

The Relationship Chain for Enhance Innovation and the Performance Perspective from Environmental Condition, Knowledge Sharing Behavior and Strategic Planning Process

A Study on Small Medium Enterprise (SME's) of the leather industry centre in East Java

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ABSTRACT

The purpose of this research is to enhance innovation and performance SME's with perspective from environment, knowledge sharing behavior, and strategic planning process. The sample of the research is small and medium sized enterprise of handicraft industry that made of leather, e.g. shoes, leather jackets, bags, luggage, belts, wallets, and other products made of genuine leather which still can't compete in Malang, Mojokerto, Magetan, and Sidoarjo. Business world, especially small and medium sized enterprise, faces many challenges which must be anticipated so that the enterprise can keep its sustainable life cycle. In the other hand, environment changes force them to become more careful in planning their business, to always do some information searching so that they can manage their knowledge to create creativity and innovation that can increase competitiveness and work performance. The finding of the research shows that from the nine tested hypotheses with SEM analysis, there are 7 (seven) accepted tests (and they have significant impact), and there are 2 (two) unaccepted tests (and they have insignificant impact), such as the impact of environment and knowledge sharing behavior to business performance. The findings of this research are, *first*, the impact of sharing behavior/developing knowledge to work performance of small and medium sized enterprise should use innovation as antecedent variable, and *second*, the impact of environment changes to work performance of small and medium sized enterprise, is determined by strategic planning variable mediation. A stronger work environment changes force the enterprises to create effective strategic planning process intensity, which do some sustainable information search about market and other information to create creativity in product making designing and services. The implementation of small and medium sized enterprise's knowledge management is not only just to share knowledge about their market, but also must be followed by increasing the knowledge/ability of the employers, giving opinion about employers' performance, fluently communicating, and using technology to design product and facilitate communication and etc.

Keywords: Environment, Knowledge Sharing Behavior, Strategic Planning, Innovation, and Performance

INTRODUCTION

The business world, especially SMEs, have to be able to anticipate various challenges they are facing in order to maintain their business. In the other side, environmental change has required them to take caution in planning their business, and also to continuously searching for information in order to manage the knowledge in creating creativity and innovation which will increase their competitiveness and performance.

Enterprise environmental changes will make the strategic planning more difficult. Harris et al. [1] suggested that there are significant positive influences from the environmental changes factors which influence the strategic planning process. Covin and Slevin [2] proposed that a hostile environment characteristic is as follows unstable industrial settings, a high competition intensity, a tough and hard business climate, and also the lack of exploitable opportunities, whereas the benign environment was characterized as: safe, munificent and manipulated environment.

The key to the enterprise success in a tight competition is their ability to adapt to environmental changes. Companies have to be able to overcome and adjust to a turbulent environmental changes [3][4]. Bourgeois & Eisenhardt [5] posits that environmental changes will make the information needed in a strategic planning process more rapid to obtain. Research of Cohen [6] concluded that general and task environment has an influence to the strategic planning and whereas the strategic planning will influence performance. Fuller [7] also suggested that the decrease of change and uncertainty through high quality information access as one of the effort to accomplish the strategic planning objectives.

In an ever changing enterprise environment, the organization is required to share knowledge between organization members [8]. To overcome a continuously changing environment, the enterprise needed a power to create and maintain the core competence of an organization. This core competence was noted by Hussein [9] to

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shift from a market based from to a resources based view. There are three resources based strategy in an organization: tangible and intangible resources, and very intangible resources. These three resources will eventually leads to knowledge. Handzic [10] emphasized that knowledge management (KM) which include knowledge sharing behaviour, is a practical tool for every company. Knowledge management practice in SMEs is required in order to increase the competitive advantage in a new business environment [10].

