leader in facing the competition. If there is a high degree of entrepreneurial orientation it will be easy for an entrepreneur or company leader to adjust the strategies needed to win the competition. The main capital to become a market leader, one of which is always adjusting to the developments that exist both within the company and outside the business company. Referring to the above description, the following hypothesis can be developed:

- H_{2a}: the higher the degree of entrepreneurial orientation the higher the flexibility strategy
- H_{2b}: the higher the degree of flexibility of strategy, the higher the business performance of SMEs
- H_{2c}: the flexibility strategy mediates the relationship between entrepreneurial orientation and SME business performance

Business external environment: Environment is everything that is outside the organization (Robbins, 1994). According to Smircich and Stubbart (1985), Mansfield, (1990) by Ian and Weatherston (1997), environmental definitions have intellectual problems, so, researchers categorize them with different approaches. In

the context of strategic management, the environment is defined based on the proximity and distance of the environment of the organization or the direct and indirect environment that influences the organization.

The environment that is closest to the organization or also called the task environment, industry environment (Hitt *et al.*, 2001; Pearce and Robinson, 2003), specific environment (Robbins, 1994) is an environment that directly influences strategy including competitors, suppliers, customers and trade unions. Furthermore, the environment indirectly influences the strategy or is also called the general environment (Hitt *et al.*, 1995; Robbins, 1997), remote environment (Pearce and Robinson, 2003).

The external environment in fact can change conditions, considering many factors that influence it. Seeing these conditions become increasingly uncertain about the business continuity undertaken by business people. As a businessman facing such conditions is uncertain, a strategy is needed that can adjust to the dynamics that are even faster than what is done by competitors (Hooley and Beracs, 1997; Mason, 2007) not rigid with the initial strategy of the company by remaining at the forefront (Chakravarthy, 1997; Brown and Eisenhardt, 2000; Mason, 2007), always conduct evaluations to find out the shortcomings that exist and immediately correct them (Alf, 1995; Barnett and Burgelman, 1996; Mason, 2007) and anticipate enormous environmental changes through the application of flexibility strategies (Aaker and Mascarenhas, 1984; De Toni and Tonchia, 2005).

The developments and dynamics that occur outside the company describe uncertain conditions. Uncertainty, of environmental conditions that occur in the business world requires business people to map or identify factors that affect the company's performance. As much information as possible through the identification becomes the material to determine what steps will be taken in the future. On the basis of this information, companies can take action to build capacity and buffer against environmental impacts or to build relationships with stakeholders in their environment. To take successful action, they must do it effectively in analyzing the external environment (Hitt *et al.*, 2009).

Hill and Jones (2012) also stated that the starting point in the analysis of the external environment is to identify the industry where the company's competitors enter. In doing this, a manager must look at the basic needs of the customer in which the company serves it and they must be customer-oriented in their business as product-oriented as exposed in the following picture in relation to competing forces.

Pearce and Robinson (2003) suggests a model of an external business environment that influences an organization which consists of distant environments and industrial environments. Remote environment known as macro environment consists of legal and political power, technological power, economic power, social strength and ecological power.

The macro environment is also called the social environment or societal environment (Wheelen and Hunger, 2012), the remote environment (Pearce and Robinson, 2003), the macro environment (Hill and Jones, 2012). The social environment is a common force that is indirectly related to short-term organizational activities but can and often affects long-term decisions. The social environment in question is the strength of the economy, the power of technology, the power of law-politics and the strength of socio-culture (Wheelen and Hunger, 2012). Considering that the complexity of the environment is so large that it affects the company, the following hypothesis can be developed:

- H₃: the external environment moderates the in carrying out their duties and responsibilities in public accountability in the form of successes and shortcomings that occur

Performance is a function extent to which the results have been achieved should have a certain degree of willingness and level of ability. A person's willingness and skills are not effective enough to do something without a clear understanding of motivation and ability while to complete a task or job, someone influence of entrepreneurial orientation on SME business performance.

