Examining and Exploring Indonesia Small and Medium Enterprise Performance: An Empirical Study

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Abstract: This study attempts to explore and examining about Indonesia Small and Medium Enterprise (SME) performance through relationship with strategic management theory. We apply strategic management model into our research to explain the relationship of firm performance with firm determinants. Firm strategy, external environment factors and internal resource factors of firm will be used as determinant of firm performance. Samples from Indonesia SME are collected and statistical analysis is applied to produce valid results. Result shows direct positive relationship of firm strategy and internal factors of firm with firm performance. Direct positive relationship of external and internal factors of firm with firm strategy also recorded. Our finding shows that high perform firms of Indonesia SME tend to use differentiation strategy, emphasize on organization assets and human resource capabilities, and focus more on customer needs.

Key words: Indonesia small and medium enterprise, firm performance, firm strategy, firm factors

INTRODUCTION

Subject of Small and Medium Enterprise (SME) will always be an important factor in building economy of developing country, such as Indonesia. Indonesian Ministry of Small and Medium Enterprise announced that up until 2009, there were almost 53 million unit of SME in Indonesia and those units provide jobs to almost 100 million citizen of Indonesia (MCSMERI, 2010). Brata (2003) noted that Indonesian SME comprised for almost 90% of all business unit that was founded in Indonesia. Therefore it is very logical that Kuncoro (2000) argued that Indonesian SME significantly promotes new jobs, new business, and contributes heavily in reducing poverty. Those figures reflect how Indonesia really depends on SME growth and SME will become a key factor to develop Indonesian economy.

On the other hand, researchers show that even though for developing countries SME is a vital key to promote economic growth; evidences show that to ensure the sustainability of a SME business is not an easy feat. Southiseng and Walsh (2010) clearly pointed out that entrepreneurs in Laos faced numerous hurdles in their struggle to keep the business intact. Technological barrier, lack of good human resources, lack of focus, and harsh treatment from unfair policy of government clearly slow the development of SME business in Laos. Eyaa and Ntayi (2010) also pointed out similar situation in Uganda, where SME unit survivability is really low in the first year of their founding and they focused more about problems

in supply chain and performances. Those finding clearly shows that good SME business performance is a vital necessity in order to survive and more attention needed in understanding how to increase SME firm performance in economic market.

Therefore, looking back into Indonesia situation we come across similar question: What about Indonesia SME situation? How are the performances of Indonesia SME? Unfortunately, few of research in topic of Indonesia business, moreover of Indonesia small business are currently available in international journal. While there are few Indonesian researchers try to focus on SME, but only handful of them that discuss about SME performance and impact on the firm. Agustina (2008) and Hadiati (2008) discuss about Indonesia SME and capable of mentioning some factors that affecting SME performances, but the scale is relatively small and they focus more about the operational management rather than firm characteristics and real connection with firm performance. Thus, we propose to conduct a research in order to give more insight on Indonesia SME situation in term of firm performance.

In business research scope, it has been established that essential way to examine performance of a firm is by applying strategic management theory into the research. Numerous of researchers has established firmly about the importance of firm strategy to gain competitive advantages and establishing good performance (Porter, 1985; Barney, 1991; Mintzberg and Lampel, 1999). By examining the relationship between

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firm strategy and firm performance, researchers able to look further into various factors that build the decision strategic of the firm and thus finding more about variation among firm factors, such as technology, human resources, assets, capital, knowledge creation, and environment can influence a firm decision in establishing a strategy and furthermore influence how a firm perform (William *et al.*, 1995; Pelham, 1999; Tsai and Li, 2007; Chen and Hsu, 2010; Ortega, 2010). Furthermore, a growing body of firm strategy research in SME of developing countries also report similar argument and their result also show encouragement of applying strategic management theorem in explaining variation and determinants of firm performance. Those researches provide significant evidences that similar treatment can also be applied in smaller firms and certain advantages due to firm competitive strategic, internal firm factors, or even opportunities from environmental external factors can also materialized in small firms and in developing countries region (Appiah-Adu, 1999; Li *et al.*, 2005; Amoako-Gyampah and Acquaah, 2008; Arragon-Correa *et al.*, 2008; Mashayekhi and Bazaz, 2008; Singh, 2009). Based on these facts, we find out that strategic management theorem and framework is a good platform to base our research and no conflicting problem really evident in choosing sample of SME in developing country such as Indonesia.

