

## **CHAPTER 2**

### **LITERATUR RIVIEW**

#### **2.1 Small Medium Enterprise (SMEs)**

In Indonesia, the definition of SMEs is regulated in Republican Law Indonesia No.20 of 2008 concerning SMEs. Article 1 of the Law is stated that micro-business is a productive business owned by individuals and/or entities individual businesses that have micro-business criteria as regulated in the Act. Small business is a productive economy business that stands alone, which is conducted by individuals or business entities that are open is a child company or not a subsidiary that is owned, controlled or become a part, either directly or indirectly, from medium or large businesses meet the criteria from medium businesses or large businesses that are meet the criteria for small businesses as referred to in the Act.

SMEs is a productive business unit that stands alone, which is carried out by individuals or business entities in all sectors of the economy. In principle, the distinction between Micro Business, Small Business, Medium Business, and Large Enterprises are generally based on the value of initial assets (not including land and buildings), average annual turnover, or the number of permanent workers. However, SMEs definitions based on these three measurement tools differ by country. Therefore, it is indeed difficult to compare the importance or role of SMEs between countries. For small businesses as referred to in the Act Whereas micro business is productive economic business that stands alone conducted by individuals or business entities that are not children company or non-branch company owned, controlled, or becoming both direct and indirect parts, from microbusinesses, small businesses or businesses large companies that meet the micro-business criteria as referred to in the Act.

The recent OECD definition introduced Small and medium-sized enterprises (SMEs) as non-subsidiary, independent firms that employ fewer than a given number of employees. This number varies across countries. The most frequent upper limit designating an SME is 250 employees, as in the European Union. However, some countries set the limit at 200 employees, while the United States considers SMEs to include firms with fewer than 500 employees. Small firms are generally those with fewer than 50 employees, while microenterprises have at most 10, or in some cases 5, workers (Business Sweden, 2016). SMEs are defined as those that employ 5 – 19

workers for small enterprises and 20 –99 workers for medium enterprises (Indonesian Statistic Center 2008). SMEs with less than 200 million assets, land, and buildings excluded are small industries. Those with more than 200 million up to 5 billion are medium-sized enterprises (Industry and trade ministry). Indonesian Decree Number 9 in the year 1995 defines SMEs as business entities with less than 200 million assets out of its land and building and less than 1 billion annual sales revenue for small enterprises. Indonesian decree No 10 in the year 1999 defines medium scaled enterprises as those of more than 200 million – 10 Billion assets out of its land and building.

### **2.1.1 Small Medium Enterprise (SMEs) Criteria**

In the Act, the criteria used for defining SME as stated in Article 6 is the value of wealth net or value of assets not including land and buildings for the place of business or proceeds annual sales. With the following criteria:

1. Micro business is a business unit that has the most assets of Rp.50 million, excluding land and buildings where the business has the most annual sales results of Rp.300 million.
2. Small businesses with asset values of more than Rp.50 million up to a maximum of Rp.500 million excluding land and buildings where businesses have annual sales results of more than Rp.300 million to a maximum of Rp.2,500,000, and
3. Medium-sized businesses are companies with a net worth of more than Rp.500 million to a maximum of Rp.100 billion from annual sales above Rp.2.5 billion to a maximum of Rp.50 billion.

In addition to using monetary values as a criterion, a number of government agencies such as the Ministry of Industry and the Central Statistics Agency (BPS), so far have also used the number of workers as a measure to differentiate business scales between micro, small, medium and large businesses. For example, according to the National Statistics Agency (BPS), micro businesses are business units with a total of 4 permanent workers, small businesses of 5 to 19 workers, and medium businesses from 20 to 99 people. Companies with more than 99 employees are included in the large business category.

### 2.1.2 Small Medium Enterprise (SMEs) 4.0

The future of SMEs, which are major contributors to most industries and countries (Li et al. 2016), depends largely on their capacity to respond to their clients' expectations while maintaining a competitive advantage on their market. To achieve this, SMEs need to work to constantly improve their industrial management processes, i.e. planning, using resources, controlling production, and measuring and evaluating operational performance (Moeuf, Pellerin, Lamouri, Giraldo, Barbaray, 2017). In all cases, the Industry 4.0 concept is based on the emergence of new technologies such as cloud computing, Internet of things, cyber-physical systems and big data. Such technologies should improve the transmission of information throughout the entire system, which enables better control and operations to be adapted in real time according to varying demand. Industry 4.0 concepts may also be applied for transforming the nature of products and services provided by organisations (Porter and Heppelmann 2014). However, the intent of this paper is to focus solely on the impact of Industry 4.0 on the production planning and control functions that is also referred by some researchers to the concept of Smart Factory or Digital Manufacturing. As technology keeps advancing at fast pace, SMEs must be prepared to adapt to new technology environment, in order to, at least, stay competitive. Moving towards the so-called 4th industrial revolution, several challenges are being raised. Importance of this topic is expressed in Figure 2.1, showing projected share of different parts of businesses.

