



The Influence of Social Media and Business Strategy on Business Performance in Bantul, Yogyakarta, Indonesia: Innovation Capability as a Mediating Variable

¹Shandhi Alamsyah; ^{2*}Maria Pampa Kumalaningrum

^{1,2}Management Department, STIE YKPN Business School Yogyakarta, Indonesia

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Abstract

This study analyzes the influence of social media and business strategy on business performance, with innovation capability as a mediating variable, among 145 MSMEs in Bantul, Yogyakarta. Using Partial Least Squares–Structural Equation Modeling (PLS-SEM) via Smart PLS 4.1, all seven hypotheses were accepted. Social media positively impacted business performance ($\beta=0.423$; $p<0.001$) and innovation capability ($\beta=0.661$; $p<0.001$). Business strategy positively impacted business performance ($\beta=0.313$; $p<0.001$) and innovation capability ($\beta=0.523$; $p<0.001$). Innovation capability positively impacted business performance ($\beta=0.255$; $p<0.01$) and partially mediated the influence of both predictor variables. The findings strengthen the relevance of Resource-Based View (RBV) and Dynamic Capabilities theories in managing MSMEs in the digital era.

Keywords: *Social Media; Business Strategy; Innovation Capability; Business Performance; Resource-Based View*

Introduction

Digital transformation has fundamentally changed the way businesses operate, including for micro, small, and medium enterprises (MSMEs). Social media now functions not only as a promotional tool but also as a two-way interaction channel, a real-time market information gathering platform, and a driver of community-based innovation and collaboration (Kaplan & Haenlein, 2010; Dwivedi et al., 2021). In Indonesia, data from the Ministry of Cooperatives and MSMEs shows that MSMEs play a strategic role in the national economy. More than 30 million business units contribute 61% to GDP and absorb approximately 97% of the workforce.

Despite this, MSMEs' digital readiness is far from optimal, around 27 million MSMEs have entered the digital ecosystem, but most remain passive without a clear digital. This situation is evident in Bantul Regency, a buffer zone between urban and agrarian Yogyakarta, Indonesia, where more than 55% of MSMEs still rely on conventional marketing without a well-developed digital strategy. As a result,

many MSMEs experience stagnant growth and lag behind similar businesses that are more technologically adaptable.

There is a clear gap between the enormous potential of small and medium enterprises (SMEs) and the low level of digital resource optimization in their business operations. Sugiarto et al. (2025) show that the adoption of digital technology by MSMEs in Indonesia is still hampered by institutional barriers, limited skills, and low internal capacity to optimally capture digital opportunities. This study examines whether the role of social media and business strategy can improve MSME performance, especially when linked to innovation capability as a mediating variable suspected of strengthening the influence between the two.

Previous research generally discusses social media, business strategy, and innovation capabilities separately (Trainor et al., 2014; Odoom et al., 2018; Parveen et al., 2016). These studies also tend to focus on large companies in developed countries, thus failing to fully capture the dynamics of MSMEs in Indonesia's suburban areas, which have limited resources but hold strategic potential (Kumalaningrum et al., 2023). Furthermore, the role of innovation capabilities as a mediating variable in the relationship between social media, business strategy, and business performance has rarely been studied simultaneously within the Resource-Based View (RBV) framework.

This study aims to fill this gap by simultaneously examining the influence of social media and business strategy on business performance, mediated by innovation capabilities, in the context of MSMEs in Bantul, Yogyakarta, Indonesia. The novelty of this study lies in the integration of three main constructs into a single conceptual model based on RBV and dynamic capabilities and also capturing the complexity of causal relationships between latent variables.

Literature Review and Hypothesis

The RBV theory of Barney (1991); Peteraf (1993) states that competitive advantage stems from internal resources that are Valuable, Rare, Inimitable, and Non-substitutable (VRIN). In the digital context, social media is viewed as a strategic resource that enables MSMEs to build real-time customer interactions and expand market access. Business strategy plays a role in directing optimal resource utilization (Grant, 1991), while innovation capabilities transform these resources into sustainable competitive advantages through dynamic capabilities mechanisms (Teece et al., 1997).

