

The Influence of Entrepreneurial Orientation, Market Orientation, and Corporate Governance on Firm Performance: The Mediating Role of Innovation Capability

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Keywords	Abstract
Entrepreneurial Orientation, Market Orientation, Corporate Governance, Innovation Capability, Decent Work and Economic Growth	This study is motivated by the increasing demand for manufacturing firms, particularly in the tobacco industry, to enhance competitiveness through innovation, strategic orientation, and effective governance. Despite their significant contribution to economic growth and employment, many family-owned firms still face challenges in maintaining stable performance due to weak innovation capability, limited market responsiveness, and informal governance structures. This study aims to analyze the influence of <i>Entrepreneurial Orientation, Market Orientation, and Corporate Governance on Firm Performance</i> , with <i>Innovation Capability</i> as a mediating variable. The research adopts a quantitative approach using a census sampling technique involving 166 employees of PT Tiga Berlian Anugrah Jaya. Data were analyzed using Structural Equation Modeling (SEM) with SmartPLS 4.0, supported by validity and reliability testing. The results show that <i>Entrepreneurial Orientation, Market Orientation, and Corporate Governance</i> have positive and significant effects on both <i>Innovation Capability</i> and <i>Firm Performance</i> . Furthermore, <i>Innovation Capability</i> partially mediates the relationship between these variables and <i>Firm Performance</i> , indicating its crucial role in translating strategic orientation into performance outcomes. In conclusion, strengthening <i>Innovation Capability</i> , supported by strategic orientation and good governance, is essential for improving <i>Firm Performance</i> and ensuring sustainable competitiveness in family-owned manufacturing companies.

INTRODUCTION

The manufacturing sector remains a central driver of economic resilience and industrial upgrading in many emerging economies, especially when firms are required to compete through innovation rather than cost alone. In Indonesia, this issue is particularly relevant because the national economy grew by 5.03% in 2024, while manufacturing contributed 18.98% of GDP at current prices, confirming that industrial performance remains a strategic pillar of growth. At the same time, the United Nations continues to position productive employment, industrialization, and innovation as core development targets under SDG 8 and SDG 9, meaning that firm-level competitiveness is no longer merely a business concern but also a development concern.

Within that broader industrial landscape, Indonesia's tobacco products industry continues to occupy a distinctive economic position because it combines labor absorption, domestic supply chain linkages, and state revenue generation. Official fiscal reporting shows that tobacco excise revenue reached Rp213.48 trillion in 2023, while sectoral reporting in 2025 noted that the industry contributed about Rp216 trillion in tobacco excise revenue during 2024 and supported millions of jobs across the value chain. These data indicate that the tobacco

industry remains economically significant; however, its sustainability increasingly depends on firms' ability to respond to regulation, competition, productivity pressures, and shifting market expectations.

At the firm level, these structural pressures become more visible in family-owned manufacturing businesses, where strategic agility is often constrained by informal governance and gradual organizational professionalization. The manuscript shows that PT Tiga Berlian Anugrah Jaya operates in this exact setting as a family-linked cigarette manufacturer in Lamongan that developed from a tobacco trading base into SKT and SKM production, employing around 160 local workers and experiencing fluctuating production performance in 2024–2025. The uploaded file also reports that internal diagnostic discussions identified low internal innovation, insufficient market orientation, and weak governance formalization as core managerial problems. This makes the company an appropriate empirical setting for examining how strategic orientation and governance shape performance through innovation capability.

From a theoretical perspective, this problem can be understood through Dynamic Capability Theory, which explains that firms sustain competitiveness not only by possessing resources but also by sensing opportunities, seizing them, and reconfiguring internal capabilities in response to environmental change. In volatile industries, innovation capability becomes the operational bridge that converts strategic intent into adaptive outcomes. OECD publications likewise emphasize that productivity growth, innovation, and sound governance are closely connected to long-run firm performance, especially when firms must continually improve how effectively labor, knowledge, and capital are utilized.

Recent empirical studies also provide strong support for the relevance of entrepreneurial orientation in explaining organizational outcomes. A 2024 study on SMEs in Bali found that entrepreneurial orientation significantly affects innovation capability and firm performance, with innovation capability also mediating that relationship. Other recent studies similarly show that entrepreneurial orientation strengthens proactiveness, risk-taking, and strategic renewal, which are crucial for firms operating in competitive markets. These findings suggest that entrepreneurial orientation is not simply a cultural trait but a performance-generating mechanism when it is translated into innovation routines.

