# The role of traditional knowledge-based dynamic capabilities to improve the sustainable performance of weaving craft in Indonesia

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## Abstract

**Purpose** – Indonesian woven craft small- and medium-sized enterprises (SMEs) have encountered several difficulties in sustaining their success in the digital era. The performance of the business is contingent upon its ability to gain competitive advantage through traditional knowledge capabilities. The purpose of this research is to study the role of traditional knowledge management processes towards competitive advantage and sustainable performance for woven craft SMEs.

**Design/methodology/approach** – This research used a quantitative approach with a survey strategy. Confirmatory research was conducted to test five hypotheses to determine the causal relationship of four variables, namely, traditional knowledge management, dynamic capabilities, competitive advantage and sustainable performance. This study used a purposive sampling strategy and gathered data from 385 respondents. The sample was selected based on predetermined criteria, including operation for more than five years and entrepreneurial activity using traditional knowledge as a resource to manage product innovation. The analytical technique used was structural equation modelling with the support of the AMOS programme.

**Findings** – The findings indicated that traditional knowledge management processes directly affect dynamic capabilities and sustainable performance. This study also found traditional knowledge management processes play a significant role in enhancing competitive advantage mediated by dynamic capabilities. However, traditional knowledge management processes have no significant effect on competitive advantage. Hence, there is a significant effect contributed by the relationship between traditional knowledge management processes and sustainable performance. Therefore, in the context of craft woven SMEs, the higher the traditional knowledge-based capabilities, the higher their sustainable performance.

**Originality/value** – The novelty shows a direct relationship between traditional knowledge management processes and sustainable performance. This study also found traditional knowledge management processes meditated by dynamic capabilities have a relationship with competitive advantage. Traditional knowledge management processes will trigger an increase in dynamic capability which is a source of business development; those conditions will increase sustainable performance. Traditional knowledge-based capability is an antecedent of sustainable performance. The benefits of this research can be used as scientific literature regarding the link between traditional knowledge management processes, competitive advantage and

sustainable performance. The results of this study can also be used as a basis for empowering traditional woven craft SMEs in Indonesia.

**Keywords** Traditional knowledge management, Dynamic capabilities, Competitive advantage, Sustainable performance, Traditional woven SMEs

**Paper type** Research paper

## 1. Introduction

The creative economy sector is one of the industrial fields with the greatest potential for rapid growth in the Industry 4.0 era. The creative industry promotes the actors' originality, critical thinking abilities and local culture. The creative sector in Indonesia plays a vital role in conserving the varied traditions of the Indonesian people, using local materials, developing tolerance and increasing growth in local community creativity. The potency of local resources can be transformed in terms of shape and function to support economic value (Simatupang *et al.*, 2012; Permatasari *et al.*, 2021b). The technological advancements that accompany the Industry 4.0 era also offer prospects for creating a culture-based creative industry. According to the BEKRAF report in 2019, the creative economy sector contributed IDR 1.105tn to the gross domestic product (GDP). The crafts subsector is one of the top three subsectors within the creative economy sector, contributing the most to Indonesia's GDP, exports and labour absorption. According to the report, the craft industry generated 14.9% of total national GDP, almost IDR 166tn. In spite of the COVID-19 pandemic, the income sector was in decline by around 3%–5% (CNN Indonesia, 2021). However, the craft subsector was able to adapt and survive with digitalisation. Data showed that in 2016, as many as 57.48% of craft businesses used social media and e-commerce (BEKRAF, 2019). The number keeps increasing nowadays.

Digitalisation has caused business disruption in the creative industry. The competition is becoming more intense. Small- and medium-sized enterprises (SMEs) in the creative industry must innovate and adapt to market and consumer demands and the business environment's constant changes. Ramadani and Gerguri (2011) define innovation in production as the process of developing or improving a specific product; innovation in services as the provision of new or improved services; innovation in the process as the discovery of new ways of organising and combining inputs in the process of producing specific products or services; and innovation in management as the creation of new organisational structures for business resources. As a result, SMEs that are adaptable and innovative will be able to compete and grow.

According to Kaur (2019), as the business world becomes competitive, organisations face many opportunities and problems, both internal and external. An enterprise must understand what and how to manage the numerous resources they possess to compete and survive. The ability of SMEs to manage their resources effectively to build competitive advantage is critical to their long-term viability. Local resources need to be sustained and renewed to create economic value (Permatasari *et al.*, 2021a). According to Kaur and Mehta (2017a, 2017b), a business can achieve a competitive advantage by providing clients with more benefits than competitors. Numerous company actions, including product creation, manufacture, promotion, delivery and maintenance, might result in a competitive advantage. These actions will improve the firm's relative cost position and lay the groundwork for differentiation.

The bulk of creative enterprises in the knowledge economy, particularly those operating in the digital era, embrace and transform their operations through technology. Digital transformation is the process of managing a business's knowledge and resources to improve

its operations (Kaur, 2019; Hapon, 2020). Creative enterprises seek to acquire and apply knowledge to enhance their operations. For example, in the Information Technology (IT) subsector, an organisation consciously and thoroughly obtains, organises, shares and evaluates its knowledge regarding resources, records and human capabilities (Kaur and Mehta, 2017a, 2017b; Kaur, 2019). As a result, knowledge management has increased in developing strategic value. However, managing knowledge as a strategic value is not easy. The situation of the IT sector is contradictory with the craft subsector. Craft SMEs in Indonesia are suffering the consequences of translating knowledge as their main resource into competitive advantage. Craft SMEs manage their traditional knowledge to generate products. Traditional knowledge in Indonesia is becoming an opportunity for local SMEs to develop values for their product innovations. According to Mayasari and Chandra (2020), information is gained from social capital, such as social environment and community. The social environment and society (social capital) will give information essential for the creative industry's existence in developing innovative products that may symbolise the social context in which the creative sector occurs. Therefore, traditional knowledge management is critical for improving creative SMEs, particularly traditional woven craft, to achieve competitive advantage.

