

# CHAPTER I

## INTRODUCTION

### A. Research Background

Micro, Small, and Medium Enterprises (MSMEs) are the leading foundation of the community's economic sector, which accommodates both formal and informal workforce and plays a role in a country's Gross Domestic Product (GDP). A similar thing is also experienced in Indonesia, where MSMEs are one of the pillars of the Indonesian economy (Limanseto, 2021). DATABOKS (2021) states that MSMEs contribute 60.51% to gross domestic product (GDP). The Governor of Bank Indonesia, who expressed this in the webinar, said that MSMEs are one of the factors driving the Indonesian economy. This was marked when Indonesia experienced an economic crisis in 1998 and 2008. The MSMEs sector was crucial in driving the economy during this financial crisis (Administrator, 2021). Therefore, MSMEs play an essential role in improving Indonesia's economy.

The success of the MSMEs sector in supporting economic growth has encouraged the Indonesian government to continue to develop it. The government is committed to creating financial independence and community welfare by prioritizing the MSMEs sector (Limanseto, 2021), according to INDONESIA.GO.ID (2021) shows clear evidence of Indonesia's impressive economic growth. In the second quarter of 2021,

Indonesia recorded an increase of 7.07%, the highest growth in the last 16 years. This indicates that support and development of MSMEs create economic stability and encourage significant economic growth, providing hope for a brighter future for the Indonesian people.

The increasing number of MSMEs is the reason for creating competitive advantages. The conditions that arise in MSMEs above require the development of new patterns in marketing their products (Zahara et al., 2023). To increase competitive advantage, MSMEs must think and act more broadly by concentrating on customer orientation capabilities (Zehir et al., 2015). In this case, a customer-oriented business will focus on creating value and prioritizing customer interests. Customer orientation also requires competitor orientation to analyze the competitive environment (Lengler et al., 2013). Thus, MSMEs that can combine customer orientation and competitor orientation will have a solid competitive advantage in an ever-changing market.

One crucial factor that influences increasing competitive advantage in MSMEs is competitor orientation. To remain viable and competitive, MSMEs must deeply understand their competitive environment. By adopting a competitor orientation, MSMEs can better analyze competitor actions, industry trends, and market opportunities (Aydin, 2021). Competitor orientation helps MSMEs identify their competitors' strengths and weaknesses and explore opportunities to market digitally in marketing

strategies. Therefore, digital marketing is crucial in increasing MSMEs' business (Zahara et al., 2023).

Leveraging digital marketing capabilities is another factor in creating a competitive advantage for MSMEs. MSMEs must be able to utilize digital platforms and technology in the current era of digitalization to increase the market for their products (Kilay et al., 2022). MSMEs can do this to increase their competitiveness and face increasingly fierce market competition (Hallak et al., 2018). Besides that, innovation also influences the effectiveness of digital marketing technology and aims to meet business needs. Thus, MSMEs are expected to achieve a stronger market position by utilizing digital technology and innovation in their marketing strategies (Kuntonbutra et al., 2019).

To remain competitive, MSMEs must make innovation the main factor. This is necessary to outperform their competitors in the market. MSMEs must be innovative, creative, and highly resilient to market dynamics because this is the key to managing difficulties and achieving business success (Hallak et al., 2018). This innovation process is the foundation that strengthens marketing performance in facing business challenges and contributes significantly to driving the business towards further development (Crick & Crick, 2016). With proper use, the ability to innovate can improve marketing performance and help companies to grow better so that MSMEs can maintain their competitiveness in the market (L. Wang et al., 2021).

MSMEs need to have the ability to develop in marketing performance. High marketing performance is crucial because it can determine the company's survival. Without high marketing performance, a company's survival is mainly determined by the effectiveness of a company's creativity, innovation, and industry experience (Hallak et al., 2018). Increasing marketing performance is influenced by market orientation and management's ability to act as an enabling mechanism for building marketing capabilities (Riswanto et al., 2020). In other words, a strong market orientation can positively influence a company's marketing performance.