Organization will be more innovative depending on the strategy, technology, human/culture, structural, managerial, and, environment [11]. Although environmental change occurred, it is important for SMEs to manage knowledge favourably in order to create a high level of innovation and also a better performance compared to other SMEs without it [12]. Darroch [13] has developed a three dimensional. Measurement of behaviour and, practice of knowledge sharing behaviour, that is: knowledge acquisition, knowledge dissemination and knowledge responsiveness. Knowledge sharing behaviour will influence innovation. Darroch [13] research explained that KM has influenced new innovation in shoe, slippers, leather jacket, bags, and other products design. The leather industry SMEs, spread all over East Java province, have been demanded with many new innovation in shoe, slippers, leather jacket, bags, and other products design.

Nicholas O'Regan and Abby Ghobadian [14] have referred to Milles and Snows research, where it was focused on strategic orientation to apply innovation strategy on SMEs, due to Milles and Snow's typology that was considered the most appropriate typology (Prospector, Defender). Strategic orientation is the most powerful basics to innovate and it has to be applied in strategic formulation and with certain level of distribution. The results are: strategic orientation is the most powerful basics to innovate and it have to be applied in strategic formulation and with certain level of distribution; the use of training, management basics and technology process by the prospector company is a basic used for competitive advantage in the operational environment; prospect or company give a more powerful emphasized on technology process and management in a unstable environment compared to a stable environment. The statement was that the average performance was positively influenced by strategically planning [15][4]. The result was the investigation of positive influence between the strategic planning and the company performance. Hopkins, Willie and Shirley's [3] research explained that the managerial aspect (expertise & believe), organization factors (size and structure of organization) will influence. the strategic planning and the enterprise's financial performance, however, the environmental factors (complexity and change) have no positive influence to the performance. The same opinion was suggested by Haiyang Li [16], however, Cohen [6] have found different result where the environment have a positive influence to the performance.

This research was conducted to test and explain the influence, of environment, knowledge sharing behaviour, and strategic planning process to the innovation and performance of SMEs. Specifically the main objectives of this research are to test and explain the influence of environmental condition to the strategic planning process, knowledge sharing behavior and innovation; knowledge sharing behaviour to the business performance and innovation; innovation to the business performance; strategic planning process to the business performance and innovation; and environment condition to the performance.

MATERIALS AND METHODS

Study have showed that small companies expend almost two times on Research and Development aspect compared to large companies, especially in this research. The result was that small companies are able to rely.

The strategic planning process, and not the strategic planning itself, was the key to improve the business performance [17]. Small companies are less aware aboutthe importance to have a strategic planning process and the management of knowledge.

Generally, the problems faced by SME's in Indonesia are: marketing, capitalization, technology, organization and management. This mean that a research that study the environmental condition influencing the SME's strategic planning process, knowledge management, and innovation is needed. It was feared that if this problems was not address it will decrease the SME's performance. Therefore, in addition too strategic planning, knowledge management (KM) is the practical tool in every organization.

In a turbulent business environment, the organization is required to share their knowledge between the members of the organization [8]. To accomplish a consistent strategic planning objectives, knowledge sharing is crucial in the strategic planning process [18].

From the previous various explanation and background, the hypothesis suggested are as allow: [H1] The increase of environmental change, will increase and intensify the strategic planning process. [H2] The increase of environmental change, will increase knowledge sharing behavior. [H3] The increase of environmental change, will increase the innovation strategy. [H4] The increase of knowledge sharing behavior, will increase the business performance. [H5] The increase of knowledge sharing behavior, will increase the innovation strategy. [H6] The increase of innovation, will increase the business performance. [H7] The increase of strategic planning process, will increase of the business performance. [H8] The increase of strategic planning

process, will increase innovation. [H9] The increase of environmental change, therefore the business performance of SME's will decrease.

