



**THE ROLE OF PRODUCT INNOVATION IN MEDIATING THE RELATIONSHIP
BETWEEN CUSTOMER RELATIONSHIP MARKETING AND COMPETITIVENESS OF
SMALL-MEDIUM INDUSTRY (UKM) IN BALI**

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ABSTRACT

This research aims to analyze and explain the role of product innovation in mediating the relation between Customer Relationship Marketing (CRM) and Competitiveness of small-medium Industry. The research was conducted in Bali Province, specifically on export-oriented woodcraft industry which nowadays becomes the dominant export in Bali Province. Based on the data of Industry and Trade Office of Bali Province, the biggest woodcraft products export spreads mainly in four regency and city areas; Denpasar City, Badung Regency, Gianyar Regency, and Tabanan Regency. Those four regency and city areas are known as Bali Province's Sarbagita area. The data published by the Industry and Trade Office is dated on 2014. The research population was the total proportional workforce who was 10,455 persons who spread in each area as follows; 2,134 persons in Tabanan Regency, 2,636 persons in Badung Regency, and 5,335 persons in Gianyar Regency. The sample was taken using proportional random sampling method with total research sample of 100 persons. The quantitative analysis technique using structural equation modeling (SEM) based on Partial Least Square (PLS) was used in the research. The results show that product innovation is the determiner in increasing competitiveness. The theoretical implication of the research is that the finding on product innovation latent variable has a double-role as the partial mediator of CRM which shows that product innovation has a dominant strategic implication in strengthening competitiveness. The processed data is able to give a satisfaction answer to the hypothesis formulation which states that product innovation affects competitiveness.

Key words: Customer Relationship Marketing, Product Innovation, Competitiveness

I. INTRODUCTION

The growth of the more competitive business world has caused changes on competition, production, marketing, human resources management, and transaction handling between a company and customers, and also between a company and other companies. The global and sharp competition has caused a reduction in profit earning of companies which enter the world level competition. Only companies which have competitiveness on the level of globalization era which are able to satisfy or fulfill the needs of consumers, and to produce quality and cost-effective products. Those changes have made companies to prepare their selves in order to be accepted in the global environment. This condition has forced the management to prepare, perfect, or even find new strategies which will make the company to be able to survive and develop in the world level competition.

On this matter, the company should restudy the principles which are used in order to be able to survive and grow in the tighter competition. The competitors tend to be more advance and productive because they have human resources which have more experience, productive, and faster in adopting new equipment through technology and information which they owned. Companies are required to have an effective strategy and innovation. It means that



the companies should be able to follow changes so that they have competitiveness both in national and global levels.

There are quite many researches on product competitiveness, such as researches on competitiveness which are related to dynamic ability (Teece *et al.*, 1997; Barney, 1991; Nelson and Winter, 1982; Leonard–Barton, 1995). Baark *et al.* (2011) conduct a research on competitiveness which is related to source of innovation and capacity. Researches which measure industry performance from the national competitiveness rank of a nation are conducted by Plawgo and Chapman (1998); Ozlem (2002); Pi-ying and Lai (2005). Most of those researches study the industry competitiveness using Diamond of Competitive Advantage Porter model approach. Research by Choand Moon (2003) also uses diamond Porter model which is adjusted to various competitiveness elements according to the types of industry which is being analyzed. ChoandMoon research(2003) shows that an industry will success and have a competitiveness if it has a clear vision, dynamic, and appropriate to the environment factors condition, demand condition, company strategy and competition structure, and also if it supports the industry and the related industry.

Competitiveness can be affected by many factors, such as location (Royan, 2003), price (Swasta and Irawan, 2008), quality (Ebert, 1995), promotion (Sunarto, 2004), and marketing (Hacioglu *et al.*, 2012). In the business environment nowadays, the business leaders should be able to leave the traditional management principles and replace those using new ways of thinking and behavior which do not only combine changes but also should be able to make changes which are needed. Therefore, entrepreneurship becomes important and has an important implication in marketing which is known as Entrepreneurial Marketing (EM) (Paul and Willhite, 2003; Miles and Darroch, 2006; Schulz and Hofer, 1999; Martin, 2009). To date, marketing activity emphasizes on the 4 P to 7 P strategies, however, those strategies are insufficient to face the more complex competition, especially with the condition of the small-medium industry (*UKM*) which has many limitations (Ionita, 2012).

Customer Relationship Marketing (CRM) is a strategy to develop a good long-term relationship with customers by combining the ability to respond directly and to serve customers with a high interaction (Morgan and Hunt, 1994; Callaghan *et al.*, 1995; Sivesan, 2012). Essentially, CRM is a relationship which refers to all marketing activities which aim to build, develop, and maintain a successful relationship interaction in the long term. Berry (1995) considers CRM as a way to attract, maintain, and increase customers relationship. According to Moorman *et al.* (1993), trust is "a willingness to count on a partner which can be trusted in conducting CRM." Similarly, Oliver (1999) defines CRM as a strong commitment to repurchase a product in the future even though there are situational influences and marketing efforts which have potential to create a behavior of changing into another product. In other perspective, Gundlach *et al.* (1995) states that communication is an important determinant of a CRM strength and a construct which is used to measure the probability of customer loyalty and to predict the future purchasing frequency.

Trust is one of the CRM dimensions. Fukuyama (2002) defines trust as the expectation toward regularity, honesty, and cooperative behavior which appear in a community based on the norms which are shared with the members of the community. Trust in a group is badly needed, not only between the management, but also between the members. It is important because trust will create a good relationship.

Ridell (1997) states that there are three CRM parameters; trust, norms, and networks. CRM is related to the rate of return of a production function. Lavado *et al.* (2010) state that CRM has a relationship with innovation. It can be inferred that a good communication among the staffs will make the innovation process become easier because of the increase of sharing ideas and new concepts at the time the staffs interact with each other. Meanwhile, Brooks and Nafukho (2006) state that sharing information among its organization members holds an important role in the creation of



innovation. Moreover, it refers to the probability of transferring information when the relationship among its organization members is increased. Wu *et al.* (2011) also introduce the network relationship among individuals as an important and effective factor in the process of innovation.