This research will try to explore about Indonesia SME business performance by examining the relationship of firm strategy, firm factors, and firm performance in Indonesia SME. In order to accomplish our research, we propose to discuss SME performance in paradigm of firm strategy because we believe that strategy of a firm will give direct and significant impact to firm performance. By understanding a firm strategy and competitive advantages that build strategy, we can explain performance of a firm easily. We based our research on framework that was developed by Spanos and Lioukas (2001) with some modification to cope with our situation. We choose Spanos and Lioukas (2001) as our base model for several reasons; firstly, because their framework is unique by integrating more factors (internal and external factors of a firm) and connecting them with firm strategy and performance. Rather than conflicting ideas of industry specific to firm specific factors like some of the researchers in strategic areas did (Hoopes *et al.*, 2003), they incorporate the internal factor of firms (with relationship to Resource-based View perspective (Barney, 1991) into structure-conduct-performance (SCP) of Porter (1979) hypothesis. This means more competitive advantages factor of a firm can be explained and impact to firm performance also might become more significant. Secondly because the main population of their research is SME in Greece; and our research also focus in SME scope too, so the framework should be logically

compatible with our research. Another reason is to test the robustness of the framework by conducting similar research in other demographic area.

Then, to explore deeper to the firm factors that give competitive advantage to firm performance, we will separate our sample into two groups according to their performance and compare each competitive advantage variables to find more interesting facts about Indonesian SME. Based on the model, we will establish questionnaires and gather data from Indonesia SME. We apply statistic tools to check the data validity and reliability and use Structural Equation Model (SEM) to find out the relationship of firm factors, strategy and firm performance. Furthermore, we also categorized our sample into low and high perform firms in order to give deeper and more detail view of our research. Result of the data analysis will be reported and discussion and data interpretation will be conducted to give our reader the result of our investigation. We expect our result can help us in exploring and understanding more about the situation of Indonesia SME and from the result, some rough recommendation can be constructed.

LITERATURE REVIEW

One very basic thing that always gives foundation of Porter (1979) thinking is about competition. Porter argue that basic of understanding about the main reason of firm action that in turn shape into strategy can be traced from the condition of firm competition. Here he proposed that competition of firm will not only consists of merely in term of rival or firm that do business in similar industries. Porter proposed that there will be situation of external pressure and threat that ultimately affect the way of firm doing business. He called the pressure or forces as Industrial Forces. Porter argued that there will be five kinds of Industrial forces that ultimately affect firm in deciding their action in business. In his famous writing about How Competitive Forces Shape Strategy (Porter, 1979) he developed a distinctive framework for explaining how exogenous factors impact firms in a given industries. Porter describes five structural forces that determine the performance potential of firms competing in a given industry. Essentially, five forces of industry structure effects overall industry performance, and therefore effects performance of firms within the industry. He proposed five forces of industrial forces as barrier of entry, power of suppliers, power of buyers, substitution threat of product/service, and competitive rivals in the same industry.

Furthermore, Porter tried to give interesting argument about the next step of external pressure that affects firms in coping with their business. In accordance to his view, Porter argued that firms should position their strategy in certain position in order to achieve sustainable profit. He

