

THE IMPACT OF ENTREPRENEURIAL ORIENTATION AND TRANSFORMATIONAL LEADERSHIP ON MSMEs PERFORMANCE

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Abstract: *This study was conducted on MSMEs in Kelantan assessing the impact of entrepreneurial orientation and transformational leadership on MSMEs business performance. Entrepreneurial orientation, characterized by innovation, proactivity, and risk-taking, is essential for MSMEs' adaptability and growth in dynamic markets. Similarly, transformational leadership, which inspires and motivates employees through vision, support, and intellectual stimulation, plays a critical role in enhancing organizational performance. Quantitative research design was employed, and data were collected from 146 MSMEs, and analyzed using the PLS-SEM technique. The finding indicates that entrepreneurial orientation has a significant influence on MSMEs' business performance. However, transformational leadership does not have any significant influence on business performance. The study concludes that fostering entrepreneurial orientation within MSMEs can significantly enhance their performance, offering valuable insights for business owners, policymakers, and stakeholders aiming to promote the success of micro, small and medium enterprises.*

Keywords: *Entrepreneurial orientation, transformational leadership, business performance*

Introduction

Micro, Small, and Medium Enterprises (MSMEs) are pivotal to Malaysia's economic landscape, contributing significantly to employment, innovation, and GDP. In 2023, MSMEs accounted for 96.9% of all business establishments, totaling 1,101,725 firms. This marks an increase from 907,065 MSMEs in 2015, reflecting an average annual growth rate of 2.5% (SMEs, 2015-2023). In 2023, MSMEs contributed RM613.1 billion to the nation's GDP, achieving a growth rate of 5%, which surpassed the overall economic growth of 3.6%. Consequently, the MSME sector's share of the total economy rose from 38.6% in 2022 to 39.1% in 2023. Given their substantial role, enhancing the business performance of MSMEs is crucial for Malaysia's economic development.

Entrepreneurial orientation is an attempt to create value through business opportunities, appropriate risk-taking management, and management communication skills to mobilize human, financial and other raw materials or other available resources to obtain benefits and value from business opportunities (Lin, 2012). In Malaysia, entrepreneurial orientation is a practical framework for attaining resilience and sustainable growth, not just a theoretical concept. Entrepreneurial orientation enables the success of MSMEs in Malaysia's competitive and diverse economy by efficient risk management, technological utilisation, and value generation in niche markets. Entrepreneurial orientation is a powerful driver of innovation, strategic adaptability, and resilience in various sectors across Malaysia. By adopting entrepreneurial orientation, businesses in agriculture, manufacturing, e-commerce, tourism, renewable energy, and food services have successfully navigated challenges, capitalized on new opportunities, and enhanced their competitive advantage. Entrepreneurial orientation is an attempt to create value through business opportunities, appropriate risk-taking management, and management communication skills to mobilize human, financial and other raw materials or other available resources to obtain benefits and value from business opportunities. (Lin, 2012).

Moreover, leadership also considered as a key factor in directing all organizational components towards the effective achievement of organizational goals and needs to provide interaction between all members of the organization (Suwanto, Sunarsi & Achmad, 2022). businesses in agriculture, manufacturing, e-commerce, tourism, renewable energy, and food services have successfully navigated challenges, capitalized on new opportunities, and enhanced their competitive advantage. The ability of an organisation to endure rests on its leaders' ability to remain effective and their willingness to accomplish the organization's objectives, which are accomplished with the aid of effective leadership. Therefore, without strong leadership, without motivating followers, without encouraging high employee motivation, and without cultivating employee engagement, organisations collapse. Employees under transformational leadership are more likely to be inspired and continue to put the needs of the company ahead of their own (Qomariah, Wiguna, Martini & Thamrin, 2023). Therefore, the objectives of this study to examine the effect entrepreneurial orientation and transformational leadership on MSMEs performance.