Social media improves business performance by strengthening marketing capabilities, expanding market reach, and streamlining customer communication (Ainin et al., 2015; Tajvidi & Karami, 2021). Furthermore, these platforms serve as catalysts for innovation through real-time access to market information and open, community-based collaboration (Al-Omar et al., 2024; Garrido-Moreno et al., 2020).

A targeted business strategy, including differentiation, cost leadership, and market focus (Porter, 1990), directly improves performance and builds adaptive innovation capabilities. The right strategy encourages the integration of internal and external knowledge to create sustainable innovation that aligns with the dynamics of the business environment (Teece, 2018; Saunila, 2020).

Lawson & Samson (2001) define innovation capability as a dynamic capability that enables MSMEs to consistently create and implement new ideas. As a mediating variable, innovation capability transforms digital resources and strategic orientation into superior business performance (Saunila et al., 2014; Isa et al., 2023). The hypothetical framework of this research is presented as follows:

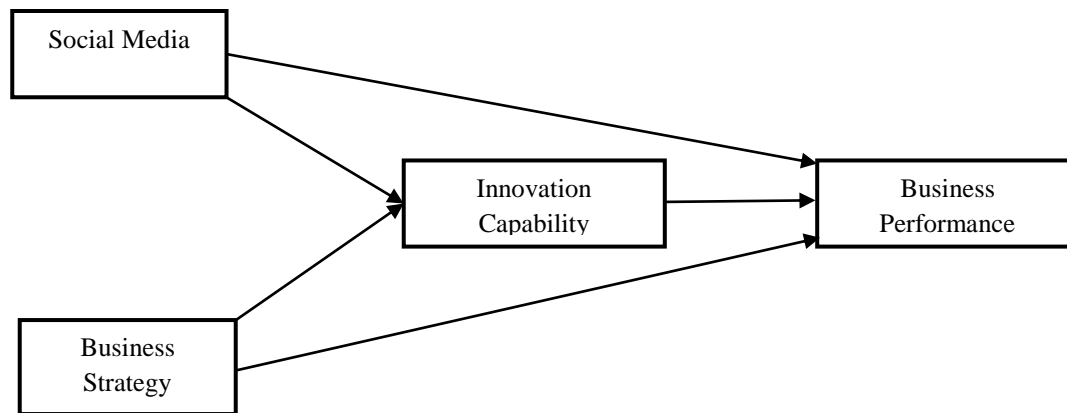


Figure 1. Research Framework

This study builds a framework that links social media and business strategy as independent variables, innovation capability as a mediating variable, and business performance as a dependent variable. The framework of this study is presented in Figure 1 above.

The Influence of Social Media on Business Performance

Social media has become an integral part of business strategy in the digital era, including in the context of micro, small, and medium enterprises (MSMEs). Theoretically, social media can function as a digital marketing tool, a means of building customer relationships, and a platform for increasing brand engagement and visibility. Within the framework of digital marketing theory, Kaplan & Haenlein (2010) describe social media as an interactive, Web 2.0-based channel that enables organizations to reach customers directly and quickly. Mangold & Faulds (2009) assert that social media is a new element in the promotional mix that can create real-time, two-way communication, thereby strengthening customer loyalty and promotional effectiveness.

In strategic management literature, social media is viewed as a strategic resource that can enhance competitive advantage when managed effectively (Jay Barney, 1991; Trainor et al., 2014). Appel et al. (2020) add that social media can improve business performance through increased interaction, customer acquisition, and communication efficiency. Furthermore, Dwivedi et al. (2021) stated that integrating social media into business processes creates organizational agility in responding to market dynamics, strengthens customer experience, and accelerates innovation processes.

Various empirical studies support this claim. Parveen et al. (2016) showed that social media strengthens customer relationships and marketing efficiency in Malaysian MSMEs. Ahmad et al. (2018) concluded that active social media use has a positive impact on sales growth and customer loyalty. Meanwhile, Odoom et al. (2018) emphasized that social media is a strategic tool for improving performance, particularly in the context of MSMEs in developing countries. Local research by Rudi et al. (2025) also indicates that social media supports the performance improvement of Indonesian MSMEs, especially when combined with innovation and business networking.

H₁: Social media has a positive impact on business performance.