Indonesia has a wide range of traditional knowledge with increasing options for business persons to commercialise traditional knowledge as a strategic value. However, many regions in Indonesia are still struggling to develop competitive advantage in terms of their domestic products and services and sustainability (Geotimes, 2017; Permatasari et al., 2021b). In renewable resource-based industries, communities primarily run those enterprises to create jobs by exploiting intellectual property rights (Mayasari and Chandra, 2020). This research fills a gap left by Mayasari and Chandra's (2020) research on the function of social capital in knowledge management systems (KMS) in the creative industry. Knowledge gained from the social environment or community is believed to be capable of fostering competitiveness and adapting swiftly to changes. However, to adapt to the evolving digital market, SMEs must provide clients with strategic options that lead to better products and competitive advantages (Vial, 2019). Additionally, as technological advancements continue, one SME's handmade items will become increasingly difficult to differentiate from that of another. Thus, to win a competition or market a current product, producers must consider the product's quality and the company's strategy. As a result, businesses engaged in creative weaving must continue to be supported to maintain a strong competitive edge and adapt to environmental changes.

This study aims to determine the sustainability performance of traditional woven businesses in Indonesia, by analysing the role of traditional knowledge management processes, dynamic capabilities and competitive advantage. The preservation of the Indonesian traditional weaving industry is very important, because traditional weaving is a characteristic of regional products throughout Indonesia. Therefore, to maintain the sustainability of woven craft SMEs, it is necessary to manage the SMEs' capability to use indigenous knowledge and resources. However, producers of traditional handicrafts face numerous obstacles that jeopardise their survival and expansion (Shafi et al., 2020):

> The study of indigenous entrepreneurship is useful. Indigenous people have developed a knowledge base that ensured survival in particular environments for countless generations. Still, the indigineous enterprises have not been sustainable (McGregor, 2004; Dana, 2007).

The dynamic changes in the traditional weaving sector include increased industrial rivalry, rising raw material prices and dwindling creative human resources. Therefore, this study applies the concept of knowledge-based dynamic capabilities by Kaur (2019) with a different

business sector, namely, the craft sector on traditional weaving. The sector consists of community enterprises that depend on local resources to sustain their business. The novelty of this research refers to indigenous knowledge management as resource-based capabilities to gain not only competitive advantage but also sustainable performance.

This study is organised as follows after the introduction and the explanation of the research background. Section 2 describes the literature review. We explore the definitions of variables and construct the relationships between variables. Five hypotheses will be tested in this study. In Section 3, we explain the methodology, the research design and strategy to answer the research questions and the data collection process because of the Covid-19 situation. The hypothesis testing was conducted using structural equation modelling (SEM). The next section consists of data analysis and an explanation of the findings and discussion related to the real context. Finally, in Section 5, we conclude and provide recommendations for future research.

## 2. Literature review

### 2.1 Sustainable performance

Sustainable performance is defined as the effort to "meet the needs of present generations without compromising the needs of future generations". In the future, the more successful a business, the more sustainable it will be. This study refers to the dimensions of business performance based on resources. Resources and capabilities are the main sources for companies to achieve profitability. According to Ramadani and Gerguri (2011), the aspects of business innovation consist of growth profit and sustainable development. Sustainability in company refers to an organisation's management process which consists of three aspects of performance, namely, economic, social and environmental. Meanwhile, the failure of business sustainability causes environmental issues, social injustice and inequality. Therefore, to gain sustainable performance, a company needs to have a strategy for synergising those three aspects.

The main objective of sustainable performance is not just profit, but also creating a positive effect on the environment and society. "Environmental commitment is a significant predictor of environmental sustainability practices in the company" (Sendawula *et al.*, 2020). The environment issue causes business operation processes that will impact on economic performance. In terms of the social aspect, sustainable performance can be achieved by managing the social capital of the company to benefit the stakeholders including the community. Therefore, sustainable performance is the company's success in operating the existing resources in the company to improve three aspects of performance, namely, the profit, social and environmental aspects.

### 2.2 Traditional knowledge management

Knowledge management in the organisation is the expertise to create, retrieve and transfer knowledge – the goal is to modify organisational behaviour towards new knowledge and experiences. Kaur (2019) found a positive relationship between the knowledge management process and company dynamic capability measured by adaptive, absorptive and innovative capabilities (Kaur, 2019). The knowledge management process in this study refers to the development of traditional and new knowledge, which comes from an in-depth information processing process that can increase company dynamic capability. Traditional knowledge or indigenous knowledge is the scope of intellectual work that comes from the ideas or inventions of a group of people of a country. Berkes (1999) in Dana (2007):

> [. . .] defined traditional ecological knowledge as knowledge, practice and belief, evolving by adaptive processes and handed down through generations by cultural transmission, about the relationship of living things (including humans) with one another and with their environment.

Traditional knowledge from indigineous people is a crucial component in a company's management system. Mayasari and Chandra (2020) stated that a "Knowledge Management System (KMS) in creative industry is an organizational process and tool for acquiring, converting, applying, and protecting existing knowledge from both internal and external organizations". However, protecting traditional knowledge is an urgent issue considering that most of the economic benefits of international trade are only for external parties such as companies or other countries (Siddiq, 2018). Therefore, *H1* in this study is as follows:

*H1.* Traditional knowledge management processes have a significant effect on dynamic capabilities.