Singh and Sirdeshmukh (2000) state that trust, as one of the CRM dimensions, is the basic in developing and maintaining the relationship toward customers, in which, the trust itself in the marketing theory is the basic policy in developing and maintaining the long-term relationship (Doney and Canon, 1997), creating a mutual relationship toward the customers, and can increase competitiveness (Barney and Hansen, 1994).

Some researches on CRM show an opposite result, such as the researches by Pearce and Ensley (2004) and Zheng (2008) which find out that the effect of CRM toward competitiveness is not significant. Moreover, CRM is a form of company's responsibility which has a strong relationship to the shaping of corporate image in the eyes of consumers and societies. The company is encouraged to adopt CRM because of defensive and offensive motives. The offensive motive is related to the needs to earn business profit by minimalizing cost and increasing the revenue through the increase of customer's satisfaction and loyalty. In contrary, the defensive motivation appears when the main competitors also success in adopting CRM which causes the company becomes worry of losing its consumers and revenue (Buttle, 2004). Meanwhile, Kirita research (2010) on DB Schenker Company in Finland shows that in increasing competitiveness, CRM does not have a significant influence if there are no comprehensive service and creation of advantages. These research gaps can also be filled using innovation variable as the mediator because CRM affects innovation and innovation can determine the competitiveness of the company.

Niammuad (2014) studies entrepreneurship related to product innovation in the effort of increasing competitiveness. Sarma *et al.* (2013) and Septiani *et al.* (2012) combine entrepreneurial marketing with competitiveness. A research on competitiveness is also conducted by Singh and Sirdeshmukh (2000) who find out that trust is the basic in developing and maintaining a long-term relationship. Doney and Canon (1997) state that trust in marketing theory is the basic policy in developing and maintaining a long-term relationship. Barney and Hansen (1994) also state that the creation of mutual relationship with customers can increase competitiveness.

Research on product innovation has been done by many researchers; one of them is Cooper (2000) who states that the advantage of a new product is very important in the competitive global market environment. Advantage of a product cannot be separated from the development of a product innovation because the advantage will enable it to win the market competition. Researches by Baron and Tang (2011); Cheng *et al.* (2012); and Edison *et al.* (2013) show that innovation has become an important factor in the success of the creation of economy productivity, work method, and operation. Khalil and Olafsen (2010); Edison *et al.* (2013) in their researches find out that to achieve and maintain competitiveness, a company must innovate continuously to make a new product (product and service) so that there will be created a good relationship with the customers. Research which specifically studies the role of small-medium industry (UKM) in stimulating innovation and leading the creation of new business has become the research trend in the last few years, as stated by Marcati *et al.* (2008) and Belso-Martinez *et al.* (2013).

Other similar researches are Fasil research (2010) which studies the product innovation which is used to measure company selection, Faria and Lima research (2009) which combines various types of innovation (product innovation, process innovation, and organization innovation) in taking decision, Milling and Stumfe research (2011) which studies interdependency of product innovation and process innovation, Zakle *et al.* research (2008) which studies the external and internal factors which affect product innovation in achieving competitiveness, and also Belderbos research (2012) which studies the correlation of product innovation and export competitiveness and finds out that a certain product innovation is an important driving force of the intensity and export growth.



The research conducted by Niammuad (2014) finds out that innovations will not success without technology mastery and business development. Moreover, Niammuad research (2014) shows that entrepreneurship has a strong tendency to form and drive innovation in form of new ideas and products. However, its effect is insignificant (very weak) because the present of environment factor which often hinders businessmen in producing benefits of their creativities.

In the business environment nowadays, organization needs to consider innovation as a key factor or main factor in organization product and process to survive in the market competition and technology change (Baron and Tang, 2011). Moreover, many researchers believe that innovation is the main source for competitive advantage and it has been proven that innovation plays an important role in the economy growth (Agbor, 2008; Chen and Chen, 2009; Gumusluoglu and Ilsev, 2009; and Karkalakos, 2013). A concept which relates innovation to competitiveness is proposed by Appe (2015) who states that the global economy competition is not only based on the ownership of natural resources but it is also based on the technology ability to process resources innovatively to add economic value as much as it can and to distribute the added value. Therefore, it requires the increase the infrastructure of knowledge, technology, and innovation. Various statements in form of official and scientific studies show that a nation will success globally if it can count on its industrial competitiveness and able to compete with other nations (Atkinson, 2013). Meanwhile, data shows that Indonesia competitiveness is far left behind from other nations if it is seen from the Global Competitiveness Index, Network Readiness Index, and Human Development Index indicators which are the indicators which often be used to measure the position of a nation in the global environment and competition (Hermana, 2012).

In order to increase the competitiveness of *UKM*, it requires researches related to the role of product innovation in mediating customer relationship marketing (CRM) toward *UKM* competitiveness, especially on the export-oriented wood craft industry in Bali Province.

This research also wants to answer all of the present and future challenges and obstacles so that it can give a significant contribution to the development of *UKM* in Bali Province.

2. THEORETICAL REVIEW

2.1 Customer Relationship Marketing (CRM)

Separately, relationship marketing is defined as a process of creating, maintaining, and increasing a strong relationship between a company and its customers and other stakeholders. Other than designing a new strategy to attract new customers and creating transactions with them, a company will continuously try to maintain its customers. In addition, it will try to build a long-term relationship which can produce profits (Kotler and Amstrong, 2010).

Velnampy and Sivesan (2012) state that relationship marketing is a very important concept to attract and maintain customers in an organization. In the modern business world, marketing focus reflects the movement of change from a transactional marketing to relationship marketing. The efforts to build, maintain, and increase relationship with its customers is an important business aspect. Basically, customer relationship marketing or CRM is a relationship which refers to all activities which aim to build, develop, and maintain a long-term successful relationship interaction. Velnampy and Sivesan (2012) find out that CRM has a positive relationship with customer's value creation which is included in the part of process innovation. Berry (1983) considers CRM as a strategy to attract, maintain, and increase customers relationship. Similarly, Winer (2001) defines CRM as a strategy to develop a good long-term relationship with customers by combining the ability to respond directly and to serve the customers with a high interaction. To support the application of CRM strategy, it requires an instrument in form of management approach which is called customer relationship management.