The Influence of Business Strategy on Business Performance

Business strategy is an organization's long-term direction and actions designed to achieve competitive advantage in a dynamic marketplace. Chandler (1962) defined strategy as the setting of long-term goals and the allocation of resources to achieve them. Andrews (1971) defined strategy as an integrated pattern of decisions that connects internal strengths with external opportunities. Meanwhile,

Porter (1985) introduced three generic strategies: cost leadership, differentiation, and focus, that can be used to establish a strong and sustainable competitive position. Grant (1991) and Barney (1991), using the Resource-Based View (RBV) approach, emphasized that effective strategies utilize unique and valuable internal resources to create a competitive advantage that is difficult to imitate. Mechanically, business strategy contributes to business performance through managing market positioning, reducing production costs, product innovation, and strengthening customer relationships. According to the Dynamic Capability perspective (Teece et al., 1997), strategy also reflects an organization's ability to reconfigure resources in response to environmental changes. Differentiation strategy drives unique value creation that increases customer loyalty, while cost leadership increases profit margins through operational efficiency.

Various empirical studies demonstrate a positive relationship between business strategy and organizational performance. Rashidirad (2014) shows that alignment between strategy and internal capabilities contributes significantly to competitive advantage. Salunke et al. (2019) emphasize that innovation-based strategies enhance competitiveness and business performance, particularly in the service sector and MSMEs. Research in Indonesia by Dionysus (2020) also confirms that entrepreneurial-oriented strategies have a significant impact on MSME growth and adaptability amidst market volatility.

H₂: Business strategy has a positive effect on business performance.

The Influence of Social Media on Innovation Capabilities

In the era of digital transformation, social media is no longer simply a communication tool but has become a strategic driver in organizational innovation processes. Innovation, in the context of organizational capabilities, encompasses the ability to continuously generate, absorb, and implement new ideas. Social media provides a digital infrastructure that enables knowledge exchange, open collaboration, and access to real-time market insights, key to enhancing innovation capabilities (Kietzmann et al., 2011; Leonardi, 2014).

From an Open Innovation perspective, social media opens organizational boundaries and enables co-creation with customers, partners, or even competitors, which in turn accelerates the ideation and product development process (Chesbrough, 2003). Kaplan & Haenlein (2010) emphasize that the interactive features of social media enable companies to gather direct feedback from customers, strengthening the feedback loop and encouraging the exploration of new ideas. This also aligns with the Knowledge-Based View (Grant, 1996), which views organizations as knowledge-processing entities, where social media accelerates the accumulation and dissemination of strategic information in the innovation process.

Furthermore, Dynamic Capability theory (Teece et al., 1997) explains that the ability to sense market changes and consumer needs is the foundation of adaptive innovation. In this regard, social media enhances the sensing and learning process through rich customer interaction data, enabling companies to respond quickly to innovation opportunities (Appel et al., 2020; Dwivedi et al., 2021). Empirically, a study by Zhang (2021) shows that strategic social media capabilities directly contribute to increased innovation capabilities by strengthening digital interactions and leveraging external knowledge. At the MSME level, Rudi et al. (2025) demonstrated that integrating social media into business processes drives product innovation through community interaction and exploring customer needs.

Thus, social media expands access to ideas and knowledge, connects entrepreneurs with various external sources of information, and creates a collaborative environment that supports the continuous development of innovation capabilities.

H₃: Social media has a positive effect on innovation capabilities.

The Influence of Business Strategy on Innovation Capabilities

Business strategy is a series of decisions and actions taken by an organization to achieve long-term competitive advantage. Chandler (1962) defined strategy as setting long-term goals and allocating resources to achieve them. Porter (1985) introduced three generic strategies: cost leadership, differentiation, and focus, which serve as the foundation for building a competitive position. Meanwhile, Barney (1991) and Grant (1991), within the Resource-Based View (RBV), view strategy as how an organization mobilizes and manages valuable, rare, and inimitable internal resources to create sustainable advantage.

In the context of innovation, business strategy plays a crucial role as a guiding force for an organization in developing innovation capabilities. A differentiation strategy, for example, encourages a company to continuously create unique products and services through the exploration of ideas and creativity. Grant (2019) emphasizes that strategies designed based on internal capabilities can foster an innovative culture and increase organizational agility. This approach aligns with Teece et al.'s (1997) Dynamic Capability theory, which states that an adaptive business strategy enables organizations to sense market changes, seize opportunities, and reconfigure resources to support continuous innovation.