described his strategic position as Generic Strategy Position (Porter, 1985). The main idea of this framework will be in accordance to positioning of firm. Porter believed that when a firm wants to sustain its advantage in term of performance, certain actions must be conducted in order to assure the sustainability. Because Porter believed that external pressure and environment effect primarily shaped firm action in business, or in other word, strategy. Porter logically believed that firm must target itself to a certain position in its market in order to survive. By positioning itself in a market, he believed firm will be able to sustain its performance for a period of time. He also believed that when a firm tries to reach more than one position in a market, in long run that firm will definitely fall into tuck in the middle situation, which he described it as a situation where a firm desperately try to reach various position without successfully define itself in a distinct position to defend. This kind of situation will ultimately harm firm performance and make it lose its advantage in industry. To achieve that position, certain actions must be taken deliberately by firm, which we call as trategy. Initially there are three types of strategic position that were mentioned by Porter, which were Cost Leadership, Differentiate, and Focus. The significance of any strength or weakness of firm posses is ultimately a function of its impact on relative cost or differentiation. So, even though it seems there are three types of positioning strategies, in reality there are only two essential positioning of cost leadership and differentiation.

In a completely different kind of focus than Porter definition of strategy, there was a different perspective of strategy, which is called as Resource-Based View (RBV) which takes root in Schumpeter thinking and defined more in Barney (1991) research. The basic concept of RBV perspective describes that firm is considered as a bundle of resources, and some of its resources are unique to the firms. This unique resources in turn will define and distinct firm performance in sustainable way (Bowman and Ambrosini, 2007). The follower of RBV concept argued that firm is heterogeneous in terms of their control of important strategic resources, and that resources are not perfectly mobile between firms (Baraldi *et al.*, 2007). The immobile resources that uniquely resided in the firm will determine the sustainability of firm performance. They believe that some characteristic are resided in those unique resources that can distinguish them from common resources, which are tacit, rare, hard to imitate, and non-transferable.

Spanos and Lioukas (2001) in their research of n Examination into the causal logic of rent generation: Contrasting Porter Competitive Strategy framework and the Resource-based Perspective in Strategic Management Journal, vol. 22, pp: 907-934 had tried to explain how Porter framework and RBV perspective play their role in business performance. They describe their model as a comprehensive model that tries to see firm performance in broader way, rather focusing in one kind of strategy perspective. They tried to explain the complementarities between two perspectives and argue that both of views are needed to explain business performance factors in more integrative way. In their framework, they considered market pressure from outside of the firm as external factors and perspective of firm resources as internal factors.

Their hypotheses mainly consist of how Porter frameworks and RBV perspective are complementing each other in explaining firm performance. They argued that in general we can view both of strategy perspective in different route, where competitive advantage of Porter frameworks provide Strength and Weakness of a firm while RBV perspective provides Opportunities and Threat in term of SWOT framework. In this light, they justified their composite framework on basis of three reasons: (a) two perspective are complementary in explaining a firm performance by giving a more balanced view on the sources of competitive advantages (internal and external factors); (b) both perspective try to explain about how a firm can sustain competitive advantage through some factors; (c) the unit of analysis is identical, which is, the firm itself. Result of their researches show that their model is quite valid and can explained, to a degree, about the relationship of firm strategy, internal and external factors of firm, and firm performance

Figure 1 gives a good view of the framework of our model. As in Spanos and Lioukas (2001) model, our framework gives the relationship of firm factors (internal and external), firm strategy, and firm performance. External factors of the firm reflect the external pressure and exogenous market strength that affect firms, and internal factors of the firm reflect the inner strength of firm, firm own resources that capable to give the firm competitive advantage in coping with competition and leveraging its own performance. Here we can see that performance of a firm is directly affected by how a firm conducts its strategy and also affected by various factors from inside of firm and from external environment. On the other hand, internal and external factors of a firm will affect how a firm react and formulate a strategy. Some minor modification is conducted on how a firm view the external environment (or in our model, external factors) on the relationship with firm strategy. Rather than going into offensive type as Spanos and Lioukas (2001) did, we prefer to build our model in the defensive type. Our main reason is because of the type of population that clearly differs from previous reference. While Greece is a country that considered as a developed country, Indonesia is a developing country. Thus it is quite impossible for a small firm in a developing country to try to affect its external environment. Lack of resources, capital, technology, and market share clearly show that in developing countries,
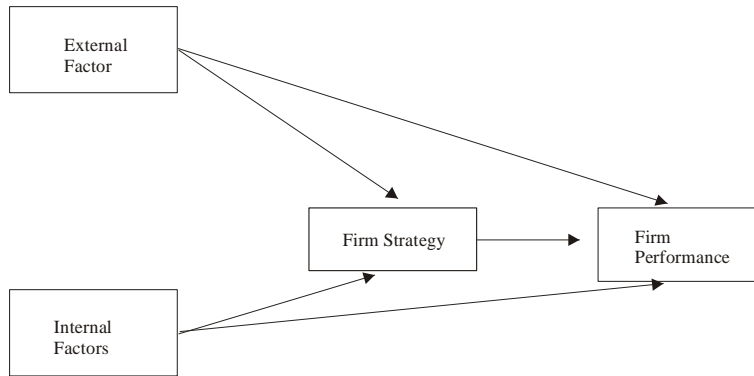
Fig. 1: Framework model (Spanos and Lioukas, 2001)