Business performance: Performance is a series of management activities that illustrate the of what to do and do it. Performance is a real behavior that is displayed by everyone as work performance produced by employees in accordance with their role in the company (Rivai, 2012). Performance is the achievement achieved by the company in a certain period that reflects the level of health of the company. Lee *et al.* (2001) divides performance based on:

- Quality performance consisting of the percentage of damaged products, returns and guarantees, damaged goods and reprocessing, etc
- Operating performance (operating performance) which consists of the average annual turnover rate and net profit last year
- Financial performance measured by ROA (Return on Assets)

Marketing performance as measured by the percentage of annual market share and sales performance as measured by an increase in the percentage of sales. Business performance is the overall performance of an organization that includes operational and financial performance. In general, business performance consists by Vijay and Tan (2003) namely market share, ROA (Return on Assets), overall product quality, overall customer service and overall competitive position. Business performance can also be divided into four types of performance measurement (Gonzalez-Benito *et al.*, 2009), namely:

- Profitability/economic performance of the company which consists of profit, margin, Return on Investment (ROI)
- Market response is a reaction to market demand which consists of sales, sales growth and market share
- Market position value, defined as achievement and favorable position in the consumer's mind, consisting of customer satisfaction, reputation, customer loyalty and image

New product success: Meanwhile, according to Venkatraman and Ramanujam (1986), it is said that business performance is distinguished on financial and operational performance. On the financial performance side, measured is the company's economic performance such as sales, profits and ROI. In terms of operational performance, the measured are customer satisfaction, quality and new product development phases (Gonzalez-Benito *et al.*, 2009).

Researchers recommend sales growth, employment growth, income growth and market share growth as the most important measure of small company performance (Kim and Choi, 1994; Lee and Miller, 1996; Luo and Peng, 1999; Miles and Covin, 2000; Hadjimanolis, 2000). This is also based on the argument that growth is a more appropriate and easily obtained indicator compared to financial performance indicators.

Another alternative opinion is that performance is multidimensional and therefore, it is useful to integrate different dimensions of performance in an empirical study (Lumpkin and Dess, 1996), it is appropriate to see financial performance and growth as different aspects of performance where each-It has important and unique information. Taken together growth and financial performance provide a richer description of the actual performance of the company when compared to using measurements individually.

Conceptual model: To provide a comprehensive picture in this study including to test concepts that can improve

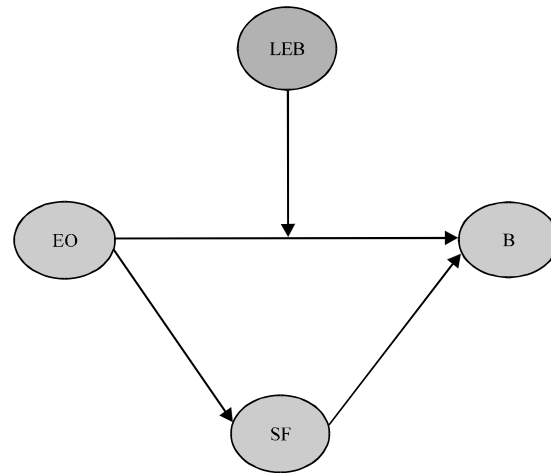


Fig. 1: Conceptual model

business performance through a knife analysis used both through entrepreneurial orientation directly or through mediation, namely the flexibility of the strategy or business environment as a moderating variable. To be easier to understand can be seen in Fig. 1.

MATERIALS AND METHODS

The population in this study is the craft sector SME industry, considering that this industry has the potential to develop new ideas and creativity that can be implemented as a result of new work. Apart from these results in the process using a technology approach or not (traditional). Meanwhile, considering the large population and uncertain numbers, according to the characteristics of this study, the sample is taken from a part of the population or as an analysis unit, namely the owner, manager or director of the UKM in the handicraft sector. The sampling technique used in this study was to use convenience sampling.