Market orientation is equally important because firms that systematically interpret customer needs, competitor signals, and market changes are generally better positioned to innovate in ways that create value. A 2024 industrial firm study reported that market orientation, together with technology orientation, helps firms build innovation capability and improve performance outcomes. Related work in Indonesian SMEs also shows that market orientation can enhance performance indirectly through innovation capability, although the strength of the relationship may differ across sectors and levels of organizational maturity. This suggests that market knowledge matters most when it is transformed into concrete product, process, or managerial innovation.

Corporate governance adds another critical dimension, particularly in family firms, where informality may support flexibility but can also weaken accountability, role clarity, and strategic monitoring. Recent scholarship on family business governance argues that governance structures can either inhibit innovation through excessive risk aversion or strengthen it through better oversight, disciplined execution, and long-term orientation. OECD guidance also underscores that well-designed governance systems help firms access financing,

improve productivity, and support innovation. Therefore, in family-owned manufacturing firms, corporate governance should be treated not merely as a compliance mechanism but as a strategic infrastructure that shapes innovation capability and performance.

Despite these advances, the literature still leaves an important gap. First, most prior studies examine entrepreneurial orientation, market orientation, corporate governance, innovation capability, and firm performance in SMEs or general manufacturing contexts rather than in family-owned tobacco firms. Second, previous findings remain inconsistent, especially regarding the strength of market orientation and corporate governance in predicting innovation outcomes. Third, few studies integrate all four constructs within one model that explicitly positions innovation capability as a mediating mechanism in a highly regulated, labor-intensive, and culturally embedded industry. These unresolved issues become more significant when viewed alongside the internal evidence from PT Tiga Berlian Anugrah Jaya, which points to innovation and governance weaknesses as real operational concerns.

Accordingly, this research is urgent because it responds simultaneously to both a practical managerial need and a scholarly gap. Practically, firms in Indonesia's tobacco manufacturing chain must strengthen competitiveness without sacrificing operational stability, labor relevance, or governance quality. Academically, this study helps clarify whether entrepreneurial orientation, market orientation, and corporate governance influence firm performance directly, or whether their effects depend on the firm's innovation capability. The urgency is heightened by the fact that industrial performance is increasingly evaluated not only in terms of output growth but also in terms of productivity, innovation readiness, and organizational resilience.

The novelty of this study lies in the construction of an integrated model that connects Entrepreneurial Orientation, Market Orientation, and Corporate Governance to Firm Performance through the mediating role of Innovation Capability in a family-owned cigarette manufacturing company in Indonesia. This is important because existing studies rarely combine these variables within a single framework in the tobacco industry, and even fewer do so in the context of organizational transition from traditional labor-based production to a more modernized production system. By focusing on PT Tiga Berlian Anugrah Jaya, the study offers contextual novelty, theoretical enrichment for Dynamic Capability Theory, and a sector-specific contribution to strategic management research.

Based on that foundation, the purpose of this research is to analyze the influence of entrepreneurial orientation, market orientation, and corporate governance on firm performance while examining the mediating role of innovation capability. The study is expected to contribute theoretically by extending the application of Dynamic Capability Theory in family-owned manufacturing firms, empirically by providing evidence from the Indonesian tobacco industry, and practically by offering managerial insight into how governance, market responsiveness, and entrepreneurial behavior can be aligned to improve innovation and performance. In this sense, the research objective is not only to test relationships among variables but also to generate benefits for business decision-making, organizational development, and future studies on strategy and performance in regulated industries.

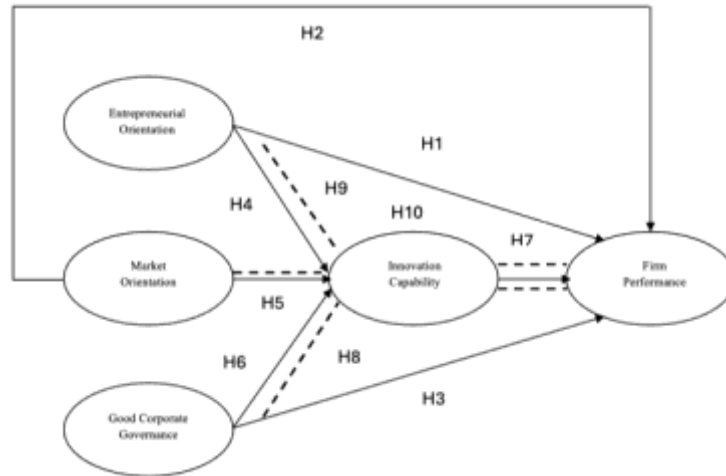


Figure 1. Research Model

RESEARCH METHOD

This study employed a quantitative approach with a descriptive and explanatory research design. The explanatory approach was used to examine causal relationships between variables (Setiawati, 2024). Data were collected using a structured questionnaire administered to all employees of PT Tiga Berlian Anugrah Jaya, a family-owned cigarette company in Lamongan. The total population consisted of 166 employees, including 106 contract workers and 60 permanent staff. The study applied a census (total sampling) technique, in which all members of the population were included as respondents. Thus, the entire population was used as the research sample. (Menambahkan kriteria karyawan yang aktif di perusahaan)