Indigenous knowledge or traditional knowledge refers to knowledge systems, creation, innovation and cultural expression that have generally been passed from generation to generation. It is considered to be related to a particular society or region, developed non-systematically and continuously in response to a changing environment (Dana, 2007; Siddiq, 2018). Meanwhile, in business, knowledge management helps organisations to have better learning efficiency to increase competitive advantages. Applying knowledge management creates many benefits, such as identifying skill gaps, developing better informed decisions, improving collaboration, optimising employee onboarding and training and retaining business knowledge (Chien and Tsai (2012; Gao *et al.*, 2017). Competitive advantage is the ability of a business to achieve profits in a competitive industry through value creation strategies (Porter, 1998). Businesses can use knowledge management to equip them with tools and methods to handle enormous amounts of information and turn it into competitive advantages (Kaur, 2019). This study refers to competitive advantage referring to Barney (1991) who adopts the dimensions of resources that are valuable, rare, difficult to imitate and difficult to replace. Competitive advantage is a unique position developed by an organisation that is directly compared to its competitors through resources management. Therefore, traditional knowledge management in this study refers to the process where a business explores new knowledge or existing (traditional) knowledge to develop competitive advantage for their product. Therefore, *H2* of this study is as follows:

*H2.* Traditional knowledge management processes have a significant effect on competitive advantage.

A company is basically an organisation formed to achieve certain goals, among others, to earn profits and ensure business sustainability. Business performance can be viewed from various points of view, including the point of view of the company's infrastructure, business operations and company's resources. Referring to the concept of management, it is reasonable to state that the company's performance is reflected by a well-performed management function, including in terms of the knowledge management process. Knowledge management is "systematically capturing, describing, organizing, and sharing knowledge – making it useful, usable, adaptable, and re-useable" (Liebowitz and Yan, 2004). Knowledge management processes help businesses to have faster outcomes as they improve organisational learning and collaboration. "The spillover of knowledge for innovation will have an impact on business performance" (Ramadani *et al.*, 2017). At the same time, Cárcel-Carrasco and Gómez-Gómez (2021) also states that knowledge generation and combinational ability directly affect innovative performance. In traditional craft SMEs,

the business is managed by indigenous people who use traditional knowledge as a resource to develop their product. "Indigenous people often rely on immediately available resources, and work in indigenous communities is often irregular" (Dana, 2007). Indigenous knowledge or traditional knowledge plays a key role in ensuring sustainability development (Gorjestani, 2001). According to Dana (2007), indigineous people:

> [. . .] desired and achieved benefits of venturing can range from the narrow view of economic profit for a single individual to the broad view of multiple, social and economic advantages for entire communities.

Traditional knowledge applied by indigenous entrepreneurs and the grassroots innovations that arise represent an underused unique source of growth with enormous potential for delivering sustainable development (Onwuegbuzie, 2010). Therefore, this study embraces traditional knowledge management to gain sustainable performance in *H3*:

*H3.* Traditional knowledge management processes have a significant effect on sustainable performance.

### 2.3 Dynamic capabilities

In terms of dynamic changes, a company needs to respond quickly and efficiently to environmental change. This concept leads to the idea of dynamic capabilities. Dynamic capability refers to the firm's ability to integrate, build and reconfigure internal and external competencies to address rapidly changing environments. This theory also involves strategy development for businesses for extreme changes while keeping the capability standards at a minimum to secure competitive survival (Teece *et al.*, 1997; Aldianto *et al.*, 2021). Chien and Tsai (2012) indicate that "dynamic capabilities increase store performance, and that both knowledge resources and learning mechanisms have a positive effect on dynamic capabilities". According to Teece *et al.* (2017), dynamic capability consists of three components: sensing (which entails recognising and assessing opportunities outside your organisation), seizing (which entails mobilising your resources to capitalise on those chances) and changing (continuous renewal).

Regardless of the industry or type of change, investing in dynamic capabilities creates long-term benefits for a business. SMEs can use dynamic capabilities to adapt and achieve strategic goals by reorganising internal and external resources to take advantage of developing technology, adjust to changing customer behaviours and, ultimately, surpass competitors. Kaur and Mehta (2017a, 2017b) stated that dynamic capabilities have an impact on a company's competitiveness. Kaur (2019) analyses how dynamic capabilities consist of adaptative, absorptive and innovative skills; those three elements have become the must-have skills for business nowadays. Pundziene *et al.* (2021) demonstrate that open innovation plays a role in mediating the relationship between dynamic capability and competitive business performance. Jiao *et al.* (2011) found that "innovation strategy is positive and significant for dynamic capabilities". In contrast, dynamic capabilities call for alteration of a resource base through integration, development, and reconfiguration of competencies. Integration correlates positively with dynamic capability (Hung *et al.*, 2010; Gonzales, 2021). However, it also finds that the interaction term between innovation strategy and environmental dynamism is insignificant in predicting dynamic capabilities. SMEs can build and upgrade dynamic capabilities towards competitive advantage in rapidly changing environments. Therefore, *H4* of this study is as follows:

*H4.* Dynamic capabilities have a significant effect on competitive advantage.