This research have an explanation research nature quantitatively and with a qualitative approach by using in-depth interview. In order to obtain the complexity and the depth the data analysis, it will also be equipped with descriptive illustration especially relating to the process of strategic planning, knowledge sharing and development behavior, innovation, and the environment condition faced by the leather industry SME's in East Java (Malang, Mojokerto, Magetan, and Sidoarjo area). The research location was chosen because of the leather icon of East Java. Whereas the research time for collecting data was conducted for six month (November 2008 until may 2009). This research was conducted to SME's which produce leather product such as: shoes, slippers, bags, leather jacket, briefcase, belt, wallet, and other products with original leather materials, with the consideration that the product produce will survive and compete and also market acceptable.

The research subject was entrepreneur of SME's, the object of the research was SME's of the leather industry center. From 160 respondents finish interviewed, only 148 questionnaire are complete and can analysed for quantitative approach. The sample collection method of this research was conducted with "*purposive sampling*", that is the researcher purposively select the SME qualified to the criteria. The sample qualification for the research objectives was: a) have been operating more than three years in their related fields. b) Have used information technology as the communication facility in expanding their market, increase their point of view and knowledge in designing product, etc. c) Willing to be interviewed, voluntarily and proactive answering the questions, that is, responsive to the information the researcher needs. Whereas for interview with qualitative analysis by in-depth interview approach, through nine respondents representing large, medium, and small scale business of the SME's that will be interviewed. The informant criteria was : the owner/entrepreneur, marketing/personnel chief executive considered knowing and involved directly in the business decision makings.

The techniques in collecting data was conducted through: survey and interview by referring to the questionnaire, with previously tested question list, was used as the interview guidance to the targeted respondent. Research questionnaire was used for quantitative approach with analysis tool is Structural Equation Modelling (SEM) which is helped by the AMOS 4.01 program, and qualitative approach by in-depth interview was conducted for the qualitative questionnaire, that is a direct detailed interview with the respondents chosen as the representation of the leather industry center at SME's with small, medium, and large scale business to support quantitative analysis. The objectives of the information and description gathering was to describe clearly the environmental condition faced, the knowledge sharing/development behavior, the existing process of strategic planning, the innovation conducted all of this time and the business performance obtain in the tight competition condition. Therefore the employment of this techniques was separated. Documentation, data gathering by studying every documents or records related to this research. Recording information in this interviews, and also collecting pictures and photographs.

Variable measurement scale with "Likert scale" seven points [19], and operational definition : 1) Environment condition is the environment condition faced by the company with characteristic of: full of risk, pressure & domination or high and overwhelming risk. 2) Strategic Planning process is the planning process that cover the companies strategic planning activity which consist of mission statement, objectives determination, internal and external environment audit, strategic implementation, and strategic option evaluation. 3) Knowledge sharing behaviour is the knowledge sharing behaviour conducted by SME's leader in acquiring (knowledge acquisition), disseminate (knowledge dissemination) and responding to knowledge (responsiveness to knowledge). 4) Innovation was the activity leading to product or service (techniques), administration, managerial change that the company have offered to adapt with the dynamical environment, both for existing product or new products. 5) Business performance was the accumulation of output and capability of every effort conducted by the organization to achieve their goals. This consist of four indicators that was relative sales growth, relative profitability, organization capability and competitive position.

Data Analysis model, the quantitative analysis consist of statistic techniques used in testing research hypothesis by using structural equation modelling (SEM), to test the variable influence hypothesized. Whereas the qualitative analysis technique was conducted by using in depth interview through separated questionnaire to reveal existing variable application on SMEs of East Java.

RESULTS AND DISCUSSION

Research variable description

Measurement result of dimensions or variable indicator which can form a construct or a latent variable will be respectively described with confirmatory factor analysis. While the magnitude of loading factors indicate the ability of each indicator significantly as the dimension of the latent variable. Factor loading values can be seen from the magnitude of standardized regression weight estimate. The magnitude of factor loading with the

criteria of either the larger ideal criteria 0.5 and 0.7 is greater [20]. Here's the translation of 5 variables in this study.