According to Moorman *et al.* (1993), in conducting CRM, trust is "a willingness to count on a partner who can be trusted". Meanwhile, Oliver (1999) defines CRM as a commitment which is



held strongly to repurchase a product in the future even though there are situational influences and marketing efforts which have potential to cause a behavior of changing to other product.

In another side, Gundlach *et al.* (1995) state that communication is an important determinant of CRM strength and a construct which is useful to measure the probability of customers loyalty and to predict the future purchasing frequency. According to Dwyer *et al.* (1987), in conducting CRM, conflict handling is a supplier ability to avoid potential conflict, solve conflict before creating problem, and discuss solutions openly when a problem arises.

According to Sivesan (2012), the main purpose of CRM is to increase a strong relationship between marketer and customer by converting or making indifferent customer to be more loyal. Its long-term aim is to produce continuous advantage from two customer groups; the present customers and the new customers (Chan, 2003). To date, researches tend to study the relationships marketing, in which, those researches always emphasize on trust and commitment dimensions. It is supported by Palmeter *et al.* statement (2009), while Sivesan (2012) states that there are four factors which affect relationship marketing; trust, commitment, communication, and conflict handling.

Based on the past studies, relationship marketing has a multi-dimension characteristic which consists of six components; trust, commitment, communication, shared value, empathy, and reciprocity (Callaghan *et al.*, 1995; Morgan and Hunt, 1994). To maximize long-term business performance in aspects such as customer growth, selling retention, and profitability, those aspects should be built, maintained, and increased in the long-term in order to create a mutual benefit with the target buyer.

1) Trust

In general, trust is seen as a basic element for the success of relationship marketing. Without trust, a relation will not last in the long-term. Morgan and Hunt (1994) state that trust is the foundation of partnership strategy when there are parties which have the needs to commit and tie themselves to a certain relationship. Trust is the commitment forming factor because commitment covers trust and sacrificial factors. Commitment cannot be formed without the present of trust. Moreover, Morgan and Hunt (1994) state that trust significantly affects commitment in a relationship. Trust is also a belief owned in the relationship with the work partner related to honest behavior and help each other. A trust is created when a party feels comfortable to make a trade with other party with honesty and can be trusted. In order to obtain a customer trust, a company should make an effective communication, adopt the norms which are believed by the customers and avoid negative judgments (Morgan and Hunt, 1994).

2) Commitment

Commitment is the ability and willingness to harmonize individual behavior to the needs, priority, and aims of an organization. It covers the ways to develop the aims or fulfill organization needs which mainly puts organization mission before individual interest (Soekidjan, 2009). According to Meyer and Allen (1991), commitment can also mean as a strong individual acceptance toward organization aims and values. Furthermore, the individual tries, works, and has a strong passion to survive in the organization.

Commitment is also a trust between the related parties who want a continuous relationship which is considered as important in maintaining the relationship. Company commitment is the core of relationship marketing. Company commitment can be achieved by placing customers as the long-term main priority, and based on the mutual relationship. Company commitment can also be described as a company promise or oath to maintain the present relationship because it has an important meaning (Morgan and Hunt, 1994). Ndubisi (2007) states that company commitment can be directed continuously to learn and provide customer needs. Moreover, service quality will increase customer satisfaction, which in the end will take the company in creating a strong relationship with the customers.

Based on the source of commitment, Meyer and Allen (1991) divide commitment into three.



- a) Affective commitment is a need which is emotionally tied to the organization, identification, and involvement based on the same values.
- b) Continuance commitment is a commitment which is based on the awareness of costs which should be paid if the commitment be broken.
- c) Normative commitment is a commitment based on the compulsory feeling as a part of the similar business environment. Here also happens internalization of norms which are present in the society.

3) Communication

When a conflict arises in a company, the cause will always be identified as a result of a bad communication. A company must manage a good communication because a failed communication might create harms such as misunderstanding and confusion. The effectively of a communication is the ease to obtain a correct and exact information which enable customers who want to do transaction to be able to take a decision directly to choose according to their needs. The obtained information accuracy indirectly can affect customer's loyalty. Communication is an important tool in building a relationship with a person. Communication is the key factor of a strong relationship between a company and its customers; therefore, communication has a vital role in building relationship. A company which is oriented on the effort of fulfilling the needs of the customers and obtaining profit continuously will surely need the role of communication.

Communication in the relationship marketing has a relation to the value which is obtained by the customers, accurate and trusted information given by the company, information on service changes which are offered, and a proactive communication when a problem occurred between the company and its customers. Customers always want an effective communication with the company. A good communication will surely increase customer trust toward the company.

4) Conflict Handling

In every relationship, socially and economically, there is always an interdependency sense between all parties. A company and its customers which are interdependent one to another should be able to create a relationship which supports each other. However, in reality, that kind of relationship can create conflicts which are caused by various things. Things that have potential of creating conflicts are not only related to product, but also related to service, courtesy, politeness, attention, and care of the staffs or the service providers. The ability of handling conflict refers to the company ability to prevent or minimize the impacts of matters which have potential in creating conflicts and the ability to solve a present conflict. Conflict can become a serious problem in a company and it has a potential in lowering the performance if it is neglected for a long period of time without solving it.

Conflict handling is a special action in the process of doing interaction with customers (Ball *et al.*, 2004). The company ability in handling conflict will create customers satisfaction and loyalty (Ndubisi, 2007). Sivesan (2012) states that when a company can be trusted, committed to the service, can be counted on, efficient in doing communication with its customers, and good in handling problems, then the customers will likely to be loyal toward the product. Sivesan also suggests that a company must maintain a good relationship with its customers in order to get customers loyalty.