*2.4 Competitive advantage*
Competitive advantage is the company's ability to add more value to its products than competitors, with added value being the value that trades benefits for customers (Kaur and Mehta, 2017a, 2017b; Kaur, 2019). Competitive advantage is achieved by implementing strategies that use the company's diverse resources effectively. This strategy must evolve to maintain a competitive advantage over time, enabling the organisation to dominate existing and future markets. Referring to Michael Porter (1990), differentiation and low cost are strategies that cannot mutually exist at the same point in time. A similar argument was also stated by Treacy and Wiersema (1997). In addition, competitive advantage is described as a strategy that uses resources and the collaboration of companies to achieve a more effective competitive advantage in their market. Referring Bharadwaj *et al.* (1993), skills and resources are seen as a source of competitive advantage. Meanwhile, Wiig (1997) states that from a knowledge management perspective, to gain a competitive advantage, companies need to actively pursue values, namely, operations, product leadership and customer intimacy. These values will ensure business sustainability and profitability. This is also revealed by Zainol and Al Mamun (2018) and Danso *et al.* (2020); corporate strategy is a valuable asset towards implementing SMEs' innovative processes to improve sustainable competitive advantage and performance. Therefore, *H5* of this study is as follows:

*H5.* Competitive advantage has a significant effect on sustainable performance.

## 3. Research method

*3.1 Research design*
This study used a quantitative approach with a survey strategy. The aim is to measure causal relationships (cause and effect). Quantitative research uses natural science methods to generate numerical data and hard truths. It uses statistical approaches to establish a causal relationship between two variables (Saunders and Lewis, 2012). Quantitative research can create raw data graphs and tables, making the outcome easier to analyse (Ong and Puteh, 2017). We classify, rank or measure the data collected. This research is about understanding the role of traditional knowledge-based capabilities through competitive advantage to improve sustainable performance. Figure 1 shows a theoretical framework of this study.

*3.2 Sample and data collection*
The population of this study is traditional woven SMEs in Indonesian who develop their business activities through social media, where their population is unknown. Purposive
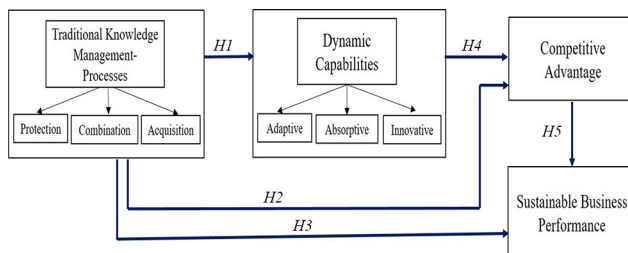


**Source:** Literature review

Figure 1.
Research framework

sampling was used for a nonprobability in this study. Nonprobability is arbitrary and subjective. We targeted a minimum of 300 respondents to have a good sampling design (Comrey and Lee, 1992). This study used a questionnaire as an instrument to collect data from respondents. The questionnaire consisting of three parts. The first part was an introduction. The second part included screening questions and the respondent's profile. The last part consisted of 12 questions to measure the variables. We use three indicators to measure sustainable performance based on Danso *et al.* (2020), while nine other indicators are used to identify knowledge management processes, dynamic capabilities and competitive advantage based on Kaur (2019). The exogenous variable in this study is traditional knowledge management processes. Meanwhile, the endogenous variables are dynamic capabilities, competitive advantage and sustainable performance.

Because of Covid-19, data collection was conducted by online survey using Facebook Advertising (FBAds). The questionnaire was distributed to traditional woven crafters who were registered on social media (Facebook) to market their business. A total of 385 respondents participated. After the respondent had filled out the questionnaire, they were compiled into an Excel form and ready to process for data analysis.

### 3.3 Data analysis
Data analysis was carried out using various instruments related to descriptive statistics and SEM to assess the model's suitability. Descriptive statistics analysis helps explain, demonstrate or summarise data points to develop patterns that meet all the data requirements. An important part of descriptive analysis is determining the tendency or response. A six-point scale was used to capture a clear assessment of the tendency by avoidance of a midpoint. SEM is a multivariate technique for testing and assessing multivariate causal relationships (Hair *et al.*, 2014). SEM is currently commonly used in research. As advanced analysis methods become common, so does the complexity of empirical models and theoretical breakthroughs in published research (Hair *et al.*, 2014). The validity and reliability test, goodness of fit test, hypothesis testing and $R$-squared analysis are discussed briefly in the next section.

## 4. Results and findings
### 4.1 Respondent profiles
The respondent profiles show, from 385 craft SMEs, 312 started their business with equity of less than IDR 35m, while 65 respondents started with equity of IDR 35m–100m. A total of 312 respondents have revenue per year <300m; 55 of them have revenue per year of IDR 300m and IDR 2.5bn. However, there are two respondents who have a revenue per year of more than IDR 2.5bn. The largest number of respondents are independent; they were not in partnerships with the government or business institutions. Overall, 61 have business partners, 39 of them cooperate with the local government and 23 of the respondents partner with central government. The others are in partnerships with multi-stakeholders (Table 1).