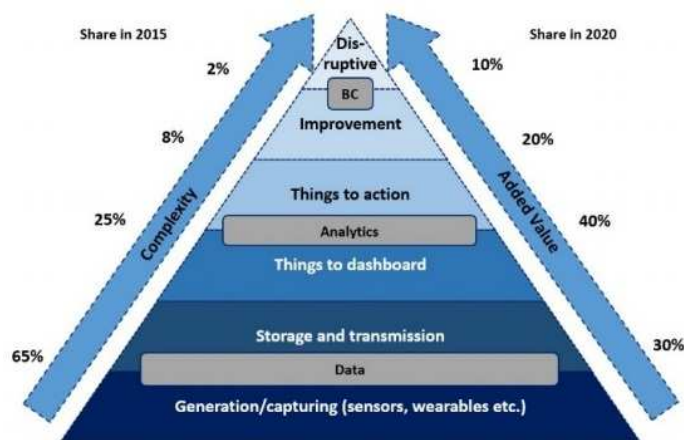


Figure 2.1 Maturity model

Source: Safar, Sopko, Bednar, Poklemba (2018)

As shown in Figure (1), Industry 4.0 gives companies the opportunity to acquire important information about methods that should be implemented in the company's internal processes, resulting in an increase in value added for companies. Analyzed a number of processes and cases of Industry 4.0 application in multiple companies, creating a six-grade maturity model that includes three important layers: “data”, “analytics” and “business cases”. The authors also estimate the added value of processes in 2020 in the layers by implementing I4.0 based on the data obtained from the analyzed companies. However, SMEs could see some troubles in implementing new technologies, and also in modifying and adapting their business models. Especially for industrial SMEs with significantly limited sources, compared to large enterprises, some guidance could be good starting point for determining strategy of implementation elements of 4.0 concept. (Safar, Sopko, Bednar, Poklemba, 2018).

### **2.1.3 Maturity Model to the Industry 4.0 revolution**

In order to apply the Maturity Model to implement Industry 4.0 scenario (Figure 2.1), we define this maturity scale for the three stage process model with the next levels (Ganzarain and Errast, 2016):

1. Initial: It doesn't exist a company specific industry 4.0 vision
2. Managed: There exist a Roadmap of industry 4.0 strategy
3. Defined: customer segments, value proposition and key resources defined
4. Transform: Transform the strategy into concrete projects.
5. Detailed BM: Transformation of Business Model

The analyzed organizations, which have not adopted the Industry 4.0 philosophy, are at level 1 and progress through the levels of maturity by adopting the goals and practices which are defined for the processes at each level.