The Entrepreneurial Orientation variable was measured using three indicators with nine questionnaire items (Annur et al., 2025). The Market Orientation variable was measured using three indicators with nine items (Ngo, 2023; Yusup, 2024). The Corporate Governance variable was measured using five indicators with ten items (Ngo, 2023; Yusup, 2024). The Innovation Capability variable was measured using three indicators with six items (Annur et al., 2025). The Firm Performance variable was measured subjectively using four indicators with eight items (Hussain et al., 2021; Ngo, 2023; Yusup, 2024).

All indicators were measured using a five-point Likert scale ranging from 1 (“strongly disagree”) to 5 (“strongly agree”) to capture respondents’ perceptions of the studied variables. (Menambahkan Teknik Analisa Data menggunakan SEM-PLS)

RESULT AND DISCUSSION

Validity and Reliability Test

Based on the validity test conducted on all 22 questionnaire items used in this study, all indicators showed outer loading values greater than 0.70. The highest value was observed in the indicator of variable Z, exceeding 0.92, while the lowest loading remained at the minimum threshold of 0.70. These findings indicate that all items in the study meet the criteria for convergent validity. Furthermore, the Average Variance Extracted (AVE) for each variable was also above the 0.50 threshold, further confirming that the constructs effectively explain the variance of their indicators.

The reliability test results showed that all variables had Cronbach's Alpha values greater than 0.70, namely X1 (0.898), X2 (0.941), X3 (0.933), Y (0.939), and Z (0.939). In addition, the Composite Reliability (CR) values for all variables were also above 0.70, ranging from 0.929 to 0.958. These values confirm that all constructs in this study exhibit excellent internal consistency, indicating that the research instruments are highly reliable.

Menambahkan R-square

Structural Model Evaluation

The structural model was evaluated using the R-Square value to determine the explanatory power of the independent variables toward the endogenous constructs. The R-Square value for Firm Performance (Y) was 0.734, with an adjusted R-Square value of 0.728. This indicates that Entrepreneurial Orientation, Market Orientation, Corporate Governance, and Innovation Capability were able to explain 73.4% of the variance in Firm Performance, while the remaining 26.6% was explained by other factors outside the research model. Meanwhile, the R-Square value for Innovation Capability (Z) was 0.451, with an adjusted R-Square value of 0.441. This means that Entrepreneurial Orientation, Market Orientation, and Corporate Governance explained 45.1% of the variance in Innovation Capability, while the remaining 54.9% was influenced by other variables not included in this study. These results indicate that the structural model has sufficient explanatory power and is appropriate for further hypothesis testing.

Descriptive Analysis Test of Responden Answers

Based on the descriptive analysis of employees at PT. Tiga Berlian Anugrah Jaya, the index value for the Entrepreneurial Orientation variable was 81.57%, indicating a high category. This suggests that the company demonstrates a strong tendency to be innovative, proactive, and willing to take risks in exploring new approaches in work processes.

The analysis also showed that the index value for the Market Orientation variable was 79.19%, placing it in the high category. This indicates that the company has a good understanding of consumer needs, monitors competitor behavior, and is capable of interfunctional coordination in its work activities.

For Corporate Governance, the analysis yielded an index value of 81.22%, indicating a high level. Employees perceive that internal coordination, role distribution, and supervision are functioning effectively. However, in practice, the company still requires improvements in areas such as organizational structure clarity, formalized standard operating procedures (SOPs), and a more standardized monitoring system.

The Innovation Capability variable obtained an index value of 75.81%, also within the high category. Employees assessed that the company is reasonably capable of generating new ideas and improving work processes. Nonetheless, the utilization of technology and systematic innovation development still need enhancement to strengthen the company's competitiveness.

Finally, the Firm Performance variable showed an index value of 81.41%, indicating high performance. Employees rated the quality of work, productivity, and internal service as effective. However, aspects such as cost efficiency, process speed, and continuity of operational improvements still need to be enhanced to achieve more optimal and sustainable performance.