### 4.2 Validity and reliability test
The validity test determines/analyses the accuracy and precision with which a measuring device performs its measurement function – the standardised loading factors (SLF) to test the requirements. A valid indicator has a significance value of 0.5. In comparison, a reliability test is applied to ascertain the extent to which the measurement result is trusted. The AVE and CR tests are analysed to determine the reliability of the study variables. If the AVE value is greater than 0.5 and the CR value is greater than 0.7, the study variables are

| Demographic characteristics | Category | Frequency | (%) |
|---|---|---|---|
| Firm age | <5 years | 276 | 71.69 |
| | 5–10 years | 58 | 15.06 |
| | 10–15 years | 21 | 5.45 |
| | 15–20 years | 10 | 2.60 |
| | >20 years | 20 | 5.19 |
| Starting equity (IDR) | <35m | 312 | 81.04 |
| | 35–100m | 65 | 16.88 |
| | >100m | 8 | 2.08 |
| Revenue per year (IDR) | <300m | 328 | 85.19 |
| | 300m–2.5bn | 55 | 14.29 |
| | >2.5bn | 2 | 0.52 |
| Stakeholder involvement (business/government) | Business partner | 61 | 15.84 |
| | Local government | 39 | 10.13 |
| | Central government | 23 | 5.97 |
| | Local government and business partner | 17 | 4.42 |
| | Central government and local government | 4 | 1.04 |
| | Central government, local government, business partner | 6 | 1.56 |
| | Independent | 235 | 61.04 |

Table 1. Respondents' profiles

reliable. The findings of the validity and reliability tests on each variable are present in Table 2.

According to Table 2, the validity test results using SLF on the study variables indicate that each variable has a significant value greater than 0.5. The result demonstrates that the variables selected are the appropriate indicators for each research variable. According to Table 3, the reliability test results using AVE and CR on the research variables indicated that the AVE value was greater than 0.5, and the CR value was greater than 0.7. As a result, it is possible to conclude that the research variables' measurement results are reliable.

| No. | Construct/variable | Indicator | Measurement | Standardised loading factors (SLF) > 0.5 (Hair *et al.*, 2010) | Validity test |
|---|---|---|---|---|---|
| 1 | Traditional knowledge management | Protection | TKM1 | 0.865 | Valid |
| | | Combination | TKM2 | 0.826 | Valid |
| | | Acquisition | TKM3 | 0.885 | Valid |
| 2 | Dynamic capability | Adaptive | DC1 | 0.913 | Valid |
| | | Absorptive | DC2 | 0.915 | Valid |
| | | Innovative | DC3 | 0.923 | Valid |
| 3 | Competitive advantage | Product quality | CA1 | 0.840 | Valid |
| | | Number of customers | CA2 | 0.932 | Valid |
| | | Sales revenue | CA3 | 0.922 | Valid |
| 4 | Sustainable business performance | Economic | SBP1 | 0.670 | Valid |
| | | Social | SBP2 | 0.867 | Valid |
| | | Environmental | SBP3 | 0.847 | Valid |

Table 2. Validity test

| No. | Construct/variable | Indicator | Measurement | AVE > 0.5 (Hair *et al.*, 2010) | CR > 0.7 (Hair *et al.*, 2010) | Reliability test |
|---|---|---|---|---|---|---|
| 1 | Traditional knowledge management | Protection Combination Acquisition | TKM1 TKM2 TKM3 | 0.738 | 0.849 | Reliable |
| 2 | Dynamic capability | Adaptive Absorptive Innovative | DC1 DC2 DC3 | 0.841 | 0.941 | Reliable |
| 3 | Competitive advantage | Product quality Number of customers | CA1 CA2 | 0.749 | 0.857 | Reliable |
| 4 | Sustainable business performance | Sales revenue Economic Social Environmental | CA3 SBP1 SBP2 SBP3 | 0.639 | 0.840 | Reliable |

**Table 3.**
Reliability test

### 4.3 Descriptive statistics

The index value was determined using descriptive analysis. This index value is useful for gaining a general sense of respondents' attitudes towards the issues posed. The following table (Table 4) summarises the index values for the indicators, indicating that the traditional knowledge management approach falls into the medium group, with an index value of 4.65. The combination indicator (TKM.2) has the highest index value of the three indicators studied. Three indicators are used to quantify the dynamic capabilities variable. The index calculation results indicate that dynamic capabilities are classified as the medium, with an index value of 4.88. The DC.1 (adaptive) indicator has the highest index value among the four indicators studied. Three indicators are used to quantify the competitive advantage variable. The index value calculation results indicate that the competitive advantage is in the middle range, with a value of 4.65. The CA.3 indicator has the lowest index value of the three indicators studied. Three metrics are applied to quantify the variable of sustainable performance. The index value computation indicates that sustainable performance is moderate, with an index value of 4.56. The BSP.1 indicator has the lowest index value of the three indicators studied.

| Items | N | Minimum | Maximum | Mean | Avg. dimension score | SD |
|---|---|---|---|---|---|---|
| TKM1 | 385 | 1 | 6 | 4.90 | 4.98 | 1.194 |
| TKM2 | 385 | 2 | 6 | 5.18 | | 0.921 |
| TKM3 | 385 | 1 | 6 | 4.85 | | 1.185 |
| DC1 | 385 | 1 | 6 | 4.92 | 4.88 | 1.181 |
| DC2 | 385 | 1 | 6 | 4.81 | | 1.195 |
| DC3 | 385 | 1 | 6 | 4.89 | | 1.144 |
| CA1 | 385 | 1 | 6 | 4.82 | 4.65 | 1.172 |
| CA2 | 385 | 1 | 6 | 4.57 | | 1.279 |
| CA3 | 385 | 1 | 6 | 4.56 | | 1.253 |
| BSP1 | 385 | 1 | 6 | 4.24 | 4.56 | 1.474 |
| BSP2 | 385 | 1 | 6 | 4.70 | | 1.296 |
| BSP3 | 385 | 1 | 6 | 4.75 | | 1.267 |

**Table 4.**
Descriptive statistics

### 4.4 Structural equation modelling analysis

*4.4.1 Goodness of fit.* After analysing the uni-dimensionality level of the dimensions/
indicators forming latent variables to test with confirmatory factor analysis, the analysis
continued with the full model SEM. The results of data processing for the complete analysis
of the SEM model are described in Figure 2.