Literature Review

Business Performance

Business performance has been defined as a continuous and flexible process involving managers, partners and people who run the business which reflects the result of business activities and strategic management process (Yusrinadini et al., 2019). A recent literature had revealed that due to the relevance of SMEs in the world economy, they need specific treatment around knowledge of performance management to address their development and generate improvements (Ximena et al., 2020). Embracing elements like strategic leadership, market adaptability, and innovative capabilities is essential for enhancing success. Research emphasizes clear performance metrics, continuous monitoring, and leadership-driven strategies are better equipped to navigate competitive landscapes and achieve long-term success (Nguyen & Tan, 2023; Santos & Pereira, 2024). Thus, the factor for MSMEs business performance is significant to be addressed so that performance management can be always on the right track.

Entrepreneurial orientation and Business Performance

Entrepreneurial orientation (EO) has emerged as one of the most studied constructs in entrepreneurship and management literature for more than three decades (Covin et al., 2019; Gupta, 2015). Findings from past studies show that entrepreneurial orientation influences SMEs' performances (Amin, 2015; Amin et al., 2016). Moreover, EO can help to achieve growth in the market (Adomako et al., 2021) and the performance of an organization (Hossain & Asheq, 2020). Study done by Titi et al (2020) there was a positive relationship between entrepreneurial SMEs performance. Adriani and Thaib (2024) examine how EO influences various indicators of company performance, including satisfaction and global competitiveness. The research suggests that a strong EO enables firms to be more responsive to market dynamics, leading to improved performance outcomes. Amaleshwari and Jeevitha (2024), indicate that dimensions of EO, such as innovativeness and risk-taking, positively affect sustainable business performance, highlighting the importance of EO in achieving long-term business success. Hanna (2024) suggests that certain dimensions of EO, including innovativeness and competitive aggressiveness, positively influence innovative co-branding partnerships, which in turn enhance business performance. Based on the discussion, the study have explored the relationship between EO and business performance, showing that a higher EO positively impacts business performance. Therefore, this hypothesis is proposed:

H1: Entrepreneurial orientation is positively related to business performance.

Transformational Leadership and Business Performance

Transformation leadership, leaders have relation-oriented behaviour and change-oriented behaviour (Yukl & Gardner, 2019). Based on Siangchokyoo et al., (2020), benefits of transformational leadership which can transform followers' attitudes and behaviour toward achieving higher organizational performance levels. Moreover, Naderi et al (2019), transformational leadership has a positive connection with the performance of social enterprise. Transformational leaders articulate a compelling vision that encourages employees to work toward shared goals, leading to higher organizational performance (Dawson & Martin, 2023). By encouraging creative thinking and problem-solving, transformational leaders in MSMEs foster a culture of innovation that can enhance product development, customer service, and operational

efficiency (Patel & Reddy, 2024). Bukhari & Ahmad, (2023), stated that, MSMEs led by transformational leaders tend to have a positive organizational culture where employees trust and support each other. Transformational leaders' envisioned impact cultivates trust, hence improving collaboration, communication, and overall performance. Conversely, Sattayaraksa and Boon (2018), raised a debate whether transformational leadership is associated with either subunit performance or only overall performance in organization. The high expectations set by transformational leaders may lead to employee burnout, especially in MSMEs with limited resources. When employees are constantly pushed to innovate or meet high standards without adequate support, it may result in stress, turnover, and ultimately reduced performance (Singh & Kumar, 2025). With the contrasting perspectives above discussion, thus this hypothesis is proposed:

H2: Transformational leadership is positively related to business performance.

