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Enhancing the MSMEs' Performance Through Strategic Flexibility: Does Competitive Intensity Matter?

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ABSTRACT

Despite being a key driver of the national economy, Micro, Small, and Medium Enterprises (MSMEs) continue to face significant challenges in enhancing their performance. While prior research has examined various factors influencing MSMEs' performance, limited attention has been given to the role of strategic flexibility and competitive intensity. This study aims to investigate the impact of strategic flexibility on MSMEs' performance, with competitive intensity as a moderating factor. To achieve this, the study involved 80 MSMEs from Yogyakarta and Sleman in data collection. Subsequently, the data was examined by employing a Partial Least Squares Structural Equation Modeling (PLS-SEM), ensuring a comprehensive evaluation of the proposed relationships. The findings reveal that strategic flexibility plays a direct role in improving MSMEs' performance, regardless the level of competitive intensity. This insight offers valuable theoretical contributions while also providing practical managerial implications for MSME owners and managers, emphasizing the importance of cultivating strategic flexibility to sustain business growth in an increasingly dynamic market environment.

Keywords: Micro, Small, and Medium Enterprises; MSMEs; Strategic Flexibility; Competitive Intensity; MSMEs' Performance

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INTRODUCTION

Micro, small, and medium Enterprises (MSMEs) have long been recognized as the backbone of Indonesia's economy. Accounting for more than 99% of all business entities (Tambunan, 2022), MSMEs contributing approximately 61% to the country's Gross Domestic Product (GDP) and employing around 97% of the total workforce (Limanseto, 2023). Despite their significant contribution, Indonesian MSMEs face substantial challenges in maintaining their performance, with 84% of them experiencing a decline in revenue (Sidik, 2022). This phenomenon underscores the difficulty MSMEs encounter in sustaining their performance in an increasingly dynamic and competitive market environment.

Recent studies have identified several critical factors that enhance the performance of small and medium enterprises (SMEs) across different countries. For instance, (Clemente-Almendros et al., 2025) highlight the importance of adopting environmental criteria to improve SMEs' performance in Spain. In addition, Giordino et al. (2025) emphasize the role of growth acceleration capabilities in driving SMEs' performance in Italy. Moreover, Malik et al. (2025) found that organizational learning about sustainability plays a crucial role in enhancing SMEs' performance in India. Furthermore, empirical research conducted in Ghana suggests that Total Quality Management (TQM) practices are key antecedents in improving SME performance (Tetteh et al., 2025).

While those previous studies provide valuable insights into factors influencing SMEs' performance, research on the role of strategic flexibility and its impact on business performance remains limited, particularly within the Indonesian MSMEs context. Whereas, according to dynamic capabilities theory, businesses that continuously develop and refine their core capabilities are more likely to achieve superior performance (Teece et al., 1997). In this regard, strategic flexibility serves as a manifestation of a firm's dynamic capabilities (Herhausen et al., 2021), indicating that it could play a crucial role in enhancing MSMEs' performance.

Recent studies have explored the influence of strategic flexibility on various organizational outcomes. For instance, Lin et al. (2025) demonstrated that strategic flexibility amplifies the impact of digital platforms on organizational knowledge. Additionally, research conducted by Li et al. (2025) confirmed that strategic flexibility plays a crucial role in fostering innovation. However, these studies have yet to examine how strategic flexibility directly influences organizational performance, leaving a gap in understanding its impact on MSME outcomes.

Despite this, some other studies have successfully validated the effect of strategic flexibility on performance outcomes. For example, Abdullatif & Masri (2024) found that strategic flexibility significantly enhances business performance. Similarly, Dwikat et al. (2023) concluded that strategic flexibility serves as a determinant for sustainable performance, particularly in turbulent environments. Nevertheless, these investigations have primarily focused on the direct effects of strategic flexibility on business performance, often overlooking the situational context that may underpin this relationship.