Empirical studies demonstrate a significant relationship between business strategy and innovation capability. Salunke et al. (2019) found that strategies based on knowledge integration and market orientation significantly contributed to increased innovation in service companies. In Indonesia, Purwati et al. (2020) demonstrated that business strategies focused on innovation and technology utilization drove increased innovation capabilities in MSMEs, particularly in the face of digital disruption. This demonstrates that business strategy not only influences performance but also forms the foundation of an organization's innovative culture and processes.

H₄: Business strategy has a positive effect on innovation capability.

The Influence of Innovation Capabilities on Business Performance

Innovation capabilities are a crucial determinant in driving sustainable business performance in an era of dynamic competition. Lawson & Samson (2001) define innovation capabilities as dynamic capabilities that enable organizations to consistently generate and implement new ideas. In the context of MSMEs, this capability refers not only to the technical ability to create new products or services but also includes the ability to adapt, engage in organizational learning, and utilize resources creatively (Guan & Ma, 2003).

According to the Resource-Based View (RBV) approach, innovation capabilities are strategic resources that are difficult to imitate and contribute significantly to competitive advantage (Barney, 1991). The RBV views innovation capabilities as valuable, rare, difficult to imitate, and non-substitutable assets that, when mobilized appropriately, have a direct impact on business performance. Furthermore, Teece et al.'s (1997) Dynamic Capability theory emphasizes that in an uncertain environment, organizations are required to possess the ability to sense, seize, and reconfigure these dimensions, which are manifested in innovation capabilities.

Innovation capabilities drive value creation through improved products and processes, operational efficiency, and increased responsiveness to market needs. Saunila & Ukko (2014) showed that organizations with high innovation capabilities tend to have better business performance because they are able to respond to change with innovative solutions. This finding is reinforced by Purwati et al. (2020), who demonstrated that innovation capabilities have a significant positive influence on the growth of MSMEs in Indonesia. In fact, Terziovski (2010) noted that innovation capabilities can bridge resource constraints in small businesses, enabling them to remain competitive and sustainable.

Therefore, it can be concluded that innovation capabilities play a crucial role in improving business performance, both financially and non-financially. MSMEs that are able to develop their innovation capabilities will be more competitive in creating value, capturing market opportunities, and maintaining business continuity amidst digital disruption and other external pressures.

H₅: Innovation capabilities have a positive impact on business performance.

Innovation Capability Mediates the Influence of Social Media on Business Performance

In the digital business landscape, social media functions not only as an external communication channel but also as an internal driver of innovation capability, which ultimately impacts business performance. Social media expands an organization's access to ideas, customer insights, and market knowledge through digital engagement, co-creation, and community-based interactions (Kaplan & Haenlein, 2010; Leonardi, 2014). Within the Knowledge-Based View and Open Innovation framework, social media facilitates knowledge sharing and idea sourcing from external sources such as customers, partners, and competitors, strengthening an organization's capacity for innovation (Chesbrough, 2003; Grant, 1996).

Innovation capability itself is the strategic ability to identify opportunities, develop new solutions, and adapt internal processes to external dynamics (Lawson & Samson, 2001; Teece et al., 1997). Through the Dynamic Capability approach, innovation capability enables organizations to adapt to market changes by creating new value, whether in the form of products, processes, or business models. Therefore, when social media is utilized strategically, it can strengthen innovation capability, which in turn improves agility, efficiency, and business performance (Appel et al., 2020; Saunila & Ukko, 2014).

Several studies support this mediating role. Zhang (2021) showed that social media capability influences performance through innovation as a mediator. Rudi et al. (2025) in the context of Indonesian MSMEs also found that innovation capability significantly mediated the relationship between digital marketing activities (including social media) and business performance. Therefore, innovation capability can be positioned as an internal mechanism that bridges the external influence of social media towards improved business outcomes.

H₆: Innovation capability mediates the effect of social media on business performance.

Innovation Capabilities Mediate the Effect of Business Strategy on Business Performance

Business strategy is the primary foundation for designing an organization's direction and capabilities to achieve competitive advantage. Porter (1985) proposed that business strategy encompasses differentiation, cost leadership, and market focus as a framework for differentiating strategic positioning. Chandler (1962) emphasized that organizational structure follows strategy, while in a contemporary approach, Grant (1991) and Barney (1991), using the Resource-Based View (RBV), view effective strategy as a unique and valuable form of resource orchestration.