Collecting data in this study using a combination model that is by questionnaire (print) and through an online questionnaire (google form). Of the 212 questionnaires that have been distributed, the total number of questionnaires returned and the complete ones are 198 of the existing provisions, namely 5 X number of parameters (Hair *et al.*, 2010). As a justification of research results, data collection is also through interviews with respondents with the aim of confirming respondent's answers and digging up as much information as possible, so that, what happens to respondents in relation to their business can be clearly broken down.

Measurement: The measurement scale in this study uses a Likert scale with seven answer choices

(strongly disagree = 1 to strongly agree = 7) by adapting and developing from previous research. Before making measurements on the instruments that are made an expert judgment is made to provide suggestions for improvement on the instrument in addition to requests for advice from SMEs on the questionnaire to correct the understanding of the language, meaning and meaning of the sentences in the questionnaire. The number of items in the questionnaire was 18 items, after repeated tests and making improvements from the test results including suggestions from experts until the number of items became 18 statements.

After the measurement is done by testing the validity and reliability obtained the results of each item >0.60 as a condition for testing an instrument (Hair *et al.*, 2014) meanwhile for reliability testing using Cronbach alpha with a minimum limit of >0.60 from the test results obtained for the entrepreneurial orientation variable of 0.900 and the external business environment of 0.851 strategy flexibility of 0.861 and business performance of 0.801. Seeing the measurement results can be said to have met the specified limits in accordance with the rule of tumbs (Hair *et al.*, 2014).

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RESULTS AND DISCUSSION

Data analysis and results: After testing the instrument as a guideline to proceed with the data analysis process and obtained values that are in accordance with

Table 1: Combined loading and cross-loading

Indicators	EO	LEB	SF	KB	p-values
eo11	0.884	-0.033	0.044	-0.076	<0.001
eo12	0.808	0.357	0.126	0.010	<0.001
eo13	0.870	-0.318	0.056	0.051	<0.001
eo14	0.788	0.256	-0.114	-0.055	<0.001
eo15	0.874	-0.211	-0.114	-0.067	<0.001
leb11	0.733	0.661	0.126	0.022	<0.001
leb12	-0.169	0.902	-0.043	-0.001	<0.001
leb13	-0.134	0.906	0.021	-0.013	<0.001
leb14	-0.247	0.853	-0.074	-0.002	<0.001
sf1	-0.076	0.247	0.674	-0.134	<0.001
sf2	-0.060	0.001	0.841	0.158	<0.001
sf3	0.175	-0.066	0.846	0.041	<0.001
sf4	0.050	-0.197	0.823	-0.049	<0.001
sf5	-0.107	0.062	0.821	-0.045	<0.001
KB1	-0.052	-0.159	0.411	0.772	<0.001
KB2	-0.120	0.124	0.005	0.879	<0.001
KB3	-0.146	0.263	-0.242	0.809	<0.001
KB4	0.375	-0.284	-0.18	0.703	<0.001

EO = Entrepreneurial Orientation, LEB = External Business Environment, SF = Flexibility Strtegy, KB = Business performance

Table 2: Ave roots and correlation coefficients

Indicators	EO	LEB	SF	KB	LEB*EO
EO	0.846	0.662	0.543	0.271	-0.201
LEB	0.662	0.836	0.360	0.295	-0.541
SF	0.543	0.360	0.803	0.582	0.054
KB	0.271	0.295	0.582	0.793	0.009
LEB*EO	-0.201	-0.541	0.054	0.009	0.732

*Bold values are significant values

Table 3: Composite reliability and cronbach's alpha

Variables	Composite reliability coefficients	Cronbach's alpha coefficients
EO	0.926	0.900
LEB	0.902	0.851
SF	0.901	0.861
KB	0.871	0.801

the measurement provisions, then data analysis is carried out. In this study using partial least square analysis through the WarpPLS Software with the aim to test the concepts offered whether it can be proven to significantly improve business performance. To find out the following, the results of the measurement are presented first in order to check their validity and reliability. From Table 1, the loading factor value of each item > 0.30 and the p-value is <0.001, so, it can be said that the indicator has fulfilled convergent validity.