According to Table 5, the goodness of fit test criteria are generally good or meet the
required standards. The Chi-square test shows that the model is valid if the Chi-square value
is smaller than the table Chi-square value. The determined CMIN/DF in Table 5 shows
the Chi-square value determined in this study is less than the crucial value/table
(acceptable). Therefore, the result indicates that the model is accurate; in other words,
there is no difference in population estimates between the samples studied.

*4.4.2 Hypothesis testing.* Following an assessment of the assumptions in SEM analysis,
hypothesis testing was conducted. This study tested five hypotheses by calculating the
critical ratio (CR) and calculating the probability of a causal relationship (Table 6). The
procedure for testing hypotheses was as follows: *H1* illustrates parameter estimation to
examine the effect of traditional knowledge management processes on dynamic capabilities,
resulting in a CR value of 25.714 and a $p$-value of 0.00. The significance of $p = 0.05$ shows
that traditional knowledge management processes have a considerable beneficial effect on
dynamic capabilities. This means that the weaving industry's traditional expertise will
expand in search of dynamic capabilities. In traditional knowledge management, the
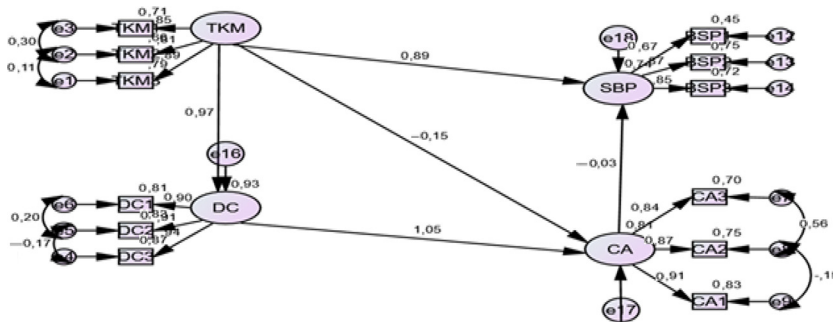combination indicator will have the most impact on dynamic capabilities.



Figure 2.
SEM model testing

| Goodness of fit measure | Cut-off value | Scoring | Result |
| --- | --- | --- | --- |
| Chi square – degrees of freedom ratio (CMIN/DF) | Ideally <3.0 but not >5.0 | 3.706 | Acceptable |
| Comparative fitness index (CFI) | >0.90 | 0.975 | Good |
| Normed fit index (NFI) | >0.90 | 0.966 | Good |
| Goodness of fit index (GFI) | >0.80 | 0.937 | Good |
| Adjusted goodness of fit (AGFI) | >0.80 | 0.887 | Good |
| Tucker–Lewis index (TLI) | >0.90 | 0.961 | Good |
| Incremental index of fit (IFI) | >0.90 | 0.975 | Good |
| Root mean square error approximation (RMSEA) | Ideally <0.05 but not >0.08 | 0.08 | Acceptable |

Table 5.
Goodness of fit
measure

*H2* illustrates parameter estimation to examine the effect of traditional knowledge management processes on competitive advantage, resulting in a CR value of $-0.53$ and a $p$-value of 0.598. Because $p > 0.05$, it is inferred that traditional knowledge management processes have no discernible positive influence on competitive advantage. This means that the traditional knowledge management processes used in the weaving business are not always enhanced to maintain a competitive edge.

*H3* illustrates the parameter estimation used to assess the traditional knowledge management processes' sustainability, with a CR value of 7.876 and a $p$-value of 0.00. The significance of $p = 0.05$ shows that traditional knowledge management processes have a considerable beneficial effect on long-term performance. This means that traditional weaving expertise expands to achieve sustainable performance. The combination show as an aggressive indicator of traditional knowledge management processes towards sustainable performance.

Parameter estimation for *H4* reveals a CR value of 3.631 with a $p$-value of 0.00 for the effect of dynamic capabilities on competitive advantage. Because of the significance of $p = 0.05$, this shows that dynamic capabilities contribute significantly to competitive advantage. This means that dynamic capability is enhanced to achieve sustainable performance. The most significant contribution to competitive advantage will come from adaptive indicators embedded in dynamic capabilities.

*H5* illustrates parameter estimation to examine the effect of competitive advantage on long-term performance, with a CR of $-0.314$ and a $p$-value of 0.754. As a result, with a $p$-value of 0.05, it may be argued that competitive advantage has no discernible effect on long-term performance. This means that the weaving industry's competitive edge is not enhanced by the pursuit of sustainable performance.

*4.4.3 R-square test.* The structural model was evaluated using $R^2$ testing, which is presented in Table 7, namely, for the dynamic capabilities, competitive advantage and marketing performance variables. The $R^2$ value for dynamic capability is 0.934, which means that traditional knowledge management process variables influence 93.4% of the variance of dynamic capability. Other factors explain 6.6% of the variance, then the $R^2$ for competitive advantage is 0.811, which means 81.1% of the competitive advantage effect is explained by the dynamic capability variable, and 18.9% of the dependent variable is

| | Hypothesis testing | | | Estimate | SE | CR | $p$ |
|---|---|---|---|---|---|---|---|
| *H1* | Traditional Knowledge Management | $\rightarrow$ | Dynamic capabilities | 0.980 | 0.038 | 25.714 | *** |
| *H2* | Traditional Knowledge Management | $\rightarrow$ | Competitive advantage | −0.149 | 0.282 | −0.53 | 0.596 |
| *H3* | Traditional Knowledge Management | $\rightarrow$ | Sustainable performance | 0.832 | 0.106 | 7.876 | *** |
| *H4* | Dynamic Capabilities | $\rightarrow$ | Competitive advantage | 1.024 | 0.282 | 3.631 | *** |
| *H5* | Competitive Advantage | $\rightarrow$ | Sustainable performance | −0.029 | 0.093 | −0.314 | 0.754 |