A business strategy designed with an innovative orientation can strengthen an organization's innovation capabilities, namely the ability to systematically create, develop, and implement new ideas (Lawson & Samson, 2001). Differentiation, innovation, and agility strategies provide an organization with the space to foster creativity, respond adaptively to the market, and manage resources dynamically (Teece et al., 1997). Thus, strategy not only sets direction but also enables the development of innovation capabilities, which become long-term competitive strengths.

Innovation capabilities contribute significantly to business performance by strengthening process efficiency, product innovation, market responsiveness, and increasing customer value (Saunila & Ukko, 2014). Within the Dynamic Capability framework, organizations capable of developing innovation capabilities can transform sustainably and maintain their relevance in a rapidly changing business

environment. Empirically, Salunke et al. (2019) demonstrated that innovation-based business strategy influences innovation capabilities, which in turn improves organizational performance. Research by Purwati et al. (2020) in the MSME sector in Indonesia also demonstrated that innovation capabilities are an important mediator in the influence of strategy on performance. Therefore, innovation capabilities can be viewed as a mediating mechanism that bridges business strategy with optimal performance outcomes. H₇: Innovation capabilities mediate the effect of business strategy on business performance.

Methods

This study employed a quantitative approach using the Partial Least Squares, Structural Equation Modeling (PLS SEM) method using Smart PLS 4.1. The population comprised SMEs in Bantul, Yogyakarta, Indonesia. A sample of 145 respondents was selected through purposive sampling, in accordance with SEM analysis requirements with a minimum ratio of 5:1 for the 29 indicators used (Hair et al., 2019). Data were collected through a five-point Likert scale questionnaire distributed online via Google Forms.

Four latent variables were measured: (1) social media with 10 indicators, (2) business strategy with 12 indicators, (3) innovation capability with 4 indicators, and (4) business performance with 3 indicators. The instrument was developed based on studies by Ainin et al. (2015), and Saunila et al. (2014). Validity was tested using outer loading (>0.70) and AVE (>0.50), while reliability was measured using Cronbach's Alpha (>0.70).

Data analysis involved two main stages. First, an evaluation of the outer model to test convergent validity, discriminant validity, and construct reliability. Second, an evaluation of the inner model, including R-square assessment, hypothesis testing through bootstrapping for direct and indirect effects (mediation), and effect size analysis (f^2). The significance level was set at $\alpha = 0.05$ with a T-statistic value >1.96 .

Data Analysis and Results

Validity and Reliability Test

Of the 145 respondents, 53.1% were female and 46.9% were male. The majority were aged 20–29 (44.1%), followed by those aged 30–39 (27.6%), and those aged 40–49 (20.7%). The majority of respondents were high school/vocational school graduates (62.1%) and bachelor's degree graduates (34.5%). The most common respondent status was employee (63.5%), followed by manager (18.6%) and business owner (17.9%). 94% of the SMEs involved were classified as small businesses with 6–19 employees.

In this study, the study used two validity tests. The first validity test is convergent validity. This test is used to determine whether the items intended to measure a variable are indeed collected on the same variable. Convergent validity is considered acceptable if the loading factor value is above 0.5 (Wixom & Watson, 2001). So it can be seen from Table 1 that for the convergent validity test of the livestreaming, online customer review, purchase, and trust variables are met because each item of the variable has a loading factor value > 0.5 . The second validity test is the discriminant validity test, from table 2 it can be seen that the Average Variance Extracted (AVE) value for each variable is > 0.5 so that the discriminant validity is stated to be met because according to Fornell & Larcker, David (1981), validity testing can be met if the Average Variance Etracted (AVE) value exceeds the conventional minimum of 0.5.