Table 2 shows the indicators on the instrument have fulfilled discriminant validity, this is known from the root value of AVE questionnaire with the correlation coefficient of the variable in question is greater than the value of the other AVE roots then it can be said to have fulfilled discriminant validity. When viewed from Table 3, the composite reliability has been fulfilled with a value of >0.70 and meets the internal reliability of consistency with values >0.60. Before interpreting the results of the test using partial least square with the WarpPLS approach, first the rule of thumb is presented to prove whether the measurement results meet the model fit and quality indices. If viewed from the numbers obtained after testing

Table 4: Rule of thumb model fit and quality indices

Model fit and quality indices	Results	p-values	Criteria
Average Path Coefficient (APC)	0.294	0.001	p<0.05
Average R ² (ARS)	0.325	0.001	p<0.05
Average Adjusted R ² (AARS)	0.318	0.001	p<0.05
Average block VIF (AVIF)	0.310	Ideal	Accepted if ≤5, ideally ≤3.3
Average Full Collinearity VIF (AFVIF)	2.061	Ideal	Accepted if ≤5, ideally ≤3.3
Tenenhaus GoF (GoF)	0.458	Ideal	Small ≥0.1, medium ≥0.25 large ≤0.36
Sympson's Paradox Ratio (SPR)	0.750	Accepted	Acceptable if ≥0.7, ideally = 1
R-Squared Contribution Ratio (RSCR)	0.989	Ideal	Acceptable if ≥0.7, ideally = 1
Statistical Suppression Ratio (SSR)	1.000	Accepted	Acceptable if ≥0.7
Nonlinear Bivariate Causality	0.750	Accepted	Acceptable if ≥0.7
Direction Ratio (NLBCDR)			

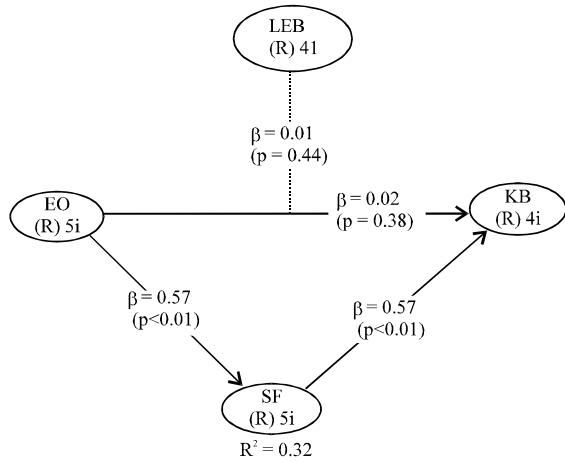


Fig. 2: Test results for structural models

in general has met the fit model, even seen from the criteria of acceptance, all models tested have met the specified criteria (fit) (Fig. 2).

The results of testing hypothesis as shown in Table 4 prove that hypothesis 1 predictions which state that entrepreneurial orientation has a significant influence on business performance is not proven, the value obtained is -0.022, so that, it can be said that the hypothesis is rejected, so, also when viewed from the p-value value there is a value the unacceptable is 0.378. Meanwhile, on the proof of hypothesis 2a which states that entrepreneurial orientation has an influence on strategic flexibility is proven, this is evidenced in the value ($\beta = 0.569$ and $p < 0.001$). Hypothesis 2b which states that the flexibility strategy has a significant effect on business performance is proven by obtaining values ($\beta = 0.572$ and $p < 0.001$). In proving the hypothesis 2c which states that strategic flexibility mediates the influence of entrepreneurial orientation on business performance, it is proven to mediate as evidenced by the value of multiple test tests where the estimated coefficient value (a) is 0.569 and estimated coefficient (b) is 0.572 for standard error (a) as big as 0.064 while the standard error