The four dimensions above are unities which correlate each other which aim to realize a good relationship between company and customers so that it can create a long-term mutual relationship between company and customers. The efforts in building trust, commitment, competence, communication, and handling conflict abilities are the main keys in applying CRM.

Right now, CRM has developed into a new paradigm for marketing strategy. CRM is able to empower the strength of customer needs with information technology pressure to



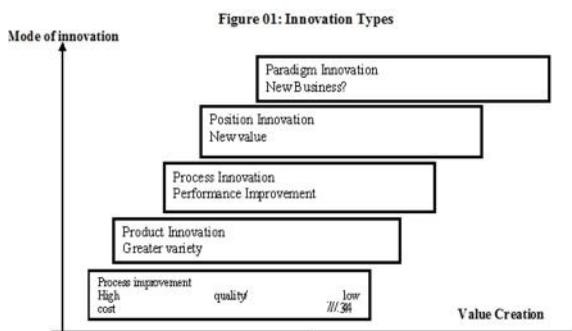
give a satisfaction to customers. Its coverage is the globally integrated quality management to face business needs with more aggressive customers. The stimulations which are needed from the concept of CRM are methods in attracting attention, maintaining customer's satisfaction, and also increasing and strengthening the customer satisfaction relationship. In other words, CRM tries to extend customers life (Tung, 1997).

2.2 Product Innovation

Companies are the most innovative in the continuity of search for a better product, service, and way to do something. Company tries to keep increasing its internal ability and other resources. The more innovative the company of a nation, then the stronger the competitiveness advantage of that nation. A company is more productive if it is more efficient in using its resources (Wang, *et al.*, 2011). Meanwhile, Wu *et al.* (2008) define innovation as an idea, a product or process or a system which is considered as new. According to Tidd (2009), innovation is defined as opening the door globally and the international competitiveness advantage through providing market with a new or unique product or service, creating a barrier which provides resources which are needed to develop innovation through learning, and creating new values which form competitive environment rules. In general, Kotler and Keller (2009) state that innovation is a product, service, or idea in which some people precept it as a new thing and do not care of the length of its history. According to Wang and Ahmed (2004), organization innovation is the overall organization innovative ability to introduce a new product to a market or open a new market through combining strategically orientation with innovative behavior and process.

Tidd *et al.* (2009) state that innovation does not only mean of having a good idea, but actually, it requires an actual action. Innovation consists of an original concept, an innovation from its members, and a real product or service. Some management experts believe that innovation is the main source for a competitive advantage. Moreover, it has been proven that innovation plays an important role in the economy growth (Agbor, 2008; Chen and Chen, 2009; Gumusluoglu and Ilsev, 2009; Karkalakos, 2013).

Figure 2.1 below, as quoted from Tidd *et al.* (2009), shows that in every kind of innovation, there is a creation of values which come from cost, quality, and performance. One of them is product innovation.



Source: Joe Tidd. *Managing Innovation for Global Competitiveness*. Renaissance Project Symposium. Tokyo, 16 March 2009 pp: 09

Figure 2.1:

Values creation which come from Cost, Quality, and Performance

Johne (1999) differentiates innovation into three types; product innovation, process innovation, and market innovation. Organization innovation is related to the new organization



format design and the new management philosophy. Behavior innovation is related to innovation activity of a company organization. Meanwhile, Meeus and Edquist (2006) divide process innovation into two categories; technology category and organization category.

Product innovation according to Crawford and De Benedetto (2000) is “an innovation which is used in the overall operation of a company in which a new product is created and marketed, including innovation in its every functional usage.” Hurley and Hult (1998) define innovation as a company mechanism to adapt in a dynamic environment. Therefore, company is expected to be able to create new ideas, offer innovative products and increase the service which satisfies the customers. Innovation can be applied on products, services, or ideas which is accepted by a person as something new, in which, it might be that an idea had previously appeared in the past, but can be considered as innovative by the customers who just knew it. Often, people think that by doing innovation on a thing, and then a person has done a positive change into advancement. This kind of thinking is correct, however, this change (in any form) might be too difficult to be accepted directly by some customers.

Based on the product innovation definitions above, it can be explained that what is meant by product innovation is “an effort which is done by a company to create a new product with the purpose of adjusting to customers taste and increasing sales. It can be said that the more product quantities which are offered to customers, which are supported by the ease of information flow on the products, then the more selective the customers will be become in purchasing a product in term of quality, design style, color, and price. Product innovation aims to maintain the life of a company because the available products are vulnerable toward the change of customer needs and taste, technology, a shorter product life cycle, and the increase of national and world competitions. Product innovation should be done through market research so that it can produce a product which is suitable to customer taste.

Even though companies prioritize quality, when a company lacks or does not consider customers taste, then it will make the product not be favoured or even the customers will change to other product which resulting in lowering the sales. According to Kotler (2012), there are six categories of a new product, they are:

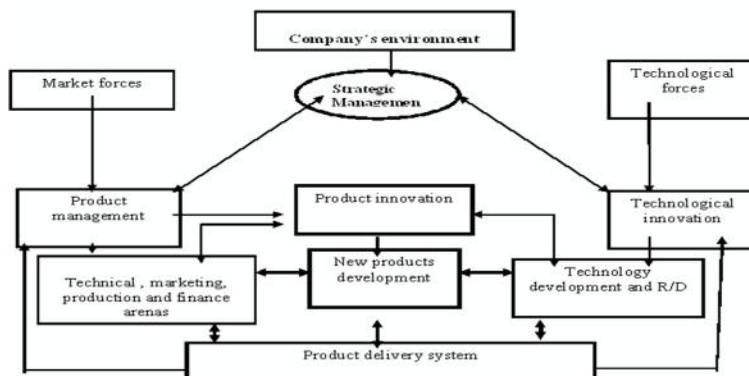
- 1) A new-to-the-world product. It is a new product which creates a whole new market.
- 2) A new product lines. It is a new product which enables a company to enter an established market for the first time.
- 3) Addition to the existing product line. It is a new product which compliments a company product line which is already established (size, packaging, and taste).
- 4) Improvement and revision of the existing product. It is a new product which gives a better performance or has a greater value and replaces the existing product.
- 5) Repositioning. The existing product is directed to a new market or new market segment.
- 6) Cost reduction. It is a new product which provides a similar performance with a cheaper price.