Whereas, Keskin et al. (2021) argue that competitive intensity is a fundamental dimension of the external business environment that increasingly influences firm performance. Within this context, competitive intensity motivates firms to undertake necessary strategic actions (Kankam-Kwarteng et al., 2019). Furthermore, competitive intensity has been widely recognized as a moderating variable in studies exploring the relationship between SMEs' performance and its antecedents (Kankam-Kwarteng et al., 2019). However, a recent study by Otache (2024) has yet to provide empirical evidence on the moderating effect of competitive intensity in the relationship between SMEs'

performance and its determinants. Therefore, this study seeks to explore the moderating role of competitive intensity in the relationship between strategic flexibility and business performance within the context of MSMEs in Indonesia.

Addressing these research gaps illustrated above, this study aims to explore the role of strategic flexibility in enhancing MSMEs' performance. Furthermore, it explores how competitive intensity moderates the strategic flexibility-MSMEs' performance link. Theoretically, this study contributes by demonstrating strategic flexibility as a reflection of dynamic capabilities theory, moderated by competitive intensity in influencing MSMEs' performance. From a practical perspective, in light of the persistent challenges hindering MSMEs' sustainability, the results provide meaningful insights that can guide MSME owners and managers in designing strategic actions to enhance performance through the lens of dynamic capabilities.

LITERATURE REVIEW

Strategic Flexibility

Strategic flexibility refers to the firm's ability to proactively adjust to changing environmental conditions, enabling it to create and sustain a competitive advantage (Bashir et al., 2023; Brozovic, 2018; Xiu et al., 2017). According to Sanchez (1995), strategic flexibility reflects an organization's capacity to restructure, reallocate, and modify resources, processes, and strategies enables adaptation to environmental changes. Furthermore, strategic flexibility is largely conceptualized as the ability to effectively respond and react to evolving market conditions (Brozovic, 2018). As a key component of dynamic capabilities, strategic flexibility allows firms to optimize resource allocation and adjust existing operational routines to maintain their competitive position (Zhou & Wu, 2010). For instance, Wright & Snell (1998) describe strategic flexibility as an organization's capacity to swiftly align its resources and activities with shifting environmental demands.

Competitive Intensity

Competitive intensity is a critical factor in shaping strategic decision-making, particularly for MSME owners who must consider both consumer preferences and their own perceptions of the business environment when formulating strategies (Homburg et al., 2002). In this context, the degree of competition in a given market is influenced by the number of firms operating within the industry and the extent to which rivalry occurs across different market segments (Keskin et al., 2021). Moreover, competitive intensity is driven by several key factors, including pricing strategies, product quality, service excellence, product differentiation, and technological advancements (Keskin et al., 2021). A highly competitive environment compels businesses to adopt strategic actions that enhance their market positioning and ensure long-term sustainability (Kankam-Kwarteng et al., 2019; Keskin et al., 2021).

Business Performance

Hussaini & Muhammed (2018) argue that business performance reflects a company's ability to sustain operations, achieve growth, and operate efficiently while maintaining profitability. It serves as an essential indicator of how well a business meets its objectives and demonstrates progress over time (Hussaini & Muhammed, 2018). According to Cho & Dansereau (2010), organizational performance is assessed by comparing a company's actual outcomes against its predefined goals and strategic targets. Similarly, Tomal & Jones (2015) define organizational performance as the tangible results achieved by a company, measured in relation to its expected outcomes. These perspectives highlight the importance of performance evaluation as a critical tool for understanding a firm's overall effectiveness in a dynamic business environment.

Hypothesis Development

Strategic Flexibility and MSMEs' Performance

Grounded in dynamic capabilities theory, strategic flexibility is recognized as an essential organizational capability that enables firms to optimize their available resources effectively (Bashir, 2023). This capability becomes particularly vital for businesses operating in emerging markets, where resource constraints necessitate continuous reconfiguration to sustain growth and competitiveness (Zahoor & Lew, 2023).