Environmental Conditions Variable. Variable dimensional or observation proposed as an indicator of the environment are: risk (X1.1), pressure (X1.2), and dominance (X1.3). In total, the average value of 4.86 indicates the respondent's answer that the environment faced by SMEs in the position of being, with a risky indicator, it's safe, it means able to control environmental conditions, despite the turmoil the sustainability of the business is still running. From the average dimension of who gets the highest ratings by respondents of 5.25 is the domination of the environment means the ability of SMEs to compete in the industrial market still needed effective efforts with a continuously improvement of the quality, full of creative design products will support innovation in various side. Revealed here and in any case whatever the environmental conditions change and turmoil, SMEs do not feel affected or changes in environmental conditions do not affect business continuity.

Knowledge Sharing Variable. *Knowledge sharing behaviour* measured with 12 (twelve) indicator, that is: attitudes and opinions (X2.1), the financial reporting system (X2.2), focus on the market (X2.3), hire and retain skilled employees (X2.4), market information (X2.5), the spread of information (X2.6), the spread of knowledge on the job (X2.7), mentoring and training (X2.8), knowledge about customers and competitors (X2.9), flexible (X2.11), marketing function (X2.12).

Generally, the average the average value of 4.97 for the respondents' answers indicate that the behaviour of sharing / transferring knowledge in performing of daily business activities are in a position that is fairly responsive to the market demand, competitors behaviour, assessing attitudes and opinions that encourage employees to improve skills still considered moderate by the respondents. From the average dimensions it appears that the focus on market to get the customers and the information industry received the highest ratings 5.78, and knowledge on consumer response, competitor, technology (what product the consumer likes at this time, model, design, price and quality) with a value of 5.76. Meanwhile the lowest score of 2.74 on the dimensions "would prefer a written communication to disseminate knowledge" in the other words, still prefer oral communication than written. This is the real nuance happening on SMEs according to the characteristics and the organizational culture, and the relationship between individuals within the organization is not through the bureaucracy, because the organizational structure of SMEs classified as light. Disadvantages of using written communication are more noticeable that there is still much weakness in the administration, especially in financial accounting. This was revealed during an interview; nearly 30% do not have a good accounting administration.

Strategic Planning Process Variable. In general, the average value of 5.87 for the answers of respondents indicated that strategic planning process carried by the businesses people with a high emphasis means business people are always set a mission and business objectives, analysing and diagnosing internal and external environment, then implementing the strategy and also always evaluating the strategies have been implemented. Dimension with the highest score of 6.11 shows SMEs are always looking at changes in the external environment, especially with the advent of market tastes of new product models, changes made by competitors can quickly adapt so that with constantly observing, and adjusting the changes their business can continue to operate smoothly.

Innovation Variable. Generally the average value of respondents answer by 4.05 shows when the business people launched its first product on the market, offering new product/services that haven't been offered yet, revise or improving the existing product lines, reducing production costs, product reposition, and the implementation of the new idea and policy are not followed with high innovation, in the other words, the innovation are only in the moderate level. It appears that mostly SMEs innovation is driven by the customer by-order demands. So even if they do not think what an innovation product is like, they did innovation because of the customer's order unwittingly.

Business Performance. The average value of respondents answer indicates that business performance shown by business people is high. It shows by the score obtained 5.29. Thus, sales growth, profitability level, level of organizational capability, and the competitive position of the business done is good and high.

Hypothesis testing or quantitative research result

The hypothesis trial was conducted to address questions in this research. The hypothesis will be accepted if the critical ratio value (t count) was higher than the t table or the p value ≤ 0.05 . It was shown that from 9 (nine) hypothesis tested, 7 (seven) trial was accepted and have a significant influence and there were 2 (two) trial rejected and have no significant influence, that was, 4th hypothesis and 9th hypothesis that is, influence of the

environmental conditions (X1) and knowledge sharing behaviour (X2) against business performance (Y2) with t count value under 1.96 and p value ≥ 0.05 . When using degrees of confidence or alpha = 10%, then all the hypotheses are significant and accepted, so there is nothing denied. The picture 5.3 below show the research result between hypothesized variables with alpha = 5%.