Customer acceptance process toward a product innovation requires time. According to Kotler (2012), customer acceptance process focuses on the mental process experienced by a person from the first-time hearing about the innovation until the end of the acceptance. There are five characteristics which affect the acceptance level of an innovation, they are:

- 1) Relative advantage. It measures how far the level of an innovation can dominate other existing products.
- 2) Compatibility. It measures how far an innovation suit to the individual value and experience in the society.
- 3) Complexity. It measures how far an innovation is relatively difficult to be understood or used.
- 4) Communicability. It measures how far the obtained advantage of an innovation usage can be observed or explained to other persons.



- 5) Differences of organization readiness to try a new product. Acceptance (adoption) will be related to various variables of organization environment (society advancement and society income), the organization itself (size, profit, pressure to change), and its management (education level, age, and its sophistication).



Source: David L. Rainey. Product Innovation: Leading Change through Integrated Product Development. Cambridge University Press. 2006. p:09

Figure 2.2:
 Factors which Affect Product Innovation

Gatignon and Xuereb (1997) state that there are three kinds of product innovation; (1) product advantage, (2) product similarity, dan (3) product cost. Product innovation can fail for many reasons such as it does not offer a unique design or miss-predicts the competition are the common mistakes that happen. Sometimes, a product has a good idea but the design and cost efficiency are higher than what has been predicted before. The present of product innovation will give additional value compared to similar products (product advantage); therefore, it will increase the sales. The competitive advantage of a product is one of the determining factors of the success of a new product (Song and Parry, 1996); therefore, an innovation of a product should have an advantage compared to other similar products.

Similarly, Cooper (2000) states that the advantage of a new product is very crucial in the competitive global market environment. The advantage itself cannot be separated from the development of the produced innovation product because by owning this advantage, the product will win the market competition. Meanwhile, Li and Calantone (1998) state that product uniqueness is defined as an important attribute of a product advantage which is influenced by innovative ability and high technology. Thus, it can produce a product which meets customer needs. The success of a company business can be achieved if the company can react fast on the condition of the new market and customer needs. In addition, the company can produce product continuously. The company should adapt and innovate continuously (Martensen and Dahlgaard, 1999). According to Zimmerer, *et al.* (2008), the indicators of product innovation are (1) design change, (2) technical innovation, and (3) product development.

2.3 Competitiveness

In the more competitive environment and dynamic market situation, a company will not be able to avoid competition; it has to face the competition properly. It means that a company must produce better product from time to time (Muhardi, 2007). A company which does not have competitiveness will be left behind by its customers because by not owning competitiveness, it means that the company does not have any advantage. By not owning any advantage, it means that



a company will not have a reason to survive in the competitive market in a long-term. According to Porter (1980), competitiveness is an ability or strategy of a product or company or industry to compete which is not only seen from the production aspect or its ability to produce a cheap product, but also from the combination of a final result (aim / mission) and the effort (policy) to achieve it. The effort which is described as the wheel of competing strategy is not only involving production efforts (manufacturing, product lines, and research and development) but also involving financial, marketing and market target, sales, distribution, procurement and purchasing goods, and also workforce. In formulating the competitive ability and strategy, there are some questions that should be answered; what is the company doing? How is the environment condition (industry analysis, competitors, social politic and relative strength and weaknesses)? And; what should be done by the company? Porter (2008) develops five strengths in industrial structure analysis; they are competition intensity in the industry, newcomer challenges, substitution product pressure, buyer and supplier bargaining ability. From those five strengths, there are three basic success strategies, they are; over-all cost leadership, differentiation, and focus. Competitiveness is related to how effective an organization in the competitive market compared to other organization which offers similar product. Companies which are able to produce good quality of products and services are the effective companies which mean they will be able to compete.

In addition, Porter (2008) also states that “competition is at the core of the success or failure of firms.” Competition raises two result sides; success or failure. The success side rises because it boosts a company to become more dynamic and competitive in producing a product and also in giving the best service for its market so that the competition is considered as a chance to motivate. Another result side is the failure because it will weaken a static company, make it afraid to compete, and not be able to produce a quality product so that the competition becomes a threat for the company. According to Muhardi (2007), operation competitiveness is an operation function which is not only oriented internally but also oriented externally by responding the target market proactively.

Factors which affect competitiveness are as follows.

a) Location

Effort in considering business location is very important to ease the buyers and becomes the main factor for the continuity of a company. The strategic business location will attract customer's attention. According to Royan (2003), position or location will become very important to ease customers to visit it. Customers will surely try to find the closest location even though it might be possible for a long-distance customer to come but it will be a small percentage only.

b) Price

Price is the sum of overall value which is exchanged by a consumer for advantage of owning or using a product or service. Price will determine whether a supermarket or minimarket will be visited by many consumers or not. Price factor also affects buyer decision. Price is also related to discount, gift coupon, and sales policy. Price is the value of a product or service which is measured using sum of money. For a sensitive customer, usually a cheap price is an important source of satisfaction because the customer will get a high value for money (Swasta and Irawan, 2008).

c) Service

Service program often becomes the first main topic of a supermarket/minimarket manager. Service through product means that consumers are served wholly through the available products and quality products. The service through physical ability mainly refers to the comfortable equipment (trolley), comfortable parking area, good lighting, and hospitality of the staffs.

d) Quality



The belief to win the market competition will be very determined by the quality of the product which is produced by a company. Related to product quality, Adam and Ebert (1995) state that “product quality is the appropriateness of design specifications to function and use as well as the degree to which the product conforms to the design specifications.” Thus, a company will have competitiveness if the company produces a quality product which matches to the market needs.

e) Promotion

The more often a supermarket/ minimarket do a promotion, the more visitors come to fulfill their needs. Promotion can be done through various advertisements such as printed, electronics, or other medias. Sunarto (2004:298) states that sales promotion consists of a short-term incentive to boost sales and purchasing of products or services. This sales promotion covers a wide variety of promotion tools which are designed to stimulate a stronger and faster market response.