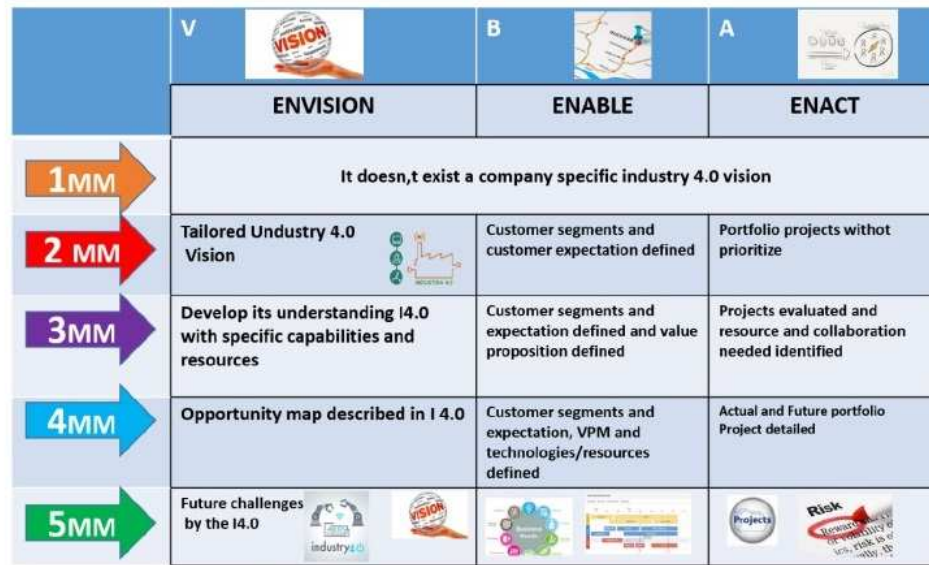


Figure 2.2 Maturity Model to the Industry 4.0 revolution

Source: Ganzarain and Errasti (2016)

#### 2.1.4 Small Medium Enterprise (SMEs) Food and beverage

Small and Medium-Sized Enterprises (SMEs) play a significant role in the economic growth and development of a country through the production of quality products (Chen, 2009; Abdul, et.al, 2017). Food and beverage is a sub-sector of the manufacturing sector which contributes to about 10% of manufacturing output. Of the total 37861 SMEs in the manufacturing sector, 6016 SMEs are involved in the processing of food and beverage products, ranking them as the second largest concentration of SMEs (Abdul, et.al, 2017). At present, the food and beverage industry seem to be one of the potential industries; thus, ensuring the quality of food and beverage products is indispensable. The quality of a food and beverage product refers to every single aspect of the product including its performance, conformance to specifications, aesthetic, durability, reliability, safety, nutritional values and hygiene which help to continuously improve the quality of food and beverage products of SME entrepreneurs (Talib *et al.*, 2009; Abdul, et.al, 2017).

These identified trends in the food and beverage industry have created opportunities for investments in the expansion of the market. thus, the food and beverage manufacturing SMEs should grasp this opportunity. In line with the trends, Food and Beverage small and medium enterprises (F&B SMEs) play a major role in the economy. SMEs increase the total number of enterprises, increase the number of

employees and SMEs is also contribute to GDP (OECD, 2016). Despite the importance of this sector, and despite the presence of a multitude of similar studies conducted in large organizations, little is known about the barriers encountered and the innovation strategies that Thai F&B SMEs adopt during their new product development (NPD) process. By following the tradition of many other studies on SMEs, the current study is highly informed by the findings from large organizations and attempts to investigate relevance and applicability of those findings to SMEs' contexts. This constitutes the main motivation and theoretical lens of the current study, particularly at a time when globalization is harshly affecting less innovative organizations, especially if they belong to the SME category, as reflected in several current studies (Chaochotechuang and Mariano, 2016).

### **2.1.5 Small Medium Enterprise (SMEs) Contribution to Economic Development**

SMEs' contribution to economic development as follows (Me, 2018):

1. Strong catalyst for technological development hence aids in reduction of the development gap (which is largely a technology gap)
2. A major source of employment since their modes of operation is more labor intensive.
3. A major source of domestic capital formation through their mobilization of private savings and channeling of such in productive investment.
4. Aid the process of redistribution of incomes.
5. Constitute a critical source of specialization for most large organizations operating in the economy.

## **2.2 Knowledge Management**

### **2.2.1 Nature of Knowledge**

Knowledge is the process of translating information (such as data) and experience into a meaningful set of relationship which is understood and applied by an individual (Debowski, 2006). According to Dalkir (2017) Knowledge is a subjective and valuable information that is used to understand; derived from accumulated experience; combining perception, trust, and values. The knowledge classification in the tacit and explicit dimensions was, initially proposed by Polanyi, 1966. Tacit knowledge is deeply rooted in action, commitment, and involvement and, thus, it is hard to formalize and communicate. Explicit knowledge is codified and

transmittable in formal, systematic language and thus it is captured in libraries, archives, and databases (Nonaka, 1994; Schniederjans, Curado and Khalajhedayati, 2019). Tacit knowledge tends to reside within the heads of “knowers” who wear explicit knowledge usually contained within tangible or concrete media (Dalkir, 2017).

Table 2.1 Comparison tacit and explicit

Tacit	Explicit
Ability to adapt, to deal with new and exceptional situation	Ability to disseminate, to reproduce, to access and re-apply throughout the organization
Expertise, know-how, know-why, and care-why	Ability to teach, to train
Ability to collaborate, to share a vision, to transmit a culture	Ability to organize, to systematize, to translate a vision into a mission statement, into operational guidelines.