Table 5: Structural models

Hypothesis	Relations	Beta	p-values	Findings
H ₁	EO-KB	-0.220	0.378	Not supported
H _{2a}	EO-SF	0.569	<0.001	Supported
H _{2b}	SF-KB	0.572	<0.001	Supported
H _{2c}	EO-SF-KB	0.325	<0.001	Mediation
H ₃	EO-LEB-KB	0.010	0.435	Not moderation

EO: Entrepreneurial Orientation, SF: Strategic Flexibility, LEB: external business environment, KB: business performance

(b) is 0.064 while for the estimated coefficient value (c) of -0.022 with a significance of 0.378 it can be stated that there is a full mediation flexibility strategy (Sobel, 1982). Proof of hypothesis 3 which states that the business external environment moderates the influence of entrepreneurial orientation on business performance is not proven to moderate, this is seen from the small coefficient value ($\beta = 0.010$ and $p = 0.435$).

This study aims to examine the effect of entrepreneurial orientation on business performance that previously occurred a gap from the results of previous research. Therefore, in this study try to offer the concept of incorporating strategic flexibility as a mediating variable in improving business performance. Furthermore, in the same model also included the external business environment variable as a moderating variable to achieve superior business performance which was carried out in the craft sector SMEs in East Java.

Influence of entrepreneurial Orientation on business Performance

Performance: As illustrated in Table 5, entrepreneurial orientation has no significant effect on business performance and even negative. This finding is interesting as a study considering the entrepreneurial nature of SMEs, especially, the craft sector has unique characteristics, so that, the first hypothesis is not accepted, the results of this study are similar to what Frank *et al.*

We view that in the context of entrepreneurial orientation, the handicraft entrepreneurs have not implemented it, so, much even though these values are

actually a reflection of the entrepreneurial spirit itself. In many factors the success of a business is not determined only in the aspect of entrepreneurial orientation but greater than that namely the ability of soft skills that must be owned by business people.

The continuity of their business is obtained through various ways, so that, their business remains sustainable and even develops including building broader networks, community development and other marketing facilities. This condition is what makes SMEs in Indonesia really tough, this can be proven during the economic crisis in 1998 which toppled the economy in Indonesia with the decline in the value of the rupiah against the US dollar but this condition did not affect SMEs.

Effect of entrepreneurial orientation on strategic flexibility: In accordance with the actual conditions that indeed entrepreneurial orientation has a significant effect on strategic Flexibility in SMEs in Indonesia, especially, East Java. These results are consistent with previous research conducted (Covin and Slevin, 1989; Mu *et al.*, 2017; Mu and Benedetto, 2011; Theodosiou *et al.*, 2012; Venkatraman, 1989).

These results show that SME business people have strategic thinking related to anticipation of uncertain conditions in the market, the uncertainty of the situation has been thought of by SMEs. They are able to redefine planning in the event of market changes by adjusting to existing demand. They are also able to make modifications to both the product and the service, so that, the market can respond well of course with a touch of technology even though it is not yet dominant in this aspect, considering that SMEs in Indonesia have not in majority adjusted to technological sophistication.

The craft industry does require high creative power to produce quality, unique, futuristic and even antique products. So that, the work produced can truly reflect the high value of the product or product characteristics. This is what makes craftsmen in Indonesia always get a special place for the world market, the uniqueness that results from their best works

Strategic flexibility mediates the effect of entrepreneurial orientation on business performance: The next test is to prove that whether strategic flexibility mediates the influence of entrepreneurial orientation on business performance and proves that strategic flexibility is mediated. This shows that there is still a need for steps to improve business performance through strategic flexibility and this strategy is indeed very close to SME business people. Strategic flexibility is seen by SME business people as the most suitable strategy due to

uncertain market demand conditions and products produced by entrepreneurs are non-fabricated, so that, products are always created according to unique market demands.

Strategic flexibility is also seen as a simple strategy, considering that it is easy to adjust to existing conditions that are always changing. SME business actors themselves are able to see future product trends, targeted market segments up to their pricing are very able to adjust. This is what can make business people survive and improve their business performance.