Table 1
Reserch Hypothesis Test

Hypothesis	Independent variable	Dependent variable	Loading Factor	T calculation	(p-value)	Result
H.1	Environment condition	Strategic planning process	0.863	2.962	0.003	Significant Positive
H.2	Environment condition	Knowledge sharing behaviour	0.812	2.848	0.004	Significant Positive
H.3	Environment condition	Innovation	-2.183	-2.810	0.005	Significant Positive
H.4	Knowledge sharing behaviour	Business Performance	1.457	1.882	0.060	Not Significant
H.5	Knowledge sharing behaviour	Innovation	0.974	3.203	0.001	Significant Positive
H.6	Innovation	Business Performance	-1.326	-2.059	0.039	Significant Positive
H.7	Strategic planning process	Business Performance	2.046	3.316	0.001	Significant Positive
H.8	Strategic planning process	Innovation	0.899	4.003	0.000	Significant Positive
H.9	Environment condition	Business Performance	- 2.964	-1.771	0.077	Not Significant

Source; data, processed

1. Hipótesis test 1

The influence of environmental conditions on the strategic planning process showed a significant positive, with a value of $p = 0.003$ and loading factor of 0.863. This testing result provide enough empirical proof to accept hypothesis 1 which said the increasing changes in environmental conditions can increase and intensify the process of strategic planning. This means, the SMEs have always been able to adjust themselves with the internal, external change occurred and also they have adjust with the competitor and the market, because only with this adjustment they will be able to increase their competitiveness.

2. Hipotesis test 2

The influence of environmental conditions on Knowledge Sharing Behaviour showed a significant positive results, with a value of $p = 0.004$ and the *loading factor* by 0.812. This testing result provide enough empirical proof to accept hypothesis 2 which said the increasing changes in environmental conditions can increase the *knowledge sharing behavior*. The increase of SMEs behavior in sharing and developing knowledge is needed. This knowledge consist of attitude and opinion judgment to encourage employee to increase their expertise, focus actively to obtain market and customer information, actively disseminate market information, and responsive to the consumer knowledge. Therefore SMEs are required to exploit and reveal tacit knowledge they have in order to accomplish their targeted market pattern and trends. To be more responsive to the competitor and technology and possessing a developed marketing function, though in a simplest context, such as flexible dissemination, and unwritten form as in large companies.

3. Hipótesis Test 3

The influence of environmental conditions on innovation showed a significant results, with a value of $p = 0.005$ and the loading factor = -2,183 This testing result provide enough empirical proof to accept hypothesis 2 which said the increasing changes in environmental conditions can increase innovation. Changing environmental conditions encourage SMEs to have time to create and innovate, so the strategic thinking ideas is growing.

The environment continuous changes have been responded by the SMEs with translating those changes into the creation of new, more creative and innovative product, although this come from other companies, and also a better administration services.

4. Hipótesis Test 4

This hypothesis test showed a different result, not significant which evaluated the effect of knowledge sharing behaviour on business performance. Knowledge sharing behaviour has no effect and not significantly affect the business performance. It appears from the value t count = 1182 and p value 0060 and the loading factor = 1.457. The test results indicate that there is not enough empirical proof to accept hypothesis 4. Knowledge sharing behaviour was not proven to influence the business performance of the SMEs in East Java. This was an interesting finding on SMEs, that is, the knowledge sharing behaviour still have a large role but it was informal, it did not have to be written, relatively simple related to the structural relationship between the entrepreneur and the workers. This relationship that was conducted without any bureaucracy line, unwritten but with direct communication, and with the problem solving relying on experience and intuition, with direct communication with trusted people or marketing department, and also by using that information as the basics to construct a strategy in innovation will automatically increase the performance. The point is that this interesting finding showed that knowledge sharing behaviour will have significant influence towards performance if innovation was used as an antecedent variable