The impact of strategic flexibility on business performance has been well-documented in the literature, emphasizing its role as a key driver of corporate competitiveness (Bashir, 2023; Brozović et al., 2023; Zhang et al., 2014). Prior empirical studies have demonstrated that firms with higher strategic flexibility are better equipped to navigate volatile business environments, allowing them to respond proactively to market shifts and maintain operational resilience (Bashir, 2023). Given these insights, this study posits that strategic flexibility plays a pivotal role in enhancing MSMEs' performance, enabling them to achieve long-term sustainability amid unpredictable market dynamics.

H1: Strategic flexibility positively impacts the performance of MSMEs.

Strategic Flexibility, Competitive Intensity, and MSMEs' Performance

Competitive intensity plays a vital contribution in shaping business strategies, as it compels firms to adopt proactive measures to remain competitive (Guo & Cao, 2014; Kankam-Kwarteng et al., 2019). As competition intensifies, businesses are more likely to adopt aggressive strategies to outperform rivals and secure their market position (Kankam-Kwarteng et al., 2019). In this context, strategic flexibility emerges as a vital capability that enables firms to respond effectively to competitive actions and dynamic market conditions (Otache, 2024).

Existing literature widely acknowledges that strategic flexibility contributes significantly to enhancing business performance (Bashir, 2023; Brozović et al., 2023; Otache, 2024; Zahoor & Lew, 2023). However, Otache (2024) argues that the effect of strategic flexibility towards the performance of MSMEs is contingent upon the level of competition intensity in the market. This suggests that in highly competitive environments, MSMEs are more likely to develop greater strategic flexibility to sustain superior performance, as also expressed by Otache (2024) in the context of SMEs. Moreover, competition intensity has been widely recognized as a moderating factor in various studies exploring the relationship between SMEs' performance and its antecedents (Kankam-Kwarteng et al., 2019). Hence, this study argue that as competitive intensity escalate, MSMEs are driven to proactively refine their strategic approaches, optimize resource allocation, and enhance their resilience in an increasingly dynamic market environment.

H2: Competitive intensity moderates the association between strategic flexibility and the performance of MSMEs.

METHODOLOGY

Sample

This study employed a survey-based quantitative approach to collect data from MSMEs based in Yogyakarta and Sleman. The sampling approach of non-probability was employed, specifically convenience sampling, to select participants. In this context, studies involving SMEs frequently encounter challenges related to the limited diversity of respondents and the time constraints faced by SME owners or managers, therefore, convenience sampling was adopted to capitalize on the availability and active participation of these respondents (Creswell & Creswell, 2017). The required minimum sample size was established through statistical power analysis. A statistical power range between 0.21 and 0.3 at a 5% significance level in Partial Least Squares Structural Equation Modeling (PLS-SEM) approach was targeted, where a minimum of 69 participants was required for the study (Hair et al., 2022).

Table 1 provides an overview of the respondents' demographic characteristics, indicating that the final sample comprised 80 MSMEs, exceeding the minimum required sample size. Drawing insights from data presented in the table, the majority of respondents in this study are MSME owners (67.50 percent), while the remaining 32.5 percent are managers, indicating that most strategic and operational decisions are made by business proprietors. Regarding business longevity, a significant proportion of MSMEs are in their early stages, with 63.75 percent operating for 1–3 years and an additional 20 percent between 3–5 years. Meanwhile, MSMEs aged 5 to 10 years and more than 10 years are 12.5 percent and 3.75 percent respectively.

The industry distribution highlights that culinary businesses dominate (43.75 percent), followed by fashion (12.5 percent), services (11.25 percent), and beauty/cosmetics (8.75 percent). Other industries, including agribusiness, handicrafts, and automotive, collectively account for a smaller fraction, reinforcing the diversity of MSMEs included in the study. Regarding annual revenue, 67.50 percent of MSMEs reported earnings below IDR 300 million, representing the common financial range of micro-enterprises. Meanwhile, 28.75 percent ranged between IDR 300 million and IDR 2.5 billion classifying them as small enterprises, and only 3.75 percent reported revenues between IDR 2.5 billion and IDR 50 billion, positioning them as medium enterprises.