Business external environment

Moderates the effect of entrepreneurial orientation on business performance: The existence of a moderator variable is whether it is able to strengthen the relationship between variables in factual to see whether it is able to improve results from before this does not occur in the results of this study that the external business environment does not moderate entrepreneurial orientation towards business performance. It can be explained that these results are in line with the actual conditions that the handicraft industry is not too dependent on government policy because products that are traded are not the primary sector which requires strict regulation.

Craft products have a broad segment, so, economic conditions are not a significant disruptive factor for entrepreneurs. Technology can be a factor that can affect the development of business work, so that, the products produced can compete with competitors. Socio-cultural factors are likely to provide contribution in improving the performance of handicrafts, considering that craft is very relevant to social and cultural aspects. Overall the external environment or in other studies mention that Peste is not able to strengthen the relationship between entrepreneurial orientation and business performance.

CONCLUSION

In this study there are interesting findings to be discussed, the first is that the existence of an entrepreneurial orientation towards business performance is not able to contribute in its relationship to improve business performance through entrepreneurial orientation among other factors in the context of the craft sector industry, this can be increased when raised strategic flexibility factor, considering that the strategy is very possible to be done by SME business people and the strategy does not require heavy thinking for businesses considering the limited resources they have. The flexibility that is meant by business actors is the ability to always

adjust to the developments or dynamics that exist in the market and see the structure of demand and market response.

Second that the existence of the external business environment for them is not able to boost the improvement of their business performance because in principle they see that the external environment is the initial door to be able to do market scanning. So that, the conditions for the principals are definitely taken into account before hand in other words the basic conditions for them to build, develop and improve their business performance.

IMPLICATIONS

This research provides a significant contribution to the development of the theory of entrepreneurial orientation, strategic flexibility, external business environment that has an impact on improving business performance in the context of SME entrepreneurs in the handicraft sector in Indonesia, especially, East Java. In practical terms, the strategy carried out by SME businessmen, so far is based on intuition, considering that the level of education of SME entrepreneurs in Indonesia is still low, only a portion of those with high education.

For SMEs, strategic flexibility is the right step in increasing business growth where this strategy is always able to adjust to the existing market developments. Strategic flexibility implementation can provide a perspective on how an SME entrepreneur must always be observant in looking at future changes and then again formulate strategies. The advantage of this strategy is that it always changes along with the pattern of change because they assess the scope of the target market is limited to the segment. The results of this study open up an overview for SMEs to return to re-orientation strategies that have only been intuition-based or only tactically to change by implementing flexibility strategies to achieve maximum performance.

This study also has implications for their ability to minimize the costs incurred to conduct open competition against rival companies. We believe that the flexibility strategy is very suitable to be applied to SME business players in Indonesia, especially, East Java, especially, the handicraft industry is very popular with both national and international markets.

LIMITATIONS

As with other studies discussing entrepreneurial orientation, there are still many limitations, considering that it is not able to answer everything needed to improve

its performance. First, the scope of this research is still limited to the East Java region, although, it is able to provide an initial picture of Indonesia in the context of SME business but it does not reflect factually covering Indonesia as a whole. Secondly, the cross sectional research approach also leaves a weakness considering that conditions that can quickly change at any time, so that, consistency still leaves debate. Third, the findings in this study view that the external business environment has not been able to boost SME business performance, testing the external business environment is not able to moderate entrepreneurial orientation to business performance.

RECOMMENDATIONS

Our recommendation to do the next research is that it is necessary to include absorptive capacity variables as mediating and moderating variables related to the relationship between entrepreneurial orientation and business performance. Absorptive capacity is important to be included in the next research model, considering that these variables are closely related to the ability of SME entrepreneurs to view information that develops in the market can be transformed which in turn is able to create new products according to market demand. The concept is closely related to the craft industry which in fact an SME entrepreneur must always have high creative power.

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