Hypothesis Testing

Direct Effect Test

Based on the analysis results, the path coefficients showed the following outcomes:

Table 1 Path Coefficients Result (Direct Effect)

Variable	Original sample	T statistics	P values	Remarks
X1 → Y	0,263	3,334	0,001	Positive and Significant
X1 → Z	0,311	3,812	0,000	Positive and Significant
X2 → Y	0,428	7,535	0,000	Positive and Significant
X2 → Z	0,232	3,748	0,000	Positive and Significant
X3 → Y	0,235	4,653	0,000	Positive and Significant
X3 → Z	0,297	2,961	0,003	Positive and Significant
Z → Y	0,180	3,143	0,002	Positive and Significant

Source: Internal Company Data (2025)

Based on the results of the test in Table 3, the T-Statistic value of Entrepreneurial Orientation (X1) on Firm Performance (Y) is $3.334 > 1.96$ with a p-value of $0.001 < 0.05$. This indicates that Hypothesis 1 is accepted. The result shows that Entrepreneurial Orientation has a positive and significant effect on firm performance, meaning that the higher the EO possessed by the company, the better the performance achieved. This is in line with previous research stating that EO enhances the organization's ability to create value and achieve higher performance (Annur et al., 2025; Hussain et al., 2021; Mulyono et al., 2024; Wales et al., 2023; Zhang & Xing, 2023).

Hypothesis 2, with a T-Statistic value of Entrepreneurial Orientation (X1) on Innovation Capability (Z) of $3.812 > 1.96$, with a p-value of $0.000 < 0.05$, indicates that Hypothesis 2 is accepted. This shows that EO has a positive and significant effect, meaning that EO can enhance innovation capability, as companies that are innovative, proactive, and willing to take opportunities are more capable of developing new ideas and processes. This aligns with previous research showing that EO encourages creativity, opportunity-seeking, and organizational learning, which strengthens innovation (Fachrunisa & Oktarina, 2024; Hussain et al., 2021; Ngo, 2023).

Hypothesis 3, with a T-Statistic value of Market Orientation (X2) on Firm Performance (Y) of $7.535 > 1.96$ with a p-value of $0.000 < 0.05$, indicates that Hypothesis 3 is accepted. The result shows that MO has a positive and significant effect on FP, meaning that the stronger the company's MO, the higher its performance. This is in line with previous studies, which state that consumer orientation, competitor analysis, and interfunctional coordination can strengthen decision quality and improve performance (Mulyono et al., 2024; Sentoso et al., 2024; Yusup, 2024; Bouhalleb & Messeghem, 2024; Fapari Arif et al., 2024).

Hypothesis 4, with a T-Statistic value of Market Orientation (X2) on Innovation Capability (Z) of $3.748 > 1.96$ and a p-value of $0.000 < 0.05$, indicates that Hypothesis 4 is

accepted. This shows that MO has a positive and significant effect, meaning that MO helps enhance the company's ability to create innovation. This is consistent with previous studies showing that MO broadens the company's perspective in reading trends, triggering creativity and relevant innovation (Mustafa et al., 2022; Yusup, 2024; Butkouskaya et al., 2024).

Hypothesis 5, with a T-Statistic value of Corporate Governance (X3) on Firm Performance (Y) of $4.653 > 1.96$ with a p-value of $0.000 < 0.05$, indicates that Hypothesis 5 is accepted. The result shows that CG has a positive and significant effect, meaning that the better the governance, the higher the company's performance. This aligns with previous research stating that CG strengthens organizational effectiveness and performance outcomes (Ngo, 2023; Yusup, 2024).

Hypothesis 6, with a T-Statistic value of Corporate Governance (X3) on Innovation Capability (Z) of $2.961 > 1.96$ with a p-value of $0.003 < 0.05$, indicates that Hypothesis 6 is accepted. This shows that CG has a positive and significant effect, meaning that good governance helps strengthen the company's innovation capability. This is in line with previous research stating that CG supports the internal stability required for innovation (Gutuleac et al., 2025; Yusup, 2024; Maclean et al., 2023).