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Table 1. Demographic Characteristics of Respondents

Characteristics		Frequency	Percentage (%)
Occupational Role	MSME Owners	54	67.50
	MSME Managers	26	32.50
Firm Age	1 – 3 years	51	63.75
	3 – 5 years	16	20.00
	5 – 10 years	10	12.50
	> 10 years	3	3.75
Industry Sector	Culinary	35	43.75
	Fashion	10	12.50
	Services	9	11.25
	Beauty/Cosmetics	7	8.75
	Agribusiness	3	3.75
	Handicrafts	3	3.75
	Automotive	3	3.75
	Other Industries	10	12.50
Annual Revenue	≤ IDR 300 million	54	67.50
	> IDR 300 million – 2.5 billion	23	28.75
	> IDR 2.5 billion – 50 billion	3	3.75

Source: Primary Data Processed, 2024

Measurement

To ensure the reliability and validity of constructs, the study utilized measurement scales adapted from previously validated sources. This study measured research variables using

a five-point Likert scale, with responses ranging from 1 (strongly disagree) to 5 (strongly agree) as suggested by Sekaran & Bougie (2016). Strategic flexibility (SF) was measured using three items adapted from (Bashir, 2023). Meanwhile, competitive intensity (CI) was assessed with six items derived from Jaworski & Kohli (1993). Moreover, business performance (P) was evaluated using five items adapted from Abeysekara et al. (2019).

Table 2 presents the results of the measurement model evaluation, assessed following PLS-SEM guidelines using key indicators such as outer loadings, the Fornell-Larcker Criterion, Composite Reliability, and Average Variance Extracted (AVE), which are essential for assessing construct validity and reliability, as suggested by Hair et al. (2022). To ensure the robustness of the measurement model, this study employed a two-phase evaluation process. In the initial evaluation stage, items with outer loadings below 0.4, namely P3, P4, CI2, CI4, and CI5, were removed as they did not meet the required threshold for convergent validity, adhering to the recommendations of Hair et al. (2022).

Table 2. Assessment of the Measurement Model

Items	Outer Loadings	AVE	Fornell-Larcker Criterion	Composite Reliability
P1	0.812			
P2	0.725			
P5	0.780	0.598	0.773	0.816
SF1	0.896			
SF2	0.698			
SF3	0.744	0.614	0.784	0.825
CI1	0.786			
CI3	0.677			
CI6	0.769	0.556	0.746	0.789

Source: Primary Data Processed, 2024

Following this refinement, the second phase, the remaining indicators (as presented in Table 2) demonstrated acceptable levels of outer loadings, with almost all retained items exceeding 0.7, which falls within the recommended threshold by Hair et al. (2022). While SF2 and CI3 exhibited outer loadings slightly below 0.7, namely 0.698 (SF) and 0.677 (CI3), their retention is justified as the AVE values exceed 0.5, indicating a satisfactory level of convergent validity, as suggested by Hair et al. (2022). Additionally, the Fornell-Larcker Criterion assessment confirms the discriminant validity of the measurement model, as the square root of the AVE for each construct exceeds its correlations with other constructs, namely 0.773 (P), 0.784 (SF), and 0.746 (CI), suggesting that all constructs exhibit sufficient distinction from one another, as recommended by Hair et al. (2022). Furthermore, the composite reliability (CR) values for all constructs were well above the 0.7 benchmark, measurement model's reliability. These findings affirm that the measurement model is both reliable and valid, providing a solid foundation for further structural model analysis.

RESULTS

The evaluation of the structural model was conducted using PLS-SEM, adhering to the recommendations outlined by Hair et al. (2022). This evaluation involved assessing path coefficients, p-values, t-statistics, and R^2 values to determine the strength and significance of the proposed relationships, where the results are presented in Table 3.

