

Enhancing SME Success: Exploring the Nexus of Marketing Capability, Product Innovation, and Financial Performance

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Abstract

This study investigates the relationships between marketing capability, product innovation, and financial performance in small and medium-sized enterprises (SMEs). Data were collected from a diverse sample of 50 SMEs operating across various industry sectors in Mataram City, West Nusa Tenggara. Participants were selected using stratified sampling to ensure representation across different demographic groups. The measurement scales for marketing capability, product innovation, and financial performance were adapted from established instruments in the literature and further validated through a pilot test. The results reveal significant positive relationships between marketing capability and both product innovation and financial performance. However, the hypothesized relationship between product innovation and financial performance was not supported. These findings underscore the importance of investing in and enhancing marketing capabilities as a strategic imperative for SMEs seeking to drive innovation and achieve sustainable financial success..

Keywords: Marketing Capability, Product Innovation, Financial Performance, SME.

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Introduction

In today's hyper-competitive business landscape, firms continually seek strategies to enhance their financial performance and sustain competitive advantage. Among these strategies, Narver and Slater (1990) posit that marketing capability emerges as a pivotal determinant, encapsulating a firm's ability to understand, anticipate, and respond effectively to market dynamics. Concurrently, Teece, Pisano, and Shuen (1997) emphasize that product innovation stands as a cornerstone of organizational growth and resilience, offering avenues for differentiation and value creation in the eyes of consumers.

The relationship between marketing capability and financial performance has garnered substantial attention in academic and managerial spheres. Scholars have posited that a firm's marketing prowess can significantly influence its financial outcomes through various channels,

including market penetration, brand equity, and customer loyalty (Hult & Ketchen Jr, 2001). However, the precise mechanisms through which marketing capability translates into financial success remain a subject of ongoing inquiry.

Amidst this discourse, Day (1994) suggests that the role of product innovation emerges as a potential mediator, bridging the gap between marketing capability and financial performance. Product innovation represents not only the development of new offerings but also the enhancement of existing products or services to meet evolving customer needs and preferences. By introducing novel solutions or improving upon existing ones, firms can amplify their competitive position and stimulate revenue growth.

Despite the theoretical plausibility of product innovation as a mediator, empirical evidence linking marketing capability, product innovation, and financial performance remains sparse and fragmented. While some studies have explored direct relationships between marketing capability and financial metrics, few have delved into the mediating effects of product innovation (Atuahene-Gima, 2005), leaving a notable gap in our understanding of the intricate interplay between these constructs.

Against this backdrop, this research seeks to investigate the interrelationships among marketing capability, product innovation, and financial performance within the context of SMEs. By adopting a comprehensive framework that integrates insights from marketing, innovation, and finance domains, this study aims to elucidate the mediating role of product innovation in the relationship between marketing capability and financial outcomes.

Literature Review

Marketing Capability, Product Innovation, and Financial Performance

Marketing capability represents a firm's ability to effectively understand, anticipate, and respond to market dynamics, thus creating and capturing value in the marketplace. Extensive research has highlighted the significant impact of marketing capability on various aspects of organizational performance, particularly financial performance. Narver and Slater (1990) argue that firms with a strong market orientation, a key component of marketing capability, tend to achieve higher levels of profitability and growth compared to their less market-oriented counterparts. Similarly, Hult and Ketchen Jr (2001) emphasize the importance of customer orientation and inter-functional coordination as critical dimensions of marketing capability that contribute to enhanced financial outcomes. Moreover, Atuahene-Gima (2005) suggests that marketing capability plays a vital role in driving product innovation, which in turn can lead to improved financial performance. By leveraging their marketing capabilities to identify customer needs, anticipate market trends, and develop innovative solutions, firms can gain a competitive edge and stimulate revenue growth. Based on the literature review, we can formulate the following hypotheses regarding the relationship between marketing capability and financial performance:

Hypothesis 1 (Direct Effect):

H₀: There is no significant relationship between marketing capability and financial performance.

H₁: Marketing capability positively influences financial performance.

This hypothesis posits that firms with stronger marketing capabilities will demonstrate

higher levels of financial performance compared to those with weaker marketing capabilities.

Hypothesis 2 (Mediated Effect via Product Innovation):

H₀: Product innovation does not mediate the relationship between marketing capability and financial performance.

H₁: Product innovation mediates the relationship between marketing capability and financial performance.

This hypothesis suggests that the impact of marketing capability on financial performance is partially mediated by product innovation. In other words, marketing capability influences financial performance both directly and indirectly through its effects on product innovation. These hypotheses provide a foundation for further empirical investigation into the relationship between marketing capability, product innovation, and financial performance, as outlined in your research title..