Table 1: Loading Results of Convergent Test

Variables	Business performance	Innovation Capability	Social media	Business Strategy
BP1	0.828			
BP2	0.858			
BP3	0.850			
IC1		0.829		
IC2		0.826		
IC3		0.856		
IC4		0.842		
SM1			0.799	
SM10			0.827	
SM2			0.731	
SM3			0.780	
SM4			0.811	
SM5			0.793	
SM6			0.815	
SM7			0.815	
SM8			0.785	
SM9			0.785	
BS1				0.825
BS10				0.798
BS11				0.758
BS12				0.862
BS2				0.766
BS3				0.826
BS4				0.801
BS5				0.836
BS6				0.756
BS7				0.804
BS8				0.811
BS9				0.828

Note:

BP: Business Performance

IC: Innovation Capability

SM: Social Media

BS: Business Strategy

Table 2: Average Variance Extracted

Variables	Average variance extracted (AVE)
Business performance	0.715
Innovation Capability	0.703
Social media	0.631
Business strategy	0.651

For reliability testing in table 3, according to Ghazali (2016), variables are declared reliable if the Cronbach's Alpha value is more than 0.60 and vice versa. From table 3, it can be seen that the Cronbach's alpha value for social media (0.935), business strategy (0.952), innovation capability (0.859), and business performance (0.801), all well above the minimum threshold of 0.70.

Table 3: Cronbach's alpha

Variables	Cronbach's alpha
Business performance	0.801
Innovation Capability	0.859
Social media	0.935
Business Strategy	0.952

Model Testing

The evaluation of the inner model yielded an R^2 value for business performance of 0.498, meaning that 49.8% of the variation in business performance can be explained by the variables in the model. The R^2 value for innovation capability of 0.610 indicates strong predictive power (Table 4).

Table 4: R Square (R^2)

Variables	R-square	R-square adjusted
Business Performance	0.498	0.487
Innovation Capability	0.610	0.604

In addition to conducting the R^2 test, the study also tested model fit by comparing the output estimation results obtained from Smart PLS version 4.1 with the assessment criteria described in Table 5.

Table 5: Model Fit Test Results

Parameter	Rule Of Thumb	Estimated model
SRMR	< 0.10	0.086
d_ ULS	> 0.05	3.229
d_ G	> 0.05	1.571
Chi-square	χ^2 statistik > χ^2 table	1048670 > 42.557
NFI	Approaching the value 1	0.720
GoF	0.1 (small), 0.25 (moderate), 0.36 (strong)	0.610

Based on the model fit test results in Table 5, the model was found to be suitable for analyzing the influence between latent variables. This indicates that the model is able to accurately represent the data and has relevant predictive ability:

1. The obtained SRMR value of 0.086 is below the maximum threshold of 0.10. This result indicates a good level of fit between the empirical data and the estimated model, meaning the difference between the observed covariance matrix and the model covariance matrix is relatively small. Thus, the model can be considered a good fit.
2. The d-ULS value of 3.229, which is greater than the 0.05 threshold, indicates that the model does not exhibit significant deviations. This finding indicates that the model structure is acceptable and approximates the ideal influence expected based on the research data.
3. The d-G value of 1.571, which also exceeds the 0.05 threshold, indicates that the model has a good level of global fit. This indicates that the influence between variables in the model does not differ significantly from the observed empirical data.
4. The Chi-Square statistic value of 1,048.670, which is greater than the Chi-Square value of 42.557 in the table, indicates a good fit for the model. This result confirms that the model adequately represents the data and adequately explains the influence between latent variables.
5. The NFI value of 0.720, which is close to the ideal value of 1, indicates that the model has a fairly good level of fit. Although not yet optimal, the model is still acceptable in describing the fit between the model structure and the research data.

6. The GoF value of 0.610, which is above the 0.36 limit, indicates that the model has a strong level of global fit. This value places the model in the high goodness of fit category, thus the model is considered very suitable for explaining the influence between latent variables in the study.

Hypothesis Testing

Based on Table 6, path analysis and hypothesis testing with standardized regression weights are explained, which can explain the path coefficient of the direction of the relationship between research variables and the significance value to show a significant influence. From Table 6, it can be seen that the direct effect test through bootstrapping shows that all five direct effect hypotheses are accepted. Social media has a positive and significant effect on business performance ($\beta = 0.423$; $T = 5.656$; $p = 0.000$) with a medium effect size ($f^2 = 0.167$), and a positive and very significant effect on innovation capability ($\beta = 0.661$; $T = 11.883$; $p = 0.000$) with a very large effect size ($f^2 = 1.096$). Business strategy has a positive and significant effect on business performance ($\beta=0.313$; $T=3.869$; $p=0.000$; $f^2=0.113$) and on innovation capability ($\beta=0.523$; $T=12.398$; $p=0.000$) with a large effect size ($f^2=0.687$).