Table 3. Structural Model Evaluation

Paths	Estimate	t-stat	p-values	Results	R-Square
SF → P	0.344	2.996	0.003	H1 supported	
SF * CI → P	-0.024	0.226	0.821	H2 not supported	0.188

Source: Primary Data Processed, 2024

As depicted in Table 3, the findings highlight that strategic flexibility (SF) exerts a significant positive influence on business performance (P), with a path coefficient of 0.344 (t = 2.996, p = 0.003). This finding supports H1, confirming that higher strategic flexibility enables MSMEs to enhance their performance by effectively adapting to dynamic market conditions. However, the moderation effect of competitive intensity (CI) on the SF-P connection, did not confirm, as reflected by a path coefficient of -0.024 (t = 0.226, p = 0.821). Consequently, H2 is not supported, suggesting that moderation effect of competitive intensity on the link between strategic flexibility and business performance was not found to be statistically meaningful. Additionally, the R^2 value of 0.188 for business performance indicates that approximately 18.8% of its variance is explained by the model, highlighting the role of strategic flexibility in driving business success.

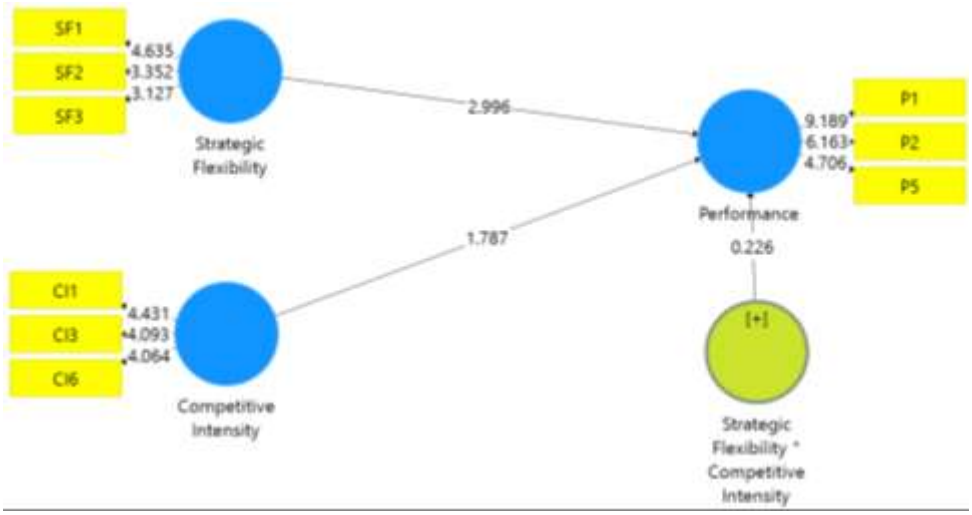

Figure 1. The Path Analysis
Source: Primary Data Processed, 2024

DISCUSSION

The study underscores that strategic flexibility plays a crucial role in enhancing MSMEs' performance. This finding aligns with previous studies (Bashir, 2023; Brozović et al., 2023; Darmawan et al., 2023; Otache, 2024), which consistently highlight the critical role of strategic flexibility in driving organizational success. According to Otache (2024), strategic flexibility is positively associated with MSMEs' performance, reinforcing the notion that businesses capable of dynamically adjusting their strategies tend to achieve superior outcomes. This finding is particularly relevant given that strategic flexibility is considered a dynamic organizational capability that enables firms to maximize the potential of their available resources (Bashir, 2023). In essence, the more extensively a business adopts strategic flexibility, the greater its potential to enhance performance (Bashir, 2023; Guo & Cao, 2014).

Furthermore, the study finds that competitive intensity does not moderate the strategic flexibility-MSMEs' performance connection. This finding is in line with the result provided by Otache (2024), who also reported that the impact of strategic flexibility on MSMEs' performance is not contingent on market competition levels. Unlike previous studies suggesting that competitive intensity acts as a moderator between business performance and its antecedents (Kankam-Kwarteng et al., 2019). The finding of this study indicates that, within the examined context, competitive intensity does not influence the effect of strategic flexibility towards business performance. In this context, Otache (2024) argues that as business environments become increasingly dynamic, MSMEs are expected to enhance their operational flexibility in response to general environmental shifts, regardless of the intensity of market competition. This perspective suggests that rather than relying on external competitive pressures, MSMEs should proactively cultivate their internal agility to navigate evolving market conditions effectively.