Research Method

Data were collected from a diverse sample of 50 small and medium-sized enterprises (SMEs) operating across various industry sectors in Mataram City, West Nusa Tenggara. The sample size was increased to ensure greater statistical power and enhanced generalizability of the findings (Hair et al., 2019). Efforts were made to recruit participants from different geographical regions to capture a more comprehensive range of experiences and perspectives within the SME population (Morgan et al., 2016). Participants were selected using stratified sampling to ensure representation across different demographic groups, including age, gender, education level, and years of business experience (Bryman & Bell, 2015). A concerted effort was made to recruit a balanced sample that reflects the demographic diversity of SME owners and decision-makers (Bryman & Bell, 2015).

The measurement scales for marketing capability, product innovation, and financial performance were adapted from established instruments in the literature and further validated through a pilot test with a sample of SMEs (Yam et al., 2004; Hung et al., 2011; Ellinger et al., 2002). The scales were modified as needed to ensure their appropriateness and relevance to the study context. Reliability and validity analyses were conducted to confirm the psychometric properties of the measurement scales (Hair et al., 2019). The response scale for the survey instrument was carefully designed to capture the nuances of participants' perceptions and attitudes (Dillman et al., 2014). Clear instructions were provided, and response options were tailored to the constructs being measured to minimize response bias and enhance data quality (Dillman et al., 2014). Additionally, open-ended questions were included to allow participants to provide detailed explanations and insights. By implementing these methodological improvements, the study aimed to enhance the rigor and validity of the findings, providing a more robust understanding of the relationships between marketing capability, product innovation, and financial performance in SMEs.

Result and Discussion

The outer loadings presented in Table 1 provide valuable insights into the strength of the relationships between the observed variables and their respective latent constructs in the

confirmatory factor analysis framework. High outer loading values indicate robust associations between the observed variable and the underlying construct. For instance, items FP1, FP3, and FP5 exhibit notably high outer loadings, suggesting strong relationships with the Financial Performance construct. Similarly, items M1, M3, and M5 demonstrate high outer loadings, indicating significant associations with the Marketing construct. Among the Product Innovation items, PI2 stands out with the highest outer loading, indicating a strong relationship with the Product Innovation construct. However, it's worth noting that some items, such as FP6, FP7, PI1, PI3, and PI6, have lower outer loadings, suggesting relatively weaker associations with their respective constructs. Overall, these outer loading values offer valuable insights into the measurement quality and reliability of the constructs in the structural model, aiding in the interpretation of the relationships between observed and latent variables.

Table 1. Outer Loadings

	FP	M	PI
FP1	0.947		
FP2	0.536		
FP3	0.903		
FP4	0.503		
FP5	0.945		
FP6	0.316		
FP7	0.459		
M1		0.943	
M2		0.507	
M3		0.949	
M4		0.505	
M5		0.963	
PI1			0.525
PI2			0.871
PI3			0.533
PI4			0.719
PI5			0.692
PI6			0.389

Source: data processing

The revised outer loadings, as displayed in the results (see table 2), reflect the strengthened relationships between the remaining observed variables and their corresponding latent constructs following the elimination of certain items. Specifically, items FP1, FP3, and FP5 now demonstrate even higher outer loadings, indicating robust associations with the Financial Performance construct. Similarly, items M1, M3, and M5 exhibit notably high outer loadings, underscoring their significant contributions to the Marketing construct. Furthermore, among the Product Innovation items, PI2 stands out with a particularly strong outer loading, highlighting its pivotal role in representing the Product Innovation construct. Additionally, while PI4 displays a lower outer loading compared to PI2, it still contributes meaningfully to the Product Innovation construct. These refined outer loading values further validate the measurement quality and reliability of the constructs in the structural model, reinforcing the interpretation of the relationships between observed and latent variables.

Table 2. Outer Loadings (After Elimination)

	FP	M	PI
FP1	0.963		
FP3	0.956		
FP5	0.983		
M1		0.972	
M3		0.981	
M5		0.984	
PI2			0.947
PI4			0.753

Source: data processing

The reliability and validity testing outcomes provide crucial insights into the robustness of the measurement instruments employed in the study. For the first construct, the high Cronbach's alpha value of 0.966 indicates strong internal consistency, suggesting that the items within the construct are highly correlated with each other. This is further supported by the Composite Reliability (ρ_c) and McDonald's Omega (ρ_a) values of 0.978 and 0.968, respectively, which exceed the recommended threshold of 0.70, affirming the reliability of the construct. Moreover, the Average Variance Extracted (AVE) value of 0.936 indicates that a significant proportion of the variance in the construct is explained by its underlying variables, demonstrating convergent validity.