**Note:** *** $p < 0.001$

**Table 6.**
Hypothesis testing

| Variable | *R*-squared |
|---|---|
| Dynamic capability | 0.934 |
| Competitive advantage | 0.811 |
| Sustainable business performance | 0.741 |

**Table 7.**
R Squared test

explained by other factors not measured in this study. The $R^2$ for sustainable performance is 0.741, which means that the dynamic capability variable influences 74.1% of the variance of competitive advantage, and 25.9% of the dependent variable is explained by other factors not measured in this study. The $R^2$ is based on Table 7; the higher the $R$-square value, the greater the ability of the independent variable to explain the dependent variable, indicating a better structural equation.

### 4.4 Discussion

*4.4.1 Traditional knowledge management processes' contribution to dynamic capabilities and sustainable performance.* Sustainable performance has been challenging for SMEs in the creative industry. The current pandemic makes its implementation even more difficult with the abrupt changes in business operations, customer behaviour and digitalisation. In spite of the challenging condition of the pandemic, sustainable performance has become widely discussed currently. Applying knowledge management and dynamic capabilities has a significant role in the business shift to sustainable practices. In terms of the economic and environmental aspects, the integration of knowledge management has supported woven craft SMEs' revival strategies through knowledge integration and dissemination. According to Dana (2007), "Indigenous entrepreneurship is usually environmentally sustainable". Capel (2014) stated mindfulness fosters an awareness of alternative knowledge and behaviours, promoting indigenous innovation and entrepreneurship (or indigenous new entry or new business venture). The literature shows that firms can use dynamic capabilities for corporate sustainability to keep track of emerging sustainability needs from various stakeholders. Therefore, managing traditional or indigenous knowledge helps businesses gain sustainable performance (Gorjestani, 2001). Shafi *et al.* (2020) state, "notably, government intervention is necessary to revive the traditional handicraft industry. It also helps businesses to seize sustainable development opportunities and reconfigure existing functional capabilities for business sustainability".

The study supports Kaur's (2019) statement that "knowledge management process capabilities are crucial for organizations to pursue competitiveness". A study by Gloet (2006) also shows that effective knowledge management related to human resources helps the leadership and management to develop their ability in terms of supporting the sustainability of the three bottom lines, which are business, environment and social impact. Company capability will also become a great advantage for businesses in facing the ever-changing world (Aldianto *et al.*, 2021). The process of dynamic capabilities (adaptive, collaborative and innovative) can create the foundation of a company's competitive advantage (Kaur, 2019; Aldianto *et al.*, 2021). A high level of dynamic capabilities strongly impacts stakeholders, the community, society and environment. It also supports the business to mobilise the company's internal resources to develop strategic changes towards sustainability. However, Dana (2007) argues that:

[. . .] indigenous people often rely on immediately available resources, and work in indigenous communities is often irregular. Much entrepreneurial activity among indigenous people involves internal economic activity with no transaction, while transactions often take place in the bazaar and in the informal sector, where enterprises often have limited inventory.

Knowledge management aims to help individuals and organisations increase their learning efficiency and information management to achieve better competitive advantages. Dynamic capabilities, as defined by Kaur (2019), are "the firm's ability to integrate, build, and reconfigure internal and external competencies to address rapidly changing environments".

These two processes, knowledge management processes and dynamic capabilities, are used to implement business sustainability and positively impact economic, social and environmental aspects. However, several studies also find out that knowledge management significantly affects business revival strategies and improves leadership and management capabilities (Iqbal and Ahmad, 2021).

On the other hand, dynamic capabilities play a role in innovation and seizing sustainable development opportunities and reconfiguring existing functional capabilities while mobilising the business's internal resources towards sustainability. This one-of-a-kind ability is the ability of the business to make its personnel an integral part of obtaining a competitive advantage. Pundziene *et al.* (2021) said that a firm's dynamic capabilities have a major impact on its open innovation performance and, consequently, on its competitive performance. The genuine assets or unique resources that a business requires to execute its competitive strategy are average assets or special resources. Both resources should be devoted to developing a low-cost competitive advantage that differentiates the company from competitors.

This study also found knowledge management process in terms of combination and dynamic capabilities in terms of adaptive are good strategies of woven craft SMEs to gain competitive advantage. However, dynamic capability in terms of innovation is viewed as a means through which a business adapts to its dynamic environment changes. The shifting business environment has compelled firms to generate new concepts and products. Ziyae *et al.* (2021) identified infrastructures necessary for service innovation, including the adoption of cutting-edge technology in various areas, human infrastructure, capital and proper space and location. Therefore, innovation is becoming increasingly crucial to ensure the sustainability of craft SMEs and enable them to flourish in the marketplace.

*4.4.2 Traditional knowledge management processes' contribution towards competitive advantage and sustainable performance.* In the digital era, a company's ability to innovate in its products will ensure that the product continues to meet the wishes and demands of customers. Gaining a competitive advantage is meeting client desires (Bharadwaj *et al.*, 1993; Hung *et al.*, 2010). Competitive advantage is derived mostly from the values or advantages generated by a business for its customers. Customers often prefer to purchase things that exceed their expectations or desires. However, protecting traditional knowledge on woven craft SMEs is critical for product differentiation towards competitive advantage. The value compares to the given price. Purchases will occur if the customers believe the product's price is reasonable compared to the value it provides. Therefore, the findings indicated that traditional knowledge management processes do not have a significant direct effect on competitive advantage. This study contradicts the view that knowledge-based dynamic capabilities can serve as additional competitive advantages for a business (Hung *et al.*, 2010; Kaur, 2019). However, Dana (2007) argues that indigenous people's perception of opportunity is culturally influenced; however, culturally determined opportunities for entrepreneurship are often disrupted by entities external to indigenous people.