Innovation capability has a positive and significant effect on business performance ($\beta=0.255$; $T=2.714$; $p=0.007$). The indirect effect test shows that innovation capability partially mediates the influence of social media on business performance ($\beta=0.168$; $T=2.656$; $p=0.008$) and the influence of business strategy on business performance ($\beta=0.133$; $T=2.565$; $p=0.010$), thus H_6 and H_7 are also accepted.

Table 6: Hypothesis Testing

Hypothesis	Coefficient	P values
Innovation Capability -> Business Performance	0.255	0.007
Social Media -> Business performance	0.423	0.000
Social Media -> Innovation Capability	0.661	0.000
Business Strategy -> Business Performance	0.313	0.000
Business Strategy -> Innovation Capability	0.523	0.000
Social Media -> Innovation Capability -> Business Performance	0.168	0.008
Business Strategy -> Innovation Capability -> Business Performance	0.133	0.010

Discussion

In the operational context of MSMEs, social media serves as a relatively low-cost strategic resource that enables market expansion and customer relationship maintenance (Ainin et al., 2015). Research on Indonesian MSMEs found that social media adoption, supported by innovation capabilities, significantly impacts MSME business performance and competitiveness (Apidana et al., 2024).

The Influence of Business Strategy on Business Performance

The results of this study indicate that business strategy has a positive and significant impact on MSME business performance (Siswanti et al., 2025). This finding indicates that implementing a well-planned business strategy, such as determining market segments, product differentiation, and adapting to environmental changes, can significantly improve business performance by making marketing and operational activities more focused and efficient (Porter, 1990). MSMEs with a clear business strategy tend to be more adaptive in responding to market dynamics, able to identify opportunities, and minimize

business risks, thereby driving increased sales, operational efficiency, and business sustainability (Siswanti et al., 2025).

These findings align with the resource-based view, which emphasizes that leveraging valuable, rare, difficult-to-imitate, and non-substitutable strategic resources and capabilities will create competitive advantage and higher performance (Dionysus, 2020; Kwame Ofori-Baafi1 & Osman Opoku, 2024). Similarly, Porter (1990) asserts that an appropriate business strategy is a key factor in improving company performance and competitiveness, including in the context of SMEs. Thus, the hypothesis that business strategy significantly influences business performance is proven.

The Influence of Social Media on Innovation Capability

The results of this study indicate that social media has a positive and significant impact on the innovation capability of SMEs (Al-Omar et al., 2024). This finding indicates that the use of social media serves not only as a promotional tool but also as a strategic tool that supports the innovation process through rapid access to market information, consumer trends, and the latest business practices (Putra & Hardiansyah, 2025). This access enables SMEs to develop more innovative products, business processes, and marketing strategies (Al-Omar et al., 2024).

In an operational context, social media serves as an interactive medium that facilitates the exchange of information and knowledge between customers, suppliers, and the business community (Garrido-Moreno et al., 2020). This interaction provides relevant feedback for SMEs to create innovations that better align with market needs (Putra & Hardiansyah, 2025). This situation increases SMEs' adaptability and responsiveness to changes in the business environment, thereby enabling sustainable innovation capability development (Al-Omar et al., 2024). This finding aligns with the resource-based view, which emphasizes that utilizing information technology-based resources, including social media, can strengthen an organization's internal capabilities (Ainin et al., 2015). Other research also shows that the use of social media as part of an organization's capabilities significantly contributes to increased innovation capability and company performance (Tajvidi & Karami, 2021). Thus, the hypothesis that social media influences innovation capability can be empirically proven.

The Influence of Business Strategy on Innovation Capability

The results of this study indicate that business strategy has a positive and significant effect on the innovation capability of SMEs. This finding indicates that the implementation of a focused and consistent business strategy encourages increased innovation capability through prioritization, market focus, and more effective resource management (Junaidi & Sudarmiatin, 2024). A clear strategy helps SMEs direct business activities toward product, process, and business model innovation that aligns with market needs (Sulistyo & Ayuni, 2020).