The competitiveness dimensions of a company as stated by Ward *et al.* (1998) consist of cost, quality, delivery, and flexibility. The indicators of those four dimensions are as follows.

- a) Cost is an operation competitiveness dimension which covers four indicators; production cost, workforce productivity, the use of production, and stock capacity. Competitiveness element consists of cost which is the compulsory capital which should be owned by a company which covers the cost of production, workforce productivity, the use of production capacity, and the present of stock (production reserves) which can be used whenever the company needs them to support the smoothness of the company.
- b) Quality as meant by Muhandi is a competitiveness dimension which is also very important which covers various indicators such as product appearance, product acceptance length, product durability, speed of solving customer complaint, and appropriateness of the product toward design specification. The appearance of the product can be reflected from its design and service. A good product appearance is having a simple design but with a high value. What is meant by the length of product acceptance is the length of product life which can be accepted by the market. The longer the life of a product in the market means the better product quality. The durability of a product can be measured from economical usage of the product life.
- c) Delivery is the competitiveness dimension which covers various indicators such as precision of production time, shorter production time, and punctual delivery. Those three indicators are correlating each other in which the punctual delivery can be influenced by the precision of production time and the waiting length of production.
- d) Flexibility is competitiveness operation dimension which covers various indicators such as the types of product and the speed in adjusting to environment needs.

3. RESEARCH METHOD

This research used a quantitative research design (Creswell, 2010) which is called positivism research to answer the problem formulation. The examined variables were quantitative variables, in which, the data were collected using perception approach to ease the measuring process. The results were used to formulate the research hypotheses. The research was conducted in Bali Province on the woodcraft export-oriented industry which nowadays becomes the dominant export of Bali Province. Based on the data of Industry and Trade Office of Bali Province, the woodcraft export-oriented product is concentrated in four Regency and City areas; Denpasar City, Badung Regency, Gianyar Regency, and Tabanan Regency. Those Regency and City areas are well-known as Sarbagita of Bali Province. The data published by Industry and Trade Office of Bali Province was the data of 2014. The research population was the proportional workforce as many as 10,455 persons who spread in each area. There were 350 persons in Tabanan Regency, 2,134 persons in Denpasar City, 2,636 persons in Badung Regency, and 5,335 persons in Gianyar



Regency. The sample was taken through proportional random sampling method, in which, it was obtained 100 persons as the total sample. The research used quantitative analysis technique based on multivariate analysis using SEM (structural equation modelling) based on Partial Least Square(PLS).

4. RESULT

4.1 The Effect of Customer Relationship Marketing (CRM) toward Competitiveness

The analysis of direct effect between Customer Relationship Marketing (CRM) variable toward Competitiveness shows that CRM affects Competitiveness based on the value score of 0.019 which is smaller than the alpha score which is 0.05. Figure 4.1 shows the effect of CRM toward Competitiveness.

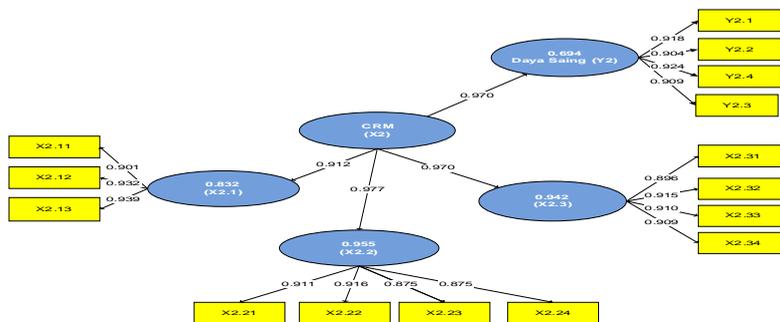


Figure 4.1
The Effect of CRM toward Competitiveness

4.2 The Effect of Customer Relationship Marketing (CRM) toward Product Innovation

Figure 4.2 shows the effect of Customer Relationship Marketing (CRM) toward Product Innovation. It shows that CRM has a positive and significant effect toward Product Innovation because the p value score is 0.004 which is smaller than the alpha score of 0.05.

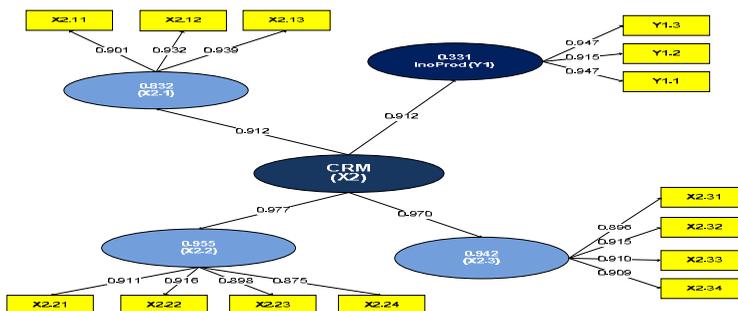


Figure 4.2
The Effect of Customer Relationship Marketing (CRM) toward Product Innovation



4.3. Product Innovation as the Mediator of CRM toward Competitiveness

Figure 4.3 describes Product Innovation as the Mediator of CRM toward Competitiveness, in which the effect of Customer Relationship Marketing (CRM) toward Product Innovation is significant. Therefore, the mediation process can be called as partial mediation.