This study also found that it is still a challenge for traditional woven craft SMEs to build their socially responsible operations and innovations. We know that dynamic capabilities in terms of innovation can provide businesses with a competitive advantage. Dröge *et al.* (1994) discovered that product innovation needs to leverage to gain a competitive advantage. Aldianto *et al.* (2021) stated knowledge plays a role in increasing service and product innovation. However, in the traditional woven craft sector, developing product innovation based on customer needs leads to risks. Dana (2007) also argues "social organisation among

indigenous peoples is often based on kinship ties, not necessarily created in response to market needs". In Indonesia, indigineous/traditional knowledge is owned by a local community. External parties who have the expertise and high technology manage traditional knowledge and then modify, specify and mix it to become a new invention that meets customer needs. For traditional knowledge protected by Intellectual Property Rights (IPR), especially patents, the economic benefits will be owned and enjoyed by external parties (Siddiq, 2018). The traditional knowledge owner or local community often gets nothing from the IPR. Therefore, in traditional craft woven businesses, the concept of innovation not only encompasses new products and the implementation of novel ideas or procedures but is also linked to community benefits.

Product innovation in the craft sector must add value to community benefits to gain an advantage over its competitors. However, product innovation might fail for various reasons, including a lack of innovative design or a misperception of customer wants and needs. It has been demonstrated that the relationship between competitive advantage and sustainable performance does not substantially affected. According to Shafi *et al.* (2020), the:

> [. . .]handicraft industry in a country needs to revitalize. Otherwise, centuries-old traditional culture and patrimonial expertise will perish. Additionally, there is a need to attract foreign investment to overcome resource constraints and strengthen the entrepreneurial community's competitive capability.

The connection between competitive advantage and sustainable performance is a culture of creativity inside the organisation when it comes to developing goods that address three aspects of sustainability (profit, people and planet). The severe competition in the traditional woven industry encourages reduced domestic market share, which requires SME weaving to adapt its strategies to changing business and environmental situations. Through changes in local resource-based strategies, the sustainability of SMEs can be assured. Naidu *et al.* (2014) investigate:

> [. . .]eight factors that influence the level of innovation in the handicraft industry, including value addition, design uniqueness, new product development, cultural uniqueness, advanced technology, owner experience, owner ability to adapt to market trends, and raw material quality.

Businesses that continue to monitor their performance and attempt to improve it have a chance of attaining company sustainability. With a strong competitive position, a business has sufficient money to compete against other companies (Dröge *et al.*, 1994; Kaur and Mehta, 2017a, 2017b). Therefore, woven craft SMEs that can develop their products around customer desires will endure in the face of competition because their products will continue to be in demand.

## 5. Conclusion

To summarise, the purpose of this research is to examine the role of traditional knowledge-dynamic capabilities in the sustainability of creative SMEs in the woven craft sector. The results concluded that traditional knowledge management processes positively affect dynamic capabilities and sustainable performance but do not directly affect competitive advantage. Meanwhile, dynamic capabilities significantly affect competitive advantage in managing traditional knowledge. Traditional weaving SMEs need to display a combination of traditional knowledge and the latest knowledge. For example, they need to develop new motifs by combining modern–traditional motifs.

The uniqueness of new motifs can build differentiation. Therefore, the competitive advantage increases if dynamic capabilities mediate the traditional knowledge management processes with market needs. Additionally, this study shows that while the traditional knowledge management processes do not directly affect competitive advantage, they do have a direct effect on long-term performance.

Managerial implications show that woven craft SMEs need to develop a long-term strategy to gain sustainable performance, not only focusing on short-term operations. Craft woven SMEs need to improve their product quality to compete with other areas or countries, stressing product uniqueness while remaining committed to sustainability (profit, social and environment). Therefore, they should improve the ability to manage traditional knowledge by studying market trends and combining traditional knowledge with market knowledge. In addition, it becomes a new challenge for the government to facilitate access to the latest information technology-based marketing, such as the use of the internet for business information and product marketing. Thus, craft woven SMEs can acquire information in a more modern way and open up their global market access. In the end, the local government must be pro-active about transferring traditional knowledge through the generations as the inspiration to create business value. Thus, the next generation can be involved in managing their business through traditional knowledge to benefit the local community.

The theoretical implication shows that traditional knowledge processes influence the sustainable performance of woven craft SMEs. The traditional knowledge processes adopted by craft woven SMEs had a significant effect on sustainable performance in terms of environment, social and profit, though the results found that the effect on profit was lower than social and environment performance. Therefore, to improve sustainable performance in terms of profit, the industry needs to study market trends.

This study can be used as a reference for theory and subsequent empirical studies on the factors that affect sustainable performance. However, in this study's results, there are still shortcomings related to indicators as a measuring tool for variables. Therefore, further research could add several variables according to the development of marketing theories. The author realises that the use of samples through social media in this study still does not meet the population criteria. Therefore, further research related to similar problems needs to expand the sample selection and distribution or expand the focus for certain scales such as the micro, small or medium scale so the results will be more specific and offer more appropriate implications for each business scale.

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