external factors of market environment will affect how a small firm formulate its strategy. The firm will go into defensive situation by trying to cope with any change and pressure that come from external environment and hope to survive.

After we defined our framework to answer our research question, the next step will be to build the appropriate questions to answer the question in the form of questionnaire. The previous research had been so generous by giving a detailed and well-established model of research questionnaire. We will based heavily our questionnaire model into Spanos and Lioukas (2001) model, but some modification also needed to make sure the question compatible with our situation. External factors variables and firm performance variables still deem to be compatible with our research, but internal factors variables will be referred to Hall (1992) and Galbreath (2005) works which give more complete and detail factors; and firm strategy will be based on Acquaah and Yasai-Ardekani (2008) works which give more appropriate form to developing country firms. The complete determinants can be viewed in Table 1.

METHODOLOGY

Based on previous framework research model, a questionnaire of cross section is constructed. The basic question will consist of what the framework model needed: internal factors, external factors, firm strategy, and firm performance. Two control variable of firm age and firm size also included. All questions, excluding age and firm size, will be in Likert scale of 1 until 7 with 1 as strongly disagree and 7 as strongly agree. References of each variables and what the questionnaire will consist of can be seen in Table 1.

Research sample collected from Indonesia SME in East Java Region. According to SME Ministry of Indonesian Republic, Small business is defined as an independent firm with annual asset below 500 million

Table 1: Research variables

Determinants	Reference
Age, Size	Control variables
Internal factors	Hall (1992) and Galbreath (2005)
External factors	Spanos and Lioukas (2001)
Firm strategy	Acquaah and Yasai-Ardekani (2008)
Firm performance	Spanos and Lioukas (2001)

rupiah (www.depkop.go.id). As one of business central in Indonesia, East Java Region is a good place to portrait the condition of Indonesia SME for the composition of business firm approximately equal to national average (90% of East Java firm are SME type according to Kanwil Deperindag, 2001). The list of SME firms acquired from SME Ministry of Indonesia, East Java Branch. We succeed in collecting about 258 respondents reply after sorting unsatisfying reply because of missing value, not in the scope of SME business, or invalid answers. From our calculation, all respondent and questionnaire had successfully clear the 0.6 cut of factor loading (first and second degree), and from Table 2 we can examine that all Composite Reliability (CR) are higher than 0.81 and Average of Variance Extracted (AVE) higher than cut off point 0.5. All of this shows validity in item reliability, composite reliability and discriminant validity (Fornell and Larcker, 1981; Hair *et al.*, 2006).