One tangible example of MSMEs that stand out and have the potential to grow is Solo City, a city in Central Java Province. In Central Java, the city of Solo experienced the most significant growth in the number of MSMEs compared to other towns and districts. The development of MSMEs operating in Solo City is considered to have good prospects in the future (Hutahayan, 2021). The impact on MSMEs can be seen from the increasingly tight trade competition in Solo (Ardhi & Mulyo, 2021). The data can be seen in Table 1.1, which presents the number of MSMEs, with the highest number being five per Regency/City in Central Java Province.

Table 1.1 MSMEs Data per Regency/City

<b>Regency/City</b>	<b>Amount of MSMEs</b>
Surakarta (Solo)	17.964 units
Demak	13.027 units
Kebumen	11.992 units
Semarang	11.922 units

Regency/City	Amount of MSMEs
Banyumas	8.564 units

Source data: Cooperative Department of MSME in Central Java (<https://satudata.dinkop-umkm.jatengprov.go.id/data/umkm>)

Based on the data above, the total number of MSMEs in Solo City reached 17,965 units. Solo leads the ranking of the number of MSMEs in Central Java Province (MSMEs Data, 2024). Moreover, the fashion industry in Solo is starting to show signs of recovery. However, intense competition underscores the need for MSMEs actors, especially in the fashion industry, to work hard and take strategic steps to maintain relevance and competitiveness amidst dynamic changes in the industry (Fares et al., 2023).

Based on this context, this research aims to determine the relationship between customer orientation and competitor orientation of MSMEs with marketing performance in Solo by replicating it with modifications from previous journals. This research will explore the role of digital marketing capability and innovation capability, which can influence the connection between customer orientation, competition orientation, and marketing performance of MSMEs in Solo City. Therefore, this research seeks to provide a deeper understanding of the factors that influence the marketing success of MSMEs amidst intense competition (Udriyah et al., 2019). The results of this research can contribute to developing a more effective marketing strategy for MSMEs in Solo City to improve overall marketing performance.

## **B. Research Question**

Based on the growth of the MSMEs industry, the formulation of the problem in this study is how to improve the marketing performance of MSME actors in the city of Solo. For this reason, research questions can be formulated, namely:

1. Does customer orientation influence digital marketing capabilities?
2. Does customer orientation influence innovation capability?
3. Does competitor orientation influence digital marketing capability?
4. Does competitor orientation influence innovation capability?
5. Does digital marketing capability influence marketing performance?
6. Does innovation capability influence marketing performance?
7. Does digital marketing capability mediate the relationship between customer orientation and marketing performance?
8. Does digital marketing capability mediate the relationship between competitor orientation and marketing performance?
9. Does innovation capability mediate the relationship between customer orientation and marketing performance?
10. Does innovation capability mediate the relationship between competitor orientation and marketing performance?

## **C. Research Objectives**

Based on the formulation of the problems outlined above, there are various purposes, such as:

1. To test the influence of customer orientation on digital marketing capability.
2. To determine the influence of customer orientation on innovation capability.
3. To find the influence of competitor orientation on digital marketing capability.
4. To investigate the influence of competitor orientation on innovation capability.
5. To examine the effect of digital marketing capability on marketing performance.
6. To determine the effect of innovation capability on marketing performance.
7. To analyze the influence of digital marketing capability in mediating the relationship between customer orientation and marketing performance.
8. To test the influence of digital marketing capability in mediating the relationship between competitor orientation and marketing performance.
9. To find the influence of innovation capability in mediating the relationship between customer orientation and marketing performance.

10. To analyze the influence of innovation capability in mediating the relationship between competitor orientation and marketing performance.

#### **D. Research Benefit**

The results of this research are expected to be beneficial for interested parties. On a large scale, this research is helpful for:

1. Theoretical Benefits

The benefits of this research will increase knowledge and insight regarding its relationship with improving marketing performance through customer orientation, competitor orientation, digital marketing capabilities, innovation capabilities, and developing marketing management knowledge.

2. Benefits in the Field of Practice

It is hoped that the practical benefits of this research will be one of the requirements for graduation with a final degree in Bachelor of Management at Muhammadiyah University of Yogyakarta, as well as information material for MSME owners regarding knowledge of improving marketing performance through customer orientation, competitor orientation, digital marketing capabilities, and innovation capabilities.