Source: Dalkir, 2017

### 2.2.2 Definition Knowledge Management

Knowledge management refers to identifying and leveraging the collective knowledge in an organization to help the organization compete (Alavi and Leidner, 2001; Bashir and Farooq, 2019). According to Bennet, et al. (2015) Knowledge management is the management practice to leverage knowledge to add value to organization advantage. Another definition came from Dalkir (2017) knowledge management is the deliberate and systematic coordination of an organization's people, technology, process, and organizational structure in order to add value through reuse and innovation. This is achieved through the promotion of creating, sharing, and applying knowledge as well as through the feeding of valuable lessons learned and best practices into corporate memory in order to foster continued organizational learning. That's mean knowledge management concept and practice are relevant for the learning organization. “learning organization an organization that is capable of continual regeneration from the variety of knowledge, experience and skills within a culture that encourages questioning and challenge” (Johson, Ragner, Scholes, Angwin and Whittington, 2016).

Wiig (1993) in Dalkir (2017) consider knowledge management is approached and examined from three perspectives, with different horizon and purposes:

1. *Business perspective*: focusing on why, where, and to what extent the organization must invest in or exploit knowledge. Strategies, product and services, alliances, acquisitions, or divestments should be considered from knowledge-related points of view.
2. *Management perspective*: focusing on determining, organizing, directing, facilitating, and monitoring knowledge-related practices and activities required to achieve the desired business strategies and objectives.
3. *Hans-on perspective*: focusing on applying the expertise to conduct explicit knowledge related work and tasks.

In fast- changing business environment, organization and employees are expecting to continue learning and catch up with the latest trend, a successful learning organization will provide sources to help employees develop their professional skill and strengthen collaboration within the organization. To summary, knowledge management is an essential source of competitive advantage. Knowledge management is the important organization resource to compete and sustain in industry, and also the basic need for a learning organization.

### **2.2.3 Knowledge Management in Small Medium Enterprise (SMEs)**

Organizations who are successful in leveraging knowledge, normally witness increased efficiencies in operations, higher rates of successful innovations, increased levels of customer service, and an ability to have foresight on trends and patters emerging in the marketplace. Besides the traditional reasons for managing knowledge, SMEs, in particular, must pay close attention to knowledge management for several salient reasons. SMEs compete on their know-how and hence have to use knowledge to their advantage, even more so than traditional resources. SMEs normally do not have deep pockets to spend on resources such as land, labor, and capital. They must do more with less. Knowledge housed in the SME, must be leveraged so that goals can be achieved in an effective and efficient manner. While an SME might be constrained by not enough capital or labor, their knowledge is bountiful and, in many cases, an unlimited resource. The only way an SME can limit this resource is by not using it effectively. Individuals who open up SMEs do so



because they have knowledge in key areas of competencies and think they can compete using such knowledge. It is hence important that they remain successful in leveraging knowledge. Having knowledge is one thing and using it effectively towards organizational ends is quite another. It will be useful for an SME owner to house knowledge in his/her mind, and not use it for business decision-making. Besides, using the knowledge directly, the owner of SMEs must also transfer knowledge to his/her employees. Seldom, do SMEs have the capabilities to recruit the best minds in the business; hence they must settle for less qualified but motivated individuals. These individuals must be trained and taught how to be successful employees. Training calls for transferring knowledge to the new hires, a function of knowledge management. Moreover, in cases where the SME has plans of expansions, they must be able to duplicate knowledge and the apply knowledge across geographic locations. In one restaurant, the owner spent three years training his protegee' about the ins and outs of managing a restaurant before he decided to open a new location. Given all of this need to manage knowledge in SMEs, little is known about how SMEs fair in knowledge management (Desouza and Awazu, 2015)

#### **2.2.4 Dimension dan Indicators Knowledge Management**

Knowledge acquisition is the process that company uses for obtaining new information and knowledge (Jimenez and Valle, 2013; Turulja and Bajgoric, 2017). Liao and Wu (2009) in Turulja and Bajgoric (2017) defines knowledge acquisition as the process to seek and acquire new knowledge which involves the creation of new knowledge out of existing knowledge through collaboration between individuals and business partners. Indicators: knowledge about our suppliers, knowledge with our business partners, knowledge about new product/ services within our industry, marketing performance.