Research Framework

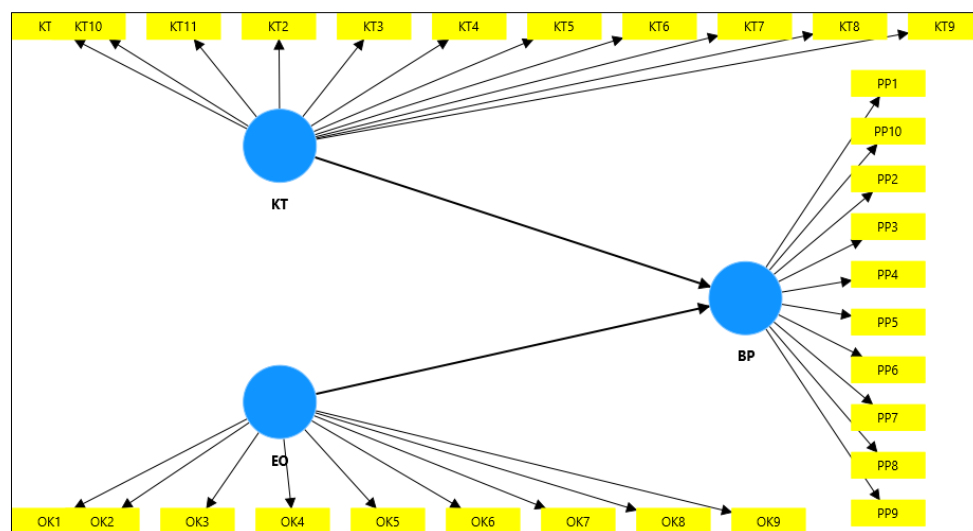


Figure 1: research Framework

Methods

The questionnaires were given to MSMEs in Malaysia's Kelantan districts. Owners and managers were singled out since they are the primary sources of information about the company and typically participate in the day-to-day operations of the businesses. A total of 146 questionnaires were returned and useable for the final analysis using the structural equation model partial least square (SEM-PLS 4.0). The questionnaires were adopted and adapted from a few selected established questionnaires and measured with 5-point Likert-scale ranging from strongly disagree to strongly agree. Transformational leadership is measured from study by Bass and Avolio (2004) whereas the measurement items of entrepreneurial orientation were based on Miller and Frisen (1982) and business performance based on Wiklund (1999).

Result and Discussion

Measurement Model

Based on Hair, Ringle, and Sarstedt (2011) highlight the importance of assessing the quality of the measurement model through convergent validity, which considers factor loadings, average variance extracted (AVE), and composite reliability (CR).

Convergent Validity

Based on Hair, Ringle, and Sarstedt (2011) highlight the importance of assessing the quality of the measurement model through convergent validity, which considers factor loadings, average variance extracted (AVE), and composite reliability (CR) (refer Table 1). With regards to this study, all indicator loadings exceeded the threshold of 0.5 indicating that each item reliably measures its intended construct. Additionally, AVE values ranged from 0.633 to 0.740, exceeding the recommended threshold of 0.5, suggesting that the constructs capture more variance than measurement error. Furthermore, CR values ranged from 0.944 to 0.962, surpassing the threshold of 0.7, indicating high internal consistency. These results collectively demonstrate strong convergent validity, indicating that this measurement model effectively measures the intended constructs.

Table 1: Convergent Validity

Constructs	Cronbach's Alpha	Composite Reliability	AVE
Entrepreneurial Orientation	0.938	0.944	0.675
Transformational Leadership	0.941	0.950	0.633
Business performance	0.961	0.962	0.740

Discriminant Validity

According to Henseler, Ringle, and Sarstedt (2015), the measurement model's discriminant validity was assessed using the heterotrait-monotrait (HTMT) ratio of correlations. This method compares the correlations between different constructs (heterotrait) to the correlations within the same construct (monotrait). A threshold value of less than 0.85 has been suggested in the literature (Clark and Watson, 1995; Kline, 2011) to determine discriminant validity. When HTMT is higher than this threshold of 0.85 (Kline, 2011) or 0.90 (Gold et al., 2001), there is evidence of a lack of discriminant validity. Based on the results obtained in Table 2, the HTMT correlation scores obtained are less than 0.85 as per the threshold recommended by Kline (2011), there is no discriminant validity issue for the research. In this study, the HTMT ratios presented in Table 2 are all below the recommended thresholds, indicating strong discriminant validity. This suggests that the constructs in this measurement model are distinct from each other and are measuring different underlying concepts.