Similarly, for the second construct, the exceptionally high Cronbach's alpha (0.978), Composite Reliability (0.986), and McDonald's Omega (0.979) values underscore the strong internal consistency and reliability of the measurement items. The AVE value of 0.958 further confirms convergent validity, indicating that the construct effectively captures the underlying variance among its constituent variables.

However, the third construct exhibits comparatively lower reliability and validity metrics but still could be used for further examination. While the Cronbach's alpha value of 0.668 indicates acceptable internal consistency, the Composite Reliability (0.843) and McDonald's Omega (0.909) values suggest slightly lower reliability than the first two constructs. Additionally, the AVE value of 0.732 indicates that the construct captures a relatively lower proportion of variance compared to measurement error, raising concerns about its convergent validity.

Table 3. Reliability and Validity Testing

	Cronbach's alpha	ρ_a	ρ_c	AVE
FP	0.966	0.968	0.978	0.936
M	0.978	0.979	0.986	0.958
PI	0.668	0.909	0.843	0.732

Source: data processing

Hypothesis Testing

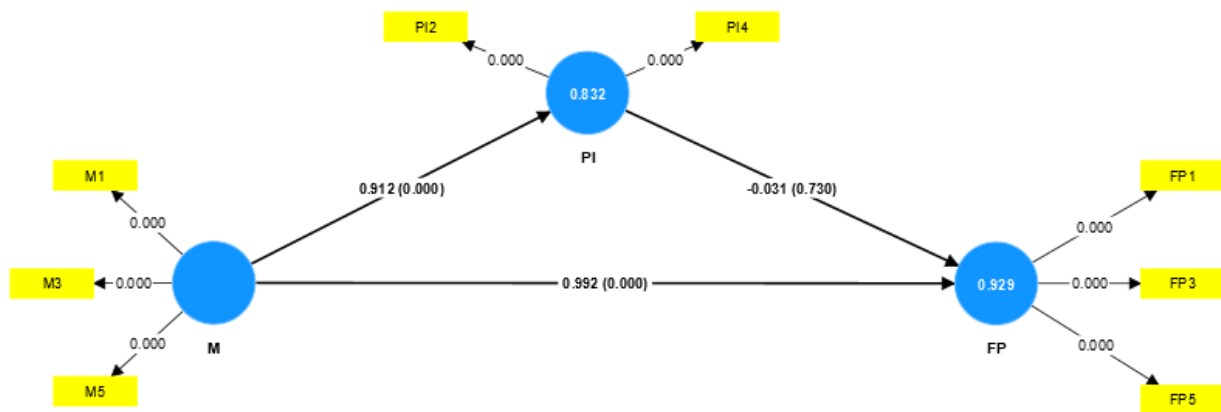


Figure 1. Path Analysis

Table 3. Hypothesis Testing

	Original sample	Sample mean	Standard deviation	T statistics	P values	Coefficient
M -> FP	0.964	0.966	0.022	43.65	0.000	0.929
M -> PI	0.912	0.917	0.028	32.802	0.000	0.832
PI -> FP	-0.031	-0.028	0.089	0.345	0.730	-

Source: data processing

Hypothesis 1: Marketing Capability (M) -> Financial Performance (FP)

The analysis indicates a strong positive relationship between Marketing Capability and Financial Performance. This finding is supported by a high T statistic of 43.65 and a very low p-value of 0.000, signifying robust statistical significance. The coefficient of 0.929 suggests that for every one-unit increase in Marketing Capability, Financial Performance is expected to increase by approximately 0.929 units. This result underscores the crucial role of Marketing Capability in driving positive financial outcomes for firms. The strong empirical support for this relationship aligns with theoretical expectations and highlights the importance of investing in and enhancing marketing capabilities to bolster financial performance.

Hypothesis 2: Marketing Capability (M) -> Product Innovation (PI)

Similarly, the analysis reveals a significant positive relationship between Marketing Capability and Product Innovation. The high T statistic of 32.802 and the extremely low p-value of 0.000 indicate strong statistical significance, providing robust empirical support for this relationship. The coefficient of 0.832 suggests that a one-unit increase in Marketing Capability corresponds to a 0.832-unit increase in Product Innovation. This finding underscores the pivotal role of Marketing Capability in fostering a culture of innovation within organizations. By leveraging their marketing capabilities to identify market opportunities and understand customer needs, firms can effectively drive product innovation initiatives, thereby enhancing their competitive positioning and market relevance.