Knowledge conversion is defined as company's ability to make knowledge useful (Liao and Wu, 2009; Gao, 2006; Turulja and Bajgoric, 2017). Some of the process that potentiate knowledge conversion are knowledge integration, organization, structuring, combination, distribution and coordination (Gao, 2006; Turulja and Bajgoric, 2017). Indicators: absorbing knowledge from individuals into the organization, absorbing knowledge from business partners into the organization, integrating, replacing outdated knowledge.

Knowledge Application refers to the application of existing knowledge for the production of goods and services (Grand, 1996; Turulja and Bajgoric, 2017) or for the process that enable the realization of the knowledge practical values (Lee *et al.*, 2012; Turulja and Bajgoric, 2017). Indicators: improve efficiency, changing competitive condition, accessible to those who need it, solving problems

### **2.3 Innovation**

According to Johson, Ragner, scholes, Angwin and whittington (2016) “innovation the conversion of new knowledge into a new product, process or service *and* the putting of this new product, process or service into actual commercial use. Another definition came from Carayannis, Samara, dan Bakouros (2015) Innovation refers to the process of conversion of an idea into a merchandized product or service, a new form of business organization, a new or improved functional production method, a new product presentation way (design, marketing) or even to a new service rendering method. It may also refer to the design and construction of new industrial equipment, the implementation of a project with a new management or may refer to a new way of thinking to deal with a situation or a problem. (Green Paper of the E.U. on innovation). Technological evolution and the parallel social and economic changes take place through the realization of innovation. A society’s ability to innovate largely constitutes a mechanism of renewal and development. Innovation regards every aspect of economic or productive process. At the level of an enterprise or an organization, innovation is mainly realized either by developing new products and services or by restructuring production–operation processes. The continuous innovative effort for new products-services or new productive processes create a competitive advantage in three critical areas:

1. Evaluation of the resources involving research and development activities, application of a new technology, sales productivity, production etc. new productive investments and expansion into new markets or broadening of the customer base.
2. Development and renewal of the entity with investments and growth, professional evolution opportunities for human resources, new recruitments and optimism, high morale and spirit.

3. Business success building on the reputation and attracting new customers, image of a dynamic business, products that distinguish from the competition, ongoing development and making hard for the competition to gather pace.

### 2.3.1 Characteristics of Innovation

According to Robbins Coulter (2017) Innovative organizations tend to have similar cultures. They encourage experimentation, set creativity goals, reward both successes and failures, and celebrate mistakes. An innovative organization is likely to have the following characteristics.

1. *Accept ambiguity.* Too much emphasis on objectivity and specificity constrains creativity.
2. *Tolerate the impractical.* Individuals who offer impractical, even foolish, answers to what-if questions are not stifled. What at first seems impractical might lead to innovative solutions. Encourage entrepreneurial thinking.
3. *Keep external controls minimal.* Rules, regulations, policies, and similar organizational controls are kept to a minimum.
4. *Tolerate risk.* Employees are encouraged to experiment without fear of consequences should they fail. “Failure, and how companies deal with failure, is a very big part of innovation.” Treat mistakes as learning opportunities. You don’t want your employees to fear putting forth new ideas. In an uncertain economic environment, it’s especially important that employees don’t feel they have to avoid innovation and initiative because it’s unsafe for them to do so. A recent study found that one fear employees have is that their coworkers will think negatively of them if they try to come up with better ways of doing things. Another fear is that they’ll “provoke anger among others who are comfortable with the status quo.” In an innovative culture, such fears are not an issue.
5. *Tolerate conflict.* Diversity of opinions is encouraged. Harmony and agreement between individuals or units are *not* assumed to be evidence of high performance.
6. *Focus on ends rather than means.* Goals are made clear, and individuals are encouraged to consider alternative routes toward meeting the goals. Focusing on ends suggests that several right answers might be possible for any given problem.

7. *Provide positive feedback.* Managers provide positive feedback, encouragement, and support so employees feel that their creative ideas receive attention.
8. *Exhibit empowering leadership.* Be a leader who lets organizational members know that the work they do is significant. Provide organizational members the opportunity to participate in decision making. Show them you're confident they can achieve high performance levels and outcomes. Being this type of leader will have a positive influence on creativity.

### **2.3.2 Small Medium Enterprise (SMEs) Innovation Capabilities**

Three main approaches for investigating SMEs' innovation capabilities include (Chaochotechuang and Mariano, 2016):

1. Emphasizing innovation-based science and technology drivers such as R&D and related human capital
2. Emphasizing learning-by-doing, learning-by-using, and learning-by-interacting strategies.
3. Combining the former two approaches with leadership strategies theorized as change agents.