Table 2: Heterotrait-monotrait Ratio (HTMT)

	OE	TL	BP
Entrepreneurial Orientation (OE)			
Transformational Leadership (TL)	0.541		
Business Performance (BP)	0.795	0.431	

Hypotheses Testing and Discussion

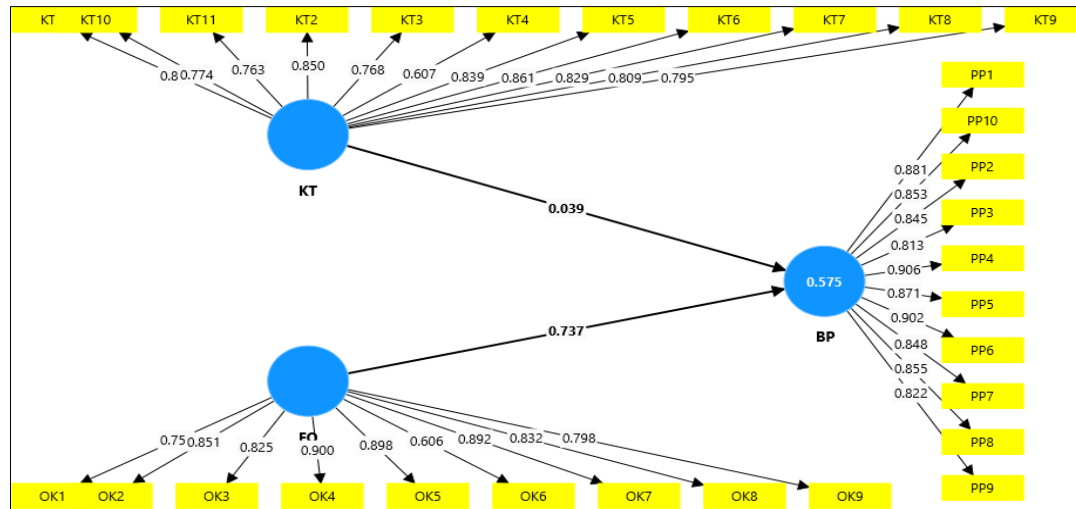


Figure 2: Structural Model

Based on Hair et al. (2011), path analysis was conducted to assess the structural model, with R^2 values and the significance of path coefficients serving as primary evaluation criteria. According to Cohen (1988) suggests that a good model should have an R^2 value of over 0.26 for endogenous latent variables. In this study, the R^2 value was found to be 0.575 indicating the variance in the dependent variable explained by the independent variables. Another 42.5% could be explained by other variables such as innovation, digital adoption, learning orientation etc.

Table 3: Result of Direct Effect

Direct Relationship	Beta	Standard deviation	T statistics	P values	Results Hypotheses
EO-> BP (H1)	0.737	0.055	13.319	0.000	Supported
TL->BP (H2)	0.405	0.065	0.597	0.551	Not Supported

*Entrepreneurial Orientation (OE), Transformational Leadership (TL), Business Performance (BP)

The significance of hypotheses was assessed using path coefficients and the bootstrapping technique. The results revealed that the relationship between entrepreneurial orientation and business performance has significant ($\beta=0.737$, $t=13.319$, $p < 0.00$), while the relationship between transformational leadership and business performance has not significant ($\beta=0.405$, $t=0.597$, $p > 0.551$). Therefore, H1 was supported and H2 was not supported.

Conclusion, Limitation and Future Research

This study significantly expands the insight of how significant entrepreneurial orientation and transformational leadership influence business performance. Entrepreneurial orientation fosters a dynamic and adaptive approach to market opportunities and challenges, enabling businesses to stay competitive and thrive. As stressed by Brown and Smith (2024), businesses that prioritize entrepreneurial orientation are more likely to experience sustainable growth and superior

performance. Transformational leaders effectively inspire and motivate their teams, fostering an environment conducive to innovation and high performance. Transformational leadership raises employee engagement and productivity by encouraging a collaborative atmosphere and coordinating personal aspirations with corporate aims. As claimed by Smith and John (2024), in order to produce better operational results, this alignment helps the company become more flexible in a market that is changing quickly.

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