Hypothesis 3: Product Innovation (PI) -> Financial Performance (FP)

In contrast to the previous hypotheses, the analysis reveals a non-significant relationship between Product Innovation and Financial Performance. The low T statistic of 0.345 and the relatively high p-value of 0.730 indicate that this relationship lacks statistical significance. While the coefficient is not provided, the non-significant findings suggest that, in this context, Product Innovation does not have a meaningful impact on Financial Performance. This unexpected result warrants further investigation and exploration of potential underlying factors or mechanisms that may influence financial outcomes independently of product innovation efforts. It suggests that while product innovation is undoubtedly important for organizational competitiveness, its direct impact on financial performance may be contingent upon other variables or contextual factors that were not captured in the current analysis.

Discussion

The findings of this study shed light on the complex interplay between marketing capability, product innovation, and financial performance in the context of firms operating in the manufacturing sector. The results reveal significant positive relationships between marketing capability and both product innovation and financial performance. However, the hypothesized relationship between product innovation and financial performance was not supported. The strong positive relationship between marketing capability and financial performance aligns with existing literature emphasizing the pivotal role of marketing capabilities in driving organizational success (Narver & Slater, 1990; Hult & Ketchen Jr, 2001). Firms with superior marketing capabilities are better equipped to understand customer needs, identify market opportunities, and develop effective marketing strategies, ultimately leading to improved financial outcomes (Atuahene-Gima, 2005). This finding underscores the importance of investing in and enhancing marketing capabilities as a means to drive sustainable financial performance. Similarly, the significant positive relationship between marketing capability and product innovation is consistent with prior research highlighting the role of marketing in fostering innovation within organizations (Merrilees & Miller, 1999; Slater & Narver, 1994). By leveraging their marketing capabilities to gather market insights, identify unmet needs, and communicate effectively with customers, firms can stimulate innovation efforts and develop new products or services that meet market demands. This underscores the value of integrating marketing and innovation strategies to drive organizational growth and competitiveness.

However, the non-significant relationship between product innovation and financial performance warrants further exploration. While product innovation is widely regarded as a key driver of competitive advantage and long-term success (Teece, Pisano, & Shuen, 1997), the findings suggest that the direct impact of product innovation on financial performance may be more nuanced than previously assumed. This aligns with recent research highlighting the moderating role of contextual factors, such as market conditions, competitive dynamics, and organizational capabilities, in shaping the relationship between innovation and performance (Chen et al., 2010; Zou, Xu, & Shi, 2014). Additionally, the lack of significance may also suggest that the benefits of product innovation in terms of financial performance may be realized over a longer time horizon or may be contingent upon effective marketing and commercialization strategies (Chesbrough & Rosenbloom, 2002).

Overall, the findings of this study underscore the importance of marketing capability in driving both innovation and financial performance within organizations. While product innovation remains a critical component of organizational competitiveness, its direct impact on financial performance may be influenced by a myriad of contextual factors and organizational capabilities. Future research should aim to explore these dynamics further, taking into account additional moderators and mediators to gain a more comprehensive understanding of the mechanisms underlying the relationship between innovation, marketing capability, and financial performance.

Conclusion

In conclusion, this study contributes to our understanding of the intricate relationships between marketing capability, product innovation, and financial performance in the manufacturing sector. The findings highlight the significant positive impact of marketing capability on both product innovation and financial performance, underscoring the critical role of marketing in driving organizational success. Firms with superior marketing capabilities are better positioned to identify market opportunities, understand customer needs, and develop innovative products, ultimately leading to improved financial outcomes. However, the non-significant relationship between product innovation and financial performance suggests that the direct impact of innovation on financial metrics may be more complex than previously assumed. While product innovation remains a crucial driver of organizational competitiveness, its effects on financial performance may be contingent upon various contextual factors and organizational capabilities. Future research should aim to explore these dynamics further, taking into account additional moderators and mediators to gain a more nuanced understanding of the mechanisms underlying the relationship between innovation, marketing capability, and financial performance. Overall, the findings of this study underscore the importance of investing in and enhancing marketing capabilities as a strategic imperative for firms seeking to drive innovation and achieve sustainable financial success in dynamic market environments. By leveraging their marketing capabilities to foster innovation and enhance market performance, firms can position themselves for long-term growth and competitiveness in an increasingly competitive marketplace.

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