5. Hipótesis Test 5

The influence of Knowledge sharing behaviour on innovation showed that a significant positive result. It appears from the t count value = 3.203 and p value = 0.001 and loading factor = 0.974, coefficient provide enough empirical proof to accept hypothesis 5 which said the increasing of knowledge sharing behaviour can improve the strategic innovation. SMEs have been aware of their role in increasing the resources quality through training, motivating, and actively searching for market information, to facilitate the creativity and innovativeness of their enterprise. Other findings are that the product from Mojokerto was superior in model but the product from Magetan was superior in quality.

6. Hipótesis Test 6

The influence of innovation on business performance showed a significant positive, it appears from the t count value = -2,059 p value = 0.039 and loading factor = -1,326. This coefficient provides enough empirical proof to accept hypothesis 6 which said the increasing of strategic innovation can improve the business performance. The innovation that SMEs has conducted to be proven to increase the business performance. Logically, this finding is acceptable and it was expected that by conducting innovation the performance and competitiveness will increase. They have to always create facilitating method or procedure: product order, payment, and sample creation according to the buyers' request. And also to search and collect information about new models that the consumers prefer because the fashion trend will always change and the service have to be continuously improved.

7. Hipótesis Test 7

The influence of strategic planning on business performance showed a significant positive result, it appears from the t count value = 3.316, p value 0.001 and loading factor = 2.046. This coefficient provides enough empirical proof to accept hypothesis 7 which said the increasing of strategic planning can improve the business performance. Effective planning has influenced the SMEs business performance. Although the strategic planning process form was more modest compared to large companies, but it have a high influence to the performance of the company. Because the SMEs have the commitment to their objectives, and continuously observing their competitor and trying to adjust themselves to the market changes in their industry

8. Hipótesis Test 8

The influence of strategic planning on innovation showed a significant positive result, it appears from the t count value = 4,003, p value 0.000 and loading factor = 0.899. This coefficient provides enough empirical proof to accept hypothesis 8 which said the increasing of strategic planning can improve the innovation. The strategic planning process conducted with high intensity has an influence to the SMEs innovation strategy. In other words, SMEs which have analysed their environment, especially external environment, with accurately and intensively will usually be entailed by the emergence of innovation both in product form, or more flexible service to customers. This flexible service includes a flexible payment form, a good relationship with the customers, improvement in administration and business accounting, and so on

9. Hipótesis Test 9

The influence of the environmental condition on business performance shows a different result that there is no significant influence between environmental condition and business performance. It was appeared on the t count value = -1,771, p value 0.077 and loading factor = -2.964. This coefficient provides not enough empirical proof to accept hypothesis 9 which said the increasing of the environmental condition can improve the business performance. To influence the business performance it has to go through strategic planning process as the intervening variable. This was an interesting finding from this research that is, they have already have a networking with their customers and their product have already based on order (there were 87 respondents, with almost 60%). There was also uniqueness in their business, where every SMEs has 5-15 craftsmen as their partners, besides their certain amount of employees. In a low market demand condition, the SMEs will continue to produce their product to fill in their product stock, and to maintain their employee payroll and jobs. SMEs have realized that their business have many limitation and obstacles. This condition have required them to maintain the continuity of their business with sacrificing some or part of their profit when the environment changes. This means they are willing and able to accept the impact from those environment changes. They can not react directly and recklessly by increasing their price right away, but they will adjust it at later period by explaining to their customers.