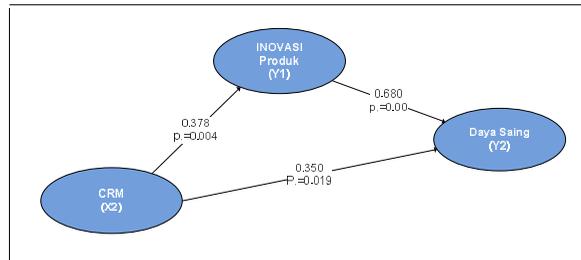


Figure 4.3

Product Innovation as the CRM Mediator

Sobel Mediation Procedure:

Indirect Effect: $A = 0.378 \times B = 0.680 = 0.231$

Sobel SEb : $A = (0.378 \times 0.125)^2 = 0.00223$

Sobel SEa $B = (0.680 \times 0.129)^2 = 0.00769$

$$\text{Sobel SE : } \sqrt{(a.SEb)^2 + (b.SEa)^2} = \sqrt{0.00223 + 0.00769} = 0.09959$$

$$Z = \frac{\text{Indirect Effect}}{\text{Sobel SE}} = 2.3195$$

$$\frac{\text{Indirect Effect}}{\text{Sobel SE}}$$

Based on the Sobel test calculation, the Z score is 2.3195 which is higher than the score of t-table which is 1.96. Therefore, the CRM mediation to Competitiveness through Product Innovation is proven to be significant.

The Effect of Product Innovation toward Competitiveness

Figure 4.4 describes the effect of Product Innovation toward Competitiveness which shows that Product Innovation has a positive and significant effect toward Competitiveness because the p value is 0.000 which is lower than the alpha score which is 0.05.

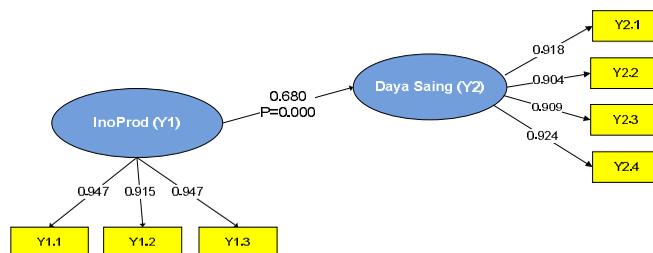


Figure 4.4

The Effect of Product Innovation toward Competitiveness



V. DISCUSSION

5.1 The Effect of Customer Relationship Marketing (CRM) toward Competitiveness

These researches success in proving the hypothesis which states that Customer Relationship Marketing (CRM) has a significant effect toward Competitiveness. It is in accordance with the research done by Singh and Sirdeshmukh (2000) which shows that in the long-term; customer relationship marketing (CRM) will be able to increase competitiveness. It is stated that trust is a part of customer relationship marketing (CRM) which is considered as a basic and important part of business world. According to Singh and Sirdeshmukh (2000), trust is the foundation in building and maintaining a long-term relationship to increase competitiveness. The statement is strengthened by Doney and Canon (1997) who state that trust in a marketing theory is the basic policy in developing and maintaining a long-term relationship to increase company competitiveness. This research is in accordance with Barney and Hansen research (1994) which finds out that creating a mutual relationship with the customers is a part of CRM and can increase competitiveness.

Kirita research on DB Schenker Company in Finland (2010) shows almost similar finding. The finding shows that in increasing competitiveness, CRM will not have a significant effect if there is no comprehension service and advantage creation in the logistic which is accompanied by a comprehensive price rate. Research by Berry (1983) also considers the relation of CRM as a tool to increase and maintain customer's loyalty to achieve a higher competitiveness.

Customer Relationship Marketing (CRM) variable is characterized by 3 (three) indicators, they are; trust (outer loading of 0.912), commitment (0.977), and conflict handling (0.970). From those three indicators, based on the outer loading, which is the respondent expectation, then Commitment is believed to be the strongest one in reflecting CRM, while the strongest Competitiveness is reflected by Flexibility. Based on the indicator aspect, it can be interpreted that the better the Commitment, then the better the Product Flexibility.

Based on that, then the hypothesis which states that CRM has a significant effect toward Competitiveness is proven empirically. This effect can be interpreted as the better the CRM, then the better the Competitiveness of the small-medium export-oriented woodcraft industry in Bali Province.

5.2 The Effect of Customer Relationship Marketing (CRM) toward Product Innovation

The hypothesis formulation which states that Customer Relationship Marketing (CRM) has a significant effect toward Product Innovation is properly answered and proven. It is in accordance with Boier finding (2014) which shows that customer relationship marketing (CRM) affects product innovation. In detail, Boier (2014) states that there is a two-way relationship between customer relationship marketing and innovation, in one side, product innovation produces a positive effect toward customer satisfaction and loyalty. In other side, product innovation produces customer satisfaction which will make the company to conduct innovation.

This research is in accordance with the finding of Smith and Barclay (1997) which states that many different actors can affect innovation of a company such as the surrounding environment. The surrounding environment consists of trusting each other, the present of commitment, the present of effort to handle conflict between companies, networking, norms, and the present of a good communication. All of them are part of CRM indicators. Gnyawali and Park (2011), and Ritala and Hurmelinna-Laukkanen (2009) find out the collaboration of CRM to increase product innovation. Von Hippel research (1988) also shows that CRM can become the source of innovative ideas to stimulate a new product or product innovation of a company.

Customer Relationship Marketing variable is characterized by three indicators, they are; trust, commitment, and conflict handling. From those three indicators, the commitment indicator is believed by the respondents to have the strongest CRM reflection. Product Innovation is also reflected by three indicators, in which, each of them conducts design change, technical innovation,



and product development thoroughly with the highest outer scores on the indicator of conducting design change and product development thoroughly which are believed by the respondents to have the strongest reflections of Product Innovation. Based on the indicator relationship, it can be interpreted that the more committed a company, the more change required on design and product development thoroughly.

Based on the variables relationship and the proven hypothesis which states that Customer Relationship Marketing significantly affects Product Innovation, then it can be interpreted that a better Customer Relationship Marketing will require more Product Innovation of the small-medium export-oriented woodcraft industry in Bali Province.