Accordingly, this study contributes by validating that, the impact of strategic flexibility on MSMEs' performance is direct and independent of competitive intensity as a conditional factor. This suggests that, regardless of the level of competitive intensity faced by MSMEs, it does not significantly enhance or diminish the effect of strategic flexibility practices on their business performance. Therefore, MSMEs' efforts to implement strategic flexibility as a means of improving performance, need not consider the prevailing level of competitive intensity in their environment.

CONCLUSIONS

Grounded in the dynamic capabilities theory, this study examines how strategic flexibility influences the performance of MSMEs, while also examining the moderating role of competitive intensity. Utilizing the PLS-SEM approach for data analysis, the findings confirm that strategic flexibility plays a crucial role in enhancing MSMEs' performance, reinforcing its significance as a key driver of business success.

Furthermore, the study reveals that competitive intensity does not moderate the link between strategic flexibility and the performance of MSMEs. These findings imply that strategic flexibility directly enhances MSMEs' performance, regardless of the level of market competition. In other words, MSMEs' ability to enhance performance through strategic flexibility is not contingent on the degree of competition they face.

Theoretical Implications

The results of this study contribute valuable theoretical insights by extending the application of dynamic capabilities theory. In this context, strategic flexibility, which originates from dynamic capabilities theory, serves as a crucial organizational capability that empowers MSMEs to improve their performance by effectively reconfigure their resources and operational strategies in changing market conditions. Interestingly, the results also reveal that competitive intensity does not serve as a moderating factor in the link between strategic flexibility and MSMEs' performance, challenging prior assumptions that external competition significantly influences the effectiveness of internal capabilities. The findings confirm that strategic flexibility directly contributes to business success, underscoring its role in enabling firms to reconfigure resources and adjust strategies in the dynamic environments. This insight suggests that the performance benefits of strategic flexibility are inherently independent of competitive intensity levels.

Managerial Implications

The results of this research suggest that strategic flexibility directly and significantly enhances the performance of MSMEs, regardless of the level of competitive intensity in the market. This underscores the importance of strategic flexibility as a critical capability that MSME owners and managers should actively cultivate to enhance business performance. To effectively implement strategic flexibility, MSME owners and managers should adopt a dynamic approach to business operations, which includes adapting business strategies, reconfiguring resource utilization, and deploying resources efficiently to achieve organizational goals (Bashir, 2023). By embracing these flexible practices, MSMEs can optimize their internal capabilities to improve their performance, even in the volatile competitive environments.

Limitations and recommendations

Although this study offers important insights into how strategic flexibility contributes to enhancing MSMEs' performance, several limitations must be acknowledged. First, the use of a cross-sectional research design in this study limits the ability to infer causal relationships between observed variables. Future studies could benefit from a longitudinal approach to capture the dynamic nature of these relationships over time. Additionally, the use of convenience sampling exclusively in Yogyakarta and Sleman may limits the generalizability of the findings, suggesting the need for future research to

consider more diverse sampling techniques to enhance external validity and expanding the sample scope and incorporating diverse industry contexts could further strengthen the generalizability of the findings and provide a more comprehensive understanding. Moreover, the non-significant moderation effect of competitive intensity in this study suggests that external market competition does not necessarily weaken or amplify the impact of strategic flexibility on performance. Although these findings provide insight of the direct influence of strategic flexibility towards MSMEs' performance, the relatively small R-square value in this study indicates the need for further investigation of additional relevant variables within this research model to enhance its explanatory power and better capture MSMEs' performance. Such variables could include organizational competencies, customer orientation, and environmental dynamism.

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