Confirmatory Factor Analysis (CFA) also conducted to ensure that manifest variables really reflected the hypothesized latent variables. Result of CFA showed $\chi^2/df = 2.141$ (p<0.001) with goodness of fit indicated GFI = 0.943, NFI = 0.898, CFI = 0.940, IFI = 0.943, RMSEA = 0.067. These indicators show that confirmatory factor model fit the data fairly well (Hair *et al.*, 2006; Simsek *et al.*, 2009)

RESULTS

Analysis will be focused on exploring the relationship on each factor in this model. As the main research question asked in the first portion of this study,

Table 2: Correlation coefficient, CR, and AVE

	Mean	S.D	1	2	3	4	CR	AVE
External factors	5.08	0.83	1				0.81	0.57
Internal factors	5.37	0.69	-0.14	1			0.96	0.53
Firm strategy	4.78	0.63	0.44	0.07	1		0.91	0.52
Firm performance	5.19	0.64	0.05	0.17	0.35	1	0.93	0.69

Table 3: Estimation of structural model

Examined path	Standardized path coefficients	p-value	Result
1. External factors → Firm strategy	0.639	0.09	Supported at 10% level
2. External factors → Firm performance	-0.068	0.459	Not supported
3. Firm strategy → Firm performance	0.192	0.03	Supported at 5% level
4. Internal factors → Firm performance	0.105	0.093	Supported at 10% level
5. Internal factors → Firm strategy	0.219	0.05	Supported at 5% level

exploring the relationship of firm competitive advantage factors (external and internal), firm strategy and firm performance will be the key to understand how a firm works. To answer these questions, this study proposes of using Structural Equation Model (SEM) method. The advantages of SEM method are because, unlike simple regression method, SEM can simultaneously construct and examine more than one unobserved factors rather than one of a time. And the major advantageous are on the strength of testing the reliability and validity of hypothetical constructs of latent variables and explaining the direct and indirect relationship among the latent variables by regressing and describing observed and unobserved variance in the model (Anderson and Gerbing, 1988).

The proposed structural model was estimated. Statistic result showed: $\chi^2/df = 1.62$ (p<0.001) with goodness of fit indicated GFI = 0.958, NFI = 0.929, CFI = 0.970, IFI = 0.972, RMSEA = 0.049. These parameters show that the proposed structural model is deemed as fit and it can provide good basis for testing the hypothesized paths. Comparing with result of CFA, we can clearly see that the proposed model give higher results, which are sign of better model fit; thus we can safely assume that our model is indeed capable of explaining the situation.

The estimation of our framework model can be viewed from Table 3. The result shows that from all direct relationship, one relationship of external factors to firm performance is not supported; while the others relationship are supported. Direct relationship of firm strategy with firm performance and internal factors of the firm with firm strategy show good evidence ($\beta_3 = 0.192$, p<0.05; $\beta_5 = 0.219$, p<0.05), while direct relationship of external factors of the firm with firm strategy and internal factors of the firm with firm performance give marginal support statistically ($\beta_1 = 0.639$, p<0.1; $\beta_4 = 0.105$, p<0.1).

Result from Table 3 gives us a general situation and relationship of Indonesian SME in term of firm performance. However, it is necessary to explore more into each factor to understand more about the building brick of those firms. That is, exploring deeper into the difference between firms in term of performance. While it is true that the previous result proved about higher

factors of firm and firm strategy will indeed leverage the performance of firm, but it is still not so clear about what kind of configuration the firms that perform better have comparing with the marginal ones. By understanding the real factors that separate better performed firms with the marginal ones, more explanation about firm factor configuration can be proposed. We referred to Kaynak and Kuan (1993) works in separating high and low perform firm in order to understand better about the relationship of strategy, performance, internal and external factors.

To start with, the very first step in separating high-performance firms with the lower ones will be to conduct a test of differences in performance. It is useless to continue exploring about firm performance differences when the result shows that statistically there are no differences between high performed firms with the lower performed firm. In order to fulfill the basic requirement, sample of this study are being separated into two major parts, high perform firms and lower perform firms. The separation is done by deciding cut off margin for the firms who perform better than others. According to the nature of the questionnaires, cut off margin is given in middle value point of firm performance range from accumulation point of each questionnaire in firm performance questions. By describing the cut off margin, this study can decide that any firms that giving score above the middle value or under it. Because we have six question that ranging in Likert scale from 1 (very poor performance) to 7 (outstanding performance) in each question, the middle point will be 21 of 42; where any firm that score 22 above will be categorized as high-perform firm and 21 lower as low-perform firm. From 258 samples of firms, this study finds that 74 firms can be considered as high performer while 184 other firms can be considered as low performer. t-test is conducted to test the difference of firm performances and the result shows that the differences are, indeed, significant ($t_{performance} = 20.0087$, significant in 5% level). This result gives good base to build next hypotheses, which is about the significance differences of high performer and low performer between firms. By conducting t-test statistic to test the differences between firms, result was gained and showed in Table 4.