5.3 Product Innovation Mediates CRM toward Competitiveness

Product Innovation can be interpreted as the mediator of CRM in building Competitiveness. Because the relation between CRM and Competitiveness is significant, then the mediation process can be called as a partial mediation (Little et al., 2012; Nitzl et al., 2012). Some factors which affect innovation process have been studied by many researchers such as by Tidd et al. (2009) and Golish et al. (2008). This research uses Product Innovation as the mediator to build business Competitiveness. Product innovation as a mediator of organization learning, employee capacity, and IT development has been conducted to increase business competitiveness (Song et al., 2010), however, this research develops Production Innovation as the mediator of Entrepreneurial Marketing, in which, researches on this subject is still few. Therefore, it can be concluded that Product Innovation as the mediator of Entrepreneurial Marketing in strengthening the Competitiveness is the novelty of this research.

Patrick (2012), Walker (2004), and Hult and Ketchen (2001) state that the in-line empirical evidence shows that product innovation becomes CRM mediator in strengthening competitiveness.

This research finds out that Product Innovation is proven to be able to mediate CRM. It is in accordance with Patrick research (2012) which finds out an empirical fact that CRM will strengthen competitiveness through strengthening product innovation to build competitive superior performance (Walker, 2004). Other studies which are in-line with the role of product innovation as a mediator which boosts the increase of competitiveness come from the studies done by Deshpande (1993) and also Hult and Ketchen (2001). This research proves that the success in developing CRM network can be achieved if the woodcraft industry conducts a new Innovation so that it will build Competitiveness of the related product.

A number of companies who had conducted a new product innovation were proven to be successful when they were able to develop their company using their new product (Cohen, Eliashberg and Ho, 1997; Farr, 2000). Customer expectation change fast; therefore, CRM development strategy becomes more relevant to be conducted, thus, building CRM strategy can direct and control the change of customer expectation to keep its customers (Berndt et al., 2005). This research proves that Product Innovation is significant in mediating CRM, therefore, it can be stated that Product Innovation which mediates CRM is the first novelty of this research.

The finding shows that Product Innovation is the determiner in the increase of Competitiveness of export-oriented woodcraft industry in Bali Province. The theoretical implication which can be suggested is that the finding on the Product Innovation latent variable has a double-role as the partial mediator of CRM which shows that Product Innovation has a dominant strategic implication in strengthening Competitiveness. This theoretical implication is in accordance with Tidd et al. (2009), Golish et al. (2008), and Plouffe et al. (2001) findings which show that product innovation is the key for expanding the market and obtaining more customers. The development of theoretical model related to Product Innovation in the effort of increasing Competitiveness needs to be increased to achieve more antecedent latent variables to boost the innovation strengthening in the future.



5.4. The Effect of Product Innovation toward Competitiveness

The research result has answered properly the hypothesis formulation which states that Product Innovation affects Competitiveness. This finding supports Zakle *et al.* research (2008) which studies the internal and external factors which affect product innovation to obtain competitiveness. The Product Innovation which is conducted by a company will have an effect on the increase of Competitiveness. Similarly, Khalil and Olafsen (2010); Edison *et al.* (2013) in their researches show that to achieve and maintain competitiveness, a business should always innovate to make a new product (product or service) so that the relationship with customers can be maintained properly.

This research finding supports Belderbos finding (2012) which examines the relationship between product innovation and export competitiveness. The finding shows that certain product innovation becomes an important booster for export intensity and growth because the owned competitiveness experiences an increase. Meanwhile, Marianne and Mile (2004) show that the main implication of their research is if the human resources is neglected, then, the product innovation to increase competitiveness can never be realized. It also means that human resources still become the resource and main actor in producing innovation.

Similar research finding is found by Roper (1997), in Janet and Ngugi (2014) who conducts a study which focuses on product innovation. The finding proves that the output of innovative small-medium industry (*UKM*) grows significantly and has a faster competitiveness compared to the non-innovative ones. This research is also in accordance with researches done by Sarma *et al.* (2013) and Phyra Sok *et al.* (2012) which state that competitiveness will be owned by a company if it is able to conduct product innovations. Sarma *et al.* (2013) find out that the innovation done by a company will surely give an effect toward the company competitiveness. Meanwhile, Phyra Sok *et al.* (2012) state that competitiveness of a company is the direct result of innovations which are done by the company, in which, one of them is the product innovation.

Khalil and Olafsen (2010) also state that to obtain and maintain competitiveness, a company must always conduct innovation to make a new product (product or service) so that the relationship with customers can be maintained properly. In line with it, Vanany (2002) states that the growth of business environment which is more dynamic affects every company in making product innovation in large, medium, and small-scale industries. Therefore, a company is required to select and determine the innovation in order to have competitiveness.

The strongest indicator for Product Innovation variable which reflects each variable based on the outer loading score is the indicator of design change and product development thoroughly which is considered as the strongest in the respondent perception. For Competitiveness variable, the respondents believe that the strongest one to reflect it is the Flexibility indicator. Thus, it can be interpreted that the better the thorough conduct of design change and product development, then, the better the product flexibility. The proven hypothesis which states that Product Innovation affects Competitiveness can be interpreted as the more Product Innovations which are conducted, then, the higher the Competitiveness of small-medium export-oriented woodcraft industry in Bali Province.

6. Suggestions

6.2.1 Suggestions for export-oriented woodcraft industry.

- 1) The research results are expected to be able to give a general guideline to manage export-oriented woodcraft industry and able to start efforts which aim more into the attitude and understanding on the importance of Product Innovation as the supporting components of market expansion in order to be able to compete with other national and international producers.
- 2) The practitioners should maintain the quality of their products because the research results show that it is a safe strategy choice other than the needs for the practitioners in creating a



product development strategy and owning a competence to increase the product competitiveness.

- 3) The practitioners should develop an intense market relationship with their customers to fulfill the needs of the customers.

6.2.2 Suggestions for further researches.

- 1) Further researches can analyze other variables from customer's perspective such as to find out the competitiveness owned by customers.
- 2) Further researches can conduct researches on the similar business such as processing raw material into product for export (such as handicrafts, leather crafts, gold and silver crafts) on small and medium industry sector.

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