In an operational context, business strategy serves as a decision-making framework that encourages SMEs to be more adaptive to changes in the business environment and integrates internal and external knowledge to create sustainable innovation (Saunila, 2020). This aligns with the resource-based view approach, which emphasizes the importance of strategically utilizing internal resources to build superior capabilities (Teece, 2018). The concepts of dynamic capabilities and business modeling also emphasize that appropriate strategy plays a central role in shaping and strengthening an organization's innovation capability (Zott et al., 2011).

The Influence of Innovation Capability on Business Performance

The results of this study indicate that innovation capability has a positive and significant impact on SME business performance. This finding indicates that SMEs' ability to create and implement

innovations in products, processes, and business models contributes directly to improved business performance (Saunila et al., 2014). SMEs with strong innovation capabilities tend to be more responsive to changing market needs, able to increase product added value, and strengthen competitiveness in a dynamic business environment (Isa et al., 2023).

From a resource-based perspective, innovation capability is viewed as a strategic capability that enables companies to manage and utilize resources more effectively to achieve superior performance (Saunila, 2020). Empirical research on SMEs in Indonesia also demonstrates that innovation capability has a positive and significant impact on performance, particularly marketing performance and business sustainability (Purmono, 2023). Thus, the hypothesis that innovation capability influences business performance can be empirically proven.

Innovation Capability Mediates the Effect of Social Media on Business Performance

The results of this study indicate that innovation capability significantly mediates the effect of social media on SME business performance. This finding indicates that social media utilization not only directly impacts business performance but also works through strengthening innovation capabilities, where social media adoption enhances innovation capabilities and, in turn, drives business performance (Apidana et al., 2024). Social media provides access to market information, customer feedback, and extensive business networks, which SMEs utilize to develop new ideas, products, and processes, thus contributing to improved performance (Rudi et al., 2025).

From the resource-based view and dynamic capabilities perspective, social media is viewed as an external resource that enriches an organization's internal capabilities, particularly innovation capabilities, which translate digital information and interactions into added value for the company (Al-Omar et al., 2024). Studies on SMEs in developing countries also show that social media adoption, through strengthening innovation and marketing capabilities, plays a crucial role in improving business performance (Qalati et al., 2022). Thus, the role of innovation capability as a mediating variable in influencing social media and business performance is proven to be significant.

Innovation Capability Mediates the Influence of Business Strategy on Business Performance

The results of this study indicate that innovation capability significantly mediates the influence of business strategy on SME business performance. This finding indicates that the business strategy implemented by SMEs not only directly impacts business performance but also works by strengthening innovation capabilities, which encourage the creation of more value-added products, processes, and business models (Al Mamun et al., 2022). A targeted business strategy helps SMEs direct resources and business activities toward developing innovations relevant to market needs, thereby enhancing competitiveness and performance.

From the resource-based view and dynamic capabilities perspectives, business strategy is understood as a resource management mechanism that enables companies to build innovation capabilities as strategic internal capabilities that support long-term performance (Teece, 2018). Other research shows that when strategy and innovation capabilities are well integrated, their impact on organizational performance is stronger (Saunila et al., 2014). Thus, the role of innovation capability as a mediating variable in the relationship between business strategy and business performance can be considered significant.

Conclusions and Recommendations

The results of this study indicate that social media has a positive and significant impact on SME business performance. Therefore, increased use of social media in business activities directly contributes to improved business performance (Ainin et al., 2015). Other findings confirm that social media improves company performance by strengthening marketing capabilities and customer relationships (Tajvidi & Karami, 2021). Research on SMEs in developing countries also shows that social media adoption can increase sales, customer relationships, and brand loyalty, while reducing marketing costs (Qalati et al., 2022).

All seven hypotheses were accepted. Social media and business strategy have a positive and significant impact on both business performance and innovation capability. Innovation capability was shown to influence business performance and partially mediate the effects of both predictor variables. The findings strengthen the relevance of the RBV and dynamic capabilities in the context of Indonesian digital SMEs.

Based on the research findings, SMEs are advised to integrate social media into their overall business strategy, not just as a promotional tool. Local governments can also utilize these findings to design digital literacy training programs and strengthen innovation capabilities. For further research, it is recommended to expand the scope of the region and add variables such as digital literacy or entrepreneurial orientation.

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