Table 4: Mean comparison of high and low performed firm

Variables	Mean of high performed firm	Mean of low performed firm
Size	9.924***[a]	5.838
Age	13.457***	17.405
External factors		
Barrier of entry	4.451	4.23
Power of the supplier	5.523**	5.919
Power of the buyer	5.538***	5.014
Substitution item	4.321**	4.946
Competitive firms	5.505**	5.905
Internal factors		
Tangible Asset	16.37*	17.04
Intelligence property	13.755	14.432
Organizational asset	16.054*	15.255
Reputational asset	18.729	18.548
Capabilities/Skill	36.678**	34.619
Firm strategy		
Cost Leadership	25.941***	30.689
Differentiation	21.858***	18.109

[a] ***: significant at 1%; **: significant at 5%; *: significant at 10%

Result from Table 4 clearly shows that almost all variable factors of firm performance differ in term of high and low perform firm, except in barrier of entry, intelligence property asset and reputational asset of the firm. Result also shows that in Indonesia SME high perform firms, averagely, have bigger size, lower age, lower external factors pressure (except in power of the buyers), higher internal factors (except in tangible asset), and preferring to differentiation strategy rather than cost leadership.

DISCUSSION

Our previous chapter gives us the detail result of statistical calculation about Indonesia SME firm performance and its relationship with firm strategy, internal factors and external factors of the firm. Next, we will try to make deeper and detail interpretation by combining all of our result into one and give a proper thought in addressing the main question of our research, which is, finding and exploring about the situation of Indonesian SME.

We will start with external factors, which are defined as exogenous factors that impact firms in a certain industry. Result shows that in relationship with performance of Indonesia SME firms, our research propose that no significance direct relationship is found but indirect relationship is found through relationship with firm strategy. This means in our sample, external pressures from market give no significant direct effect to how a firm performs in any condition. This finding shows that Indonesia SME cannot tap the opportunity of external condition and market condition to turn it into their competitive strength directly. While some example from developed countries show how firms can benefit directly from exogenous factors that reside in their respective market (Bobillo *et al*., 2010), but our finding proves otherwise. We argue that this kind of situation might

happen in a developing country because not like in developed countries where market, government, and industry environment give supporting advantages such as higher educational labor, technology-based policy, good infrastructure, etc, situation in developing countries show lack of encouragement to establish a business (Flemming *et al*., 2009). Size of market share and volume of the firms certainly show that SME in Indonesia lack of power in the market and in turn give no significant contribution to its performance. With the sheer volume of SME business in Indonesia, this finding cannot be said as encouraging news to us. Firstly, no significance of external pressures and factors mean policies of our government regarding of the development of SME are not effective. Secondly, Indonesian market and industry is controlled wholly by bigger firms and in the long run, these kinds of situation will detriment the development and growth of smaller firms. Thirdly, this sign of the benign of market external situation in Indonesia. Researchers pointed out that good and dynamic condition of market environment is needed in order for firms to growth and prosper.

On the other hand, external factors of the firm still contribute to variety of firm performance indirectly through the relationship with firm strategy. Our result find out that there are relationship through firm external factors and firm strategy (and because relationship of firm strategy and firm performance is significant, we can say that external factors relate indirectly to the firm performance). This finding show when an Indonesia SME firm formulate its strategy to gain competitive advantage in the market and getting better performance, it also consider into the pressure of its environment. The relationship of how external factors of a firm could affect how a firm reacts in the form of applying some kind of strategy had been discussed quite a lot and positive and significant relationship also reported (Forman and Hunt, 2005; Li *et al*., 2005). Going further into the discussion, we find out that firms with higher performance face relatively lower pressure from external environment, except on factor of power of the buyers. Lower pressure from supplier, rivalry and item substitution in higher performing SME in Indonesia prove to give a certain encouragement to choose their own strategy. The choice of strategy become more varied because pressure to yield into supplier demand or getting into bitter pricing wars with the rival or new industry also take lesser consideration. Thus the higher performing firms tend to position themselves into differentiation strategy in our result. The exception of higher effect of power of the buyers might also become the encouragement of higher perform firms to bolster their strategy in order to cope with customer needs, and coping with customer needs mean they will going into customizing their strategy which is one sure