### **2.3.3 Dimensions and Indicators of Innovation**

According to (Goh, 2005; Hussain et al.,2019) innovation is a change in the existing products, services, ideas, and operations new to the end user or unit of adoption. Creativity and innovation have become an important thing to survive in the competitive markets and firms in established industries investing heavily in R&D to stay competitive (Hayes et al., 2005; Hussain et al.,2019). For most SMEs, innovation is the only remedy for survival Hussain et al. (2019). An indicator of Innovation is a new idea, new methods, being inventive, marketing novel.

## **2.4 Business Performance**

Business performance management is a critical segment of the company that is a combination of human resources and knowledge management to achieve competitiveness (Turulja and Bajgoric, 2017). Performance is the end result of activities carried out and for any business it is concerned with the general efficiency or productivity. Two ways to deal with performance has been recognized in

literatures: the financial or “sales-based” and the non-financial or “firm-based”. Whereas the financial is measured with dimensions such as profitability, growth, productivity, level of sales revenue, market share and product, return on investments, product added value; the non-financial is measured in terms of employee development, customer satisfaction, job satisfaction and efficient organizational internal processes (Eniola and Ektebang, 2014). Therefore, the practice of strategic management is justified in terms of its ability to improve organizations’ performance (Me, 2018)

According to Hajar (2015) key measures of business performance have been used in the literature to assess the impact of business environment, strategic decisions, and manufacturing strategy on firm performance is decided to measure firm performance through: (i) sales growth, (ii) profit growth, and (iii) assets growth. Reijonen (2008) defines business performance as an indicator that measures business’ efficiency and effectiveness in achieving.

#### **2.4.1 Dimensions and Indicators of Business Performance**

Organizational business performance is a first-order reflective measurement model consisting of five indicators adopted from (Chen et al.,2009; Turulja and Bajgoric, 2017) subjective indicators of business performance:

1. For the past few years, enhanced sales
2. For the past few years, have been profitable
3. For the past few years, have achieved profit objectives
4. For the past few years, have achieved market share objectives
5. For the past few years, have achieved return on investment

### **2.5 Relationships between variables**

#### **2.5.1 Effect of knowledge management on business performance**

Knowledge management (KM) as a concept has become important because of the growing awareness of the importance of knowledge for the organization’s prosperity and survival (Byukusenge dan Munene, 2017). This research was supported by Byukusenge and Munene (2017) KM influences BP. KM has a value = 0.074 which means there is a significant relationship between KM and BP, because of for instance, Wang and lin (2013) in Byukusenge and Munene (2017) confirmed that knowledge management orientation played positive roles in promoting

organizational performance in china. This research was supported by Abdullah (2019) “there is a positive relationship between knowledge management and SMEs performance”. KM has a value = 262 which means there is a significant relationship between KM and BP, because According to Wiklund & Shepherd (2003) in Abdullah (2019), the application of knowledge could maintain firm’s competitive advantage by determining and exploit market opportunities. Employees knowledge play a role as one of the dynamic elements in the entrepreneurial process through vibrant network, effective knowledge management and proper intellectual asset. this research was also supported by Mardani, Nikoosokhanb, Moradib, Doustar (2018) “there is a positive relationship between knowledge management and organizational performance”. KM has a value = 0,176 yang which means there is a significant relationship between KM and BP, because KM can improve corporate performance and competitiveness (Civi, 2000; DeTienne & Jackson, 2001; Holsapple & Jones, 2004, 2005; Mardania, Nikoosokhanb, Moradib, Doustar, 2018 ).

### **2.5.2 The Influence of Innovation on business performance**

Innovation (IN) provide firm with a strategic orientation to achieve sustainable competitive advantage (Byukusenge dan Munene, 2017). This research was supported by Byukusenge dan Munene (2017) “there is a significant relationship between innovation and business performance in SMEs”. Has value = -0,046 which means there is a significant relationship between IN and BP, because Ar and Baki (2011) in Byukusenge dan Munene (2017) found that product and process innovations led to superior performance was measure by sales, market share, and profitability. This research was supported by Hajar (2015) “there is a significant, positive effect exist between innovation and firm performance”. Has value = 0.432 which means there is a significant relationship between IN and BP, because According to Hajar (2015) found that the ability of owner-managers in identifying and overcoming barriers to innovation and maximizing innovation resources will result in a product that can be accepted by customer, which in turn is able to compete with the performance of the company above the industry average. This research was supported by Juárez, Lema, and Guzmán (2016) “there is a significant, positive effect exist between innovation and firm performance”. Has value = 0.201 which means there is a significant relationship between IN and BP, because According to Bagnoli and Vedovato (2014); Roxas, Battisti and Deakins (2014) in Juárez, Lema, and

Guzmán (2016) Organizations are likely to achieve substantial improvements in innovation and better performance, which can lead to greater productivity.