Hypothesis 7, with a T-Statistic value of Innovation Capability (Z) on Firm Performance (Y) of $3.143 > 1.96$ with a p-value of $0.002 < 0.05$, indicates that Hypothesis 7 is accepted. The result shows that IC has a positive and significant effect, meaning that high innovation capability helps improve the quality of the company's performance. This aligns with previous studies showing that innovation is a key driver of organizational performance improvement (Annur et al., 2025; Shinta Dewi & Pradhanawati, 2025)

Table 2. Indirect Effect Test Results

Variable	Original Sample	T statistics	P values	Remarks
X1 → Z → Y	0,056	2,258	0,024	Positive and Significant
X2 → Z → Y	0,042	2,031	0,042	Positive and Significant
X3 → Z → Y	0,053	2,289	0,022	Positive and Significant

Source: Internal Company Data (2025)

Based on the test results in Table 2, the mediation hypothesis shows that the T-Statistic value of Entrepreneurial Orientation (X1) through Innovation Capability (Z) on Firm Performance (Y) is $2.258 > 1.96$ with a p-value of $0.024 < 0.05$. This indicates that Hypothesis 8 is accepted. The result shows that the indirect effect of Entrepreneurial Orientation on Firm Performance through Innovation Capability is positive and significant, meaning that EO enhances creativity, proactiveness, and risk-taking, which in turn strengthens the company's ability to generate innovation. This innovation subsequently contributes to improving firm performance. This aligns with previous studies stating that innovation capability serves as an important mechanism bridging EO to FP (Annur et al., 2025; Hussain et al., 2021; Fachrunisa & Oktarina, 2024; Marchyta et al., 2025).

Hypothesis 9 shows a T-Statistic value of Market Orientation (X2) through Innovation Capability (Z) on Firm Performance (Y) of $2.031 > 1.96$ with a p-value of $0.042 < 0.05$. This

indicates that Hypothesis 9 is accepted. The result shows that the indirect effect of Market Orientation on Firm Performance is positive and significant, meaning that MO helps the company understand market needs, monitor competitor movements, and promote interfunctional coordination. This market understanding enhances the company's ability to create relevant innovations, which ultimately strengthens firm performance. This is consistent with previous research showing that MO enables more adaptive and competitive innovations, which directly contribute to improved firm performance (Annur et al., 2025; Mustafa et al., 2022; Yusup, 2024; Marchyta et al., 2025).

Hypothesis 10 shows a T-Statistic value of Corporate Governance (X3) through Innovation Capability (Z) on Firm Performance (Y) of $2.289 > 1.96$ with a p-value of $0.022 < 0.05$. This indicates that Hypothesis 10 is accepted. The result shows that the indirect effect of Corporate Governance on Firm Performance through Innovation Capability is positive and significant, meaning that good corporate governance, including clear structure, accountability, and supervision mechanisms, supports the creation of a work environment conducive to innovation. As innovation increases, firm performance is also enhanced. This aligns with previous research indicating that strong CG can strengthen the innovation process and indirectly improve FP through the quality of innovations produced (Gutuleac et al., 2025; Mulyono et al., 2024; Annur et al., 2025; Marchyta et al., 2025).

CONCLUSION

The findings indicate that Entrepreneurial Orientation, Market Orientation, Corporate Governance, and Innovation Capability all had positive and significant effects on firm performance at PT Tiga Berlian Anugrah Jaya. Entrepreneurial Orientation, reflected in innovativeness, proactiveness, and risk-taking, contributed to improved performance, while Market Orientation and well-structured Corporate Governance enhanced operational effectiveness. Innovation Capability played a crucial role not only as a direct driver of performance but also as a partial mediator that strengthened the relationships between Entrepreneurial Orientation, Market Orientation, Corporate Governance, and firm performance. This suggests that although these strategic factors directly influenced performance, their impact became more substantial when supported by strong innovation capability. Overall, the results highlight the importance of aligning strategic orientation and governance practices with innovation to achieve superior performance. Future research is recommended to incorporate additional variables such as organizational culture, technological capability, and leadership style, as well as to expand the sample across different industries and regions to improve the generalizability of the findings.

(Menambahkan kelemahan adanya hasil bias, "However, this study may contain potential perceptual bias due to differences in respondents' job roles, educational backgrounds, work experience, and access to organizational information. Some questionnaire indicators are strategic in nature, such as market orientation, competitor strategy, customer satisfaction, corporate governance, and firm growth, which may not be fully understood by all employees, especially operational and piece-rate workers. Therefore, the findings should be interpreted as employees' internal perceptions rather than an objective measurement of the company's overall condition. Practically, the results of this study should be followed up through an internal discussion or follow-up FGD with relevant company stakeholders to validate the findings and

obtain additional suggestions for improvement and innovation. Future research is recommended to involve managerial-level respondents, add variables such as organizational culture, technological capability, and leadership style, and expand the study to different industries or regions.”)

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