characteristics of differentiation strategy. In turn their actions will reward the firm with higher profit and market share. Our finding also gives further encouragement about how firm strategy and firm level internal factors give more contribution in explaining variation of firm performance rather than direct relationship between external factors and firm performance (Galbreath, 2005; Goddard *et al.*, 2009).

Result of relationship between internal factors of the firm with firm performance report a positive significant direct relationship. Our finding suggest that internal factors of Indonesia SME, which is firm own resources, will affect directly to firm performance. Our result also shows significant indirect positive relationship between internal factors of the firm with firm performance through firm strategy. These results show us that (a) in Indonesia SME, formulation of how a firm reacts and operate in the market, i.e., strategy of the firm, will also be affected by the configuration of its own internal firm resources and (b) those internal firm resources also directly affect on how a firm perform in that industry. This finding give further encouragement to the importance of Resource-based view perspective that firm internal resource are, indeed, a necessity for a firm to attain its competitive advantage and firm strategy simultaneously with internal firm resources explain how a firm perform. Numerous body of researches also report similar finding (Canto and Gonzales, 1999; Edelman *et al.*, 2005).

Going further into the result, we find out that Indonesia SME give no significant emphasize in term of intelligence property and reputation. This can be translated as low-level technology based characteristics on the SME and lack of advertising skill. Low added-value products certainly become the major products for Indonesia SME and this finding explain why Indonesia SME performance is very lacking. By considering producing and selling high added-value and good advertising management; higher gain and higher market share can be expected in the long run (Mc Cutchen and Swamidass, 1966; Gjerde and Slotnic, 2004). Higher performing firms show characteristics of higher emphasize on organizational assets and skill of human resource. Higher performance of a firm in Indonesia clearly affected by higher skill of human resource in the firm and good organization management; in turn, those factors also reflected on the choice of differentiation strategy (Chan and Wong, 1999; Morchet *et al.*, 2006). This finding further encourage others finding about how good human resource and good management of organizational will directly impact to performance of a firm (Collis, 1994; Wu and Wang, 2007). One more interesting finding in our research is about the tangible factor of firm internal factors. Our finding show that higher performing firms consider tangible factor less important than low performing ones, this kind of finding

give one more proof of how tangible asset can be disregard in discussing about firm resources. As Galbreath (2005) propose, we find no evidence in relating tangible assets of a firm with higher performance. Thus we recommend for Indonesia SME to focus more into developing their intangible internal asset rather than worrying into tangible asset, for in long term intangible and capabilities of the firm will significantly affecting higher profit and higher performance.