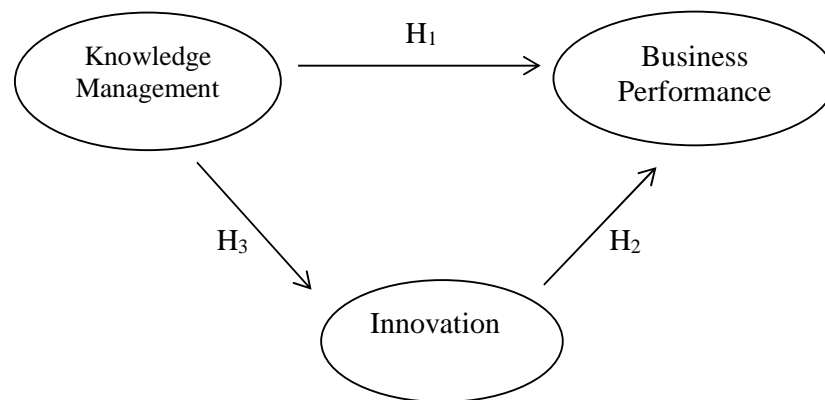
### **2.5.3 Influence of Knowledge Management on Innovation**

A KM system that expands the creativity envelope is thought to improve the innovation process through quicker access and trend of new knowledge (Majchrzak et al., 2004; Mardani, Nikoosokhanb, Moradib, Doustar, 2018). Also, effective KM is a critical success factor to launch new products. In this sense, this paper supports that one of the factors influencing innovation capacity in organizations is knowledge, and its management (Mardani, Nikoosokhanb, Moradib, Doustar (2018). This research was supported by Mardani, Nikoosokhanb, Moradib, Doustar, 2018) “there is a significant relationship between Knowledge Management (KM) and Innovation (IN)”. has a value = -0,195 which means there is a significant relationship between KM and IN, because the innovative efforts include discovery, experimentation, and development of new technologies, new products and/or services, new production processes, and new organizational structures. Innovation is about implementing ideas (Borghini, 2005). This research was supported by Byukusenge dan Munene (2017) “there is a significant mediation effect of innovation on the relationship on the relationship between knowledge management and business performance”. Has value = 0.308 which means there is a significant relationship between KM and IN, because According to wilson (2007) in Byukusenge and Munene (2017) found that innovation is the transformation of knowledge into new products, practices, process and service. This research was supported by Mardani, Nikoosokhanb, Moradi, Doustar (2018) “innovation is positively related to firm performance”. Has value = 0.156 which means there is a significant relationship between KM and BP, because According to Mardani, Nikoosokhanb, Moradi, Doustar (2018) found that Innovation quality is another key factor influencing firm performance. A high quality of innovation is adopting numerous new products, processes or practices across a broad cross-section of organizational activities.

## 2.6 Research Model

From the literature review developed about and the research questions was found that the current research has similarity variables and research objective with Byukusenge and Munene (2017) in analyzing the influence of Knowledge Management, Innovation and Business Performance in SMEs.

The research model is modeled after Byukusenge and Munene (2017) a research model is constructed as follows:



Frame 2.3 Research Model

Source: Byukusenge and Munene, 2017

## 2.7 Hypothesis

According to Sekaran and Bogie (2016) hypothesis is a tentative, yet testable, statement that predicts what you expect to find in your empirical data”. Meanwhile, according to Sugiyono (2018), the hypothesis is the third step in research, after researchers have raised the theoretical foundation and frame of mind. The hypothesis is a temporary answer to the formulation of the research problem, where the research problem formulation has been stated in the form of sentences and statements. The hypothesis in this study is:

H<sub>1</sub>: Knowledge management has a positive and significant influence on Business performance

H<sub>2</sub>: Innovation has a positive and significant influence on Business performance

H<sub>3</sub>: Knowledge management has a positive and significant influence on Innovation