In term of firm strategy, we have already partially discussed about the significance of firm strategy in explaining firm performance. As our result suggests, formulating a strategy will give positive impact significantly to the performance of a firm and strategy formulation of a firm will be affected greatly by its external environment situation and internal resource factors simultaneously. Our result show firm strategy is the greatest factor that explains the variation of firm performance in Indonesia SME. By formulating fit and good strategy, impact on firm performance will be greatly affected (Mintzberg, 1987; Amoako-Gyampah and Acquaah, 2008). Furthermore our result shows higher performing firm in our sample show distinct characteristic by favoring into differentiation strategy rather than cost leadership strategy. This finding can be explained because in small firms, going into cost leadership strategy is not an appropriate strategy. Cost leadership strategy leans heavily into economic of scale, which only can be used in big and top market share firms. Small firms lack of means to pursue this kind of action, and doing so in long term will further detriment its own profit margin and going further into price wars (in case of price wars again big company, we can sure that small firms will have no probability of victory). Thus, by going into differentiation strategy, firm can differentiate their own unique characteristics and create a market share that solely fit into their own setting. In doing so, firm will generate higher profit and capture the loyalty of customer that satisfied with the model (Porter, 1985). By looking into the relationship of firm strategy and firm factors, we find out that in Indonesia SME, firms with concern to voice of the customers and emphasize more into organization assets and human resources will tend to formulate their strategy differently. They will try to customize their action to cope with customer needs and simultaneously looking into their own internal strength. By understanding their own internal assets and coping into customer needs, the action of the firm will create a unique customize strategy which affected greatly by external voice and internal strength. This progress will in turn take the firms into applying unique and differentiation strategy into the market. On the other hand, low performing firms in Indonesia tend to play into slashing prices strategy (or in other words, cost leadership strategy), emphasizing more into tangible assets and suffer more with pressure from the market. Without having any unique strategy and rely

solely into low prices, these firms will suffer more than higher performing firms.

CONCLUSION

In this study, we discuss about exploration of Indonesia SME firms performance in relationship with firm strategy and firm factors (internal and external). Through our model we establish the questionnaire and collect the data. By applying statistical tools, we analyze the model and present some interesting finding. We find positive direct relationship between firm strategy and firm performance; internal resource of the firm and firm performance. We find out direct positive relationship between external and internal factors of the firm with firm strategy. We argue that market condition of Indonesia SME is benign, with big firms impact heavily into the dynamic of the market environment. We also posit that Indonesia government need to rethink their policy in strengthening and regulating the small firms in Indonesia if they want Indonesia SME to grow. Formulating a firm strategy is a must if a firm wants to survive and attain sustainability in Indonesia. Firm needs to be aware of its internal strength and to cope with the environment in order to formulate a fit and good strategy in its domain business.

This study has tried to give better understanding on the subject of firm performance through inspecting similarities of two theories and viewing them as a synergic research framework. This research framework basically view firm performance as the result of combination of external forces of the firms as industrial effect, the internal strength of the firm resources as firm effect, and the action of the firms to cope with external forces and utilizing its own resources as firm strategy. Through empirical study, this study clearly showed some good evidence about the inter relationship between those factors. It is showed that external factors of the firms, together with its resources will positively affect firms in implementing its strategy. On the other hand, firm strategy and its resources clearly give positive impact in helping firm to achieve good performance. This kind of result clearly gives good acceptance and support for researchers that posit about the importance of combining and synergizing those theorems.

By going further into our analysis, finding about interesting characteristics on Indonesian SME can be reported. Indonesia SME firms that perform higher in their market tend to operate with differentiation strategy, emphasize more into organization assets and their human resource capability. Those firms also give more attention into customer needs. Combinations of those factors reward firms with greater competitive advantage and in turn give leverage into their performance. We also noted that Indonesia SME still rely heavily into low-value added products, low innovation and no intellectual property emphasize. Lack of advertising and reputation also shadows the situation of Indonesia SME. We recommend new venture that want to establish business in Indonesia should consider in producing high level value added product through higher technology level used in manufacturing/service and seriously considering applying and inventing new intelligence property. Lack of reputation and advertising also cause lower market share and in turn will cause external market environment to give no positive effect into the firm.

Of course, there still a lot of aspect that can be examined further and as a research, this study also has its own restriction and limitation. This conclusion can only be certain in its own territory, which is the sample scope. To really be able to confirm whether this conclusion can be applied to wider scope, more sample and deeper examination into Indonesian business climate and culture will be needed. Going into another direction such as bigger firms and separating into different kind of business and industries also will give clearer insight about what happened in the Indonesian business communities. Another point is, although this study can revealed some interesting relationship on the building bricks of firm performance in empirical level, still empirical limitation obstruct this study to examine further about the real detail of each relationship and how can those relationship can be started. To tackle these issues, deeper qualitative researches that include detail case studies report are recommended.

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