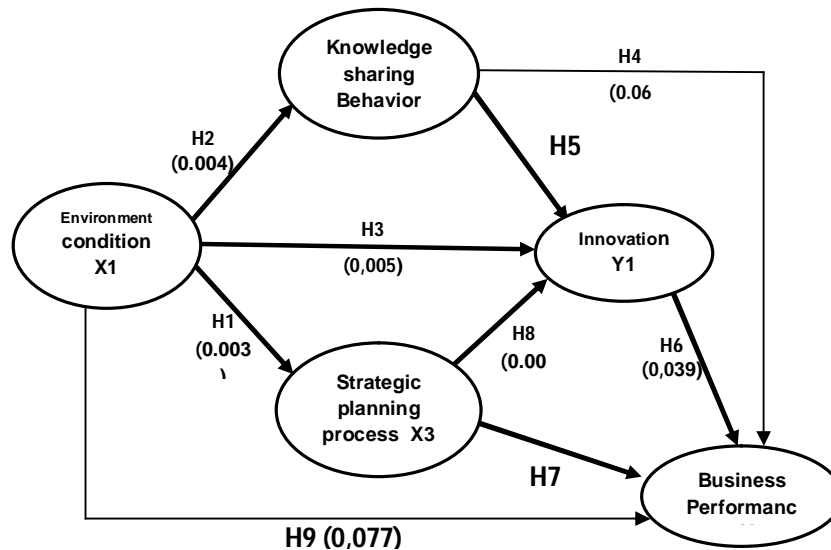


Figure 1 Quantitative result

Note: :
 —————> Significant positive
 —————> Not Significant
 Significant for $\alpha = 5\%$

Qualitative research result analysis: the explanation of In depth interview

a. Environment condition

"Although the fuel price have increase, and the dollar also increase but it gave us no problems at all, what is important is that our business survive (they view this with composure). So it is no different, although we have to give in and decrease a little of our profit. I have to maintain our relationship with my craftsmen, I don't want him to loose his jobs, therefore the company continued to stock (produce) even tough the consumer have decreased or delay their order, and sometime in the future the demand will be restored once again."

"I always search and present the product and give a better service in order to maintain my customers. I always observe product from local competitor or foreign competitor by sightseeing to JMP, Pasar Turi, read magazine, model design for artist, searching models from the internet and it was proven to have competitiveness, and always updated. Especially for jacket, my source of innovation comes from copying cloth jacket models and often those creative and innovative products were made by customer request."

b. Environmental condition faced by SMEs today

"If a business was conducted with seriousness and carefulness but also complying a good quality and service it will make customers to continue ordering our product."

"The quality of the materials supporting a quality production is sometimes hard to obtain, there are also fluctuating material prices and even limited quantity of materials."

"Clear product marketing, a strong business partner, a stand at a strategic market will make the influence of I the environment less influencing and controllable (Magetan, Mejokerto and Sidoarjo).

c. Knowledge sharing behaviour in SMEs

The method in disseminating knowledge is by communicating it to the management and then followed to related department according to the procedure and the organization system of the company (large SME), whereas the most small SME communicate it directly due to the routine meeting in the office space. They consider written communication as ineffective. And communicating all of this to strengthen and maintain quality.

We continuously maintain and preserve our employee and relationship with the craftsmen because of the difficulty in : obtaining an expert and experienced craftsman, because nowadays there are no younger people who are interested in shoes"

d. Strategic planning and process in SME

"My business -plan are always available, by determining our objectives, observing our external and internal environment, observing the competitor and the market, and then evaluate what we have done routinely in order to maintain our pace with other business, but this business plan was not arranged and written in good order.

e. Innovation in SMEs today

Often a product model was delivered by the consumer; they take this model from magazines or torn an artist (especially leather jacket and Magetan shoes). I don't need to think about innovation because the model and the variation have already been given examples from the buyer or ordered.

f. Performance

Averagely the performance reach was quite high, SME have no high target such as large companies, but as long as the craftsman and the worker keep working and my product could sell in the market, and the profit and the business will go on.

As a small entrepreneur I feel satisfied. For the last three years the profit have rise for 30%. this was caused by the increased of demand due to the difficulty in increasing product price.

"Yes I always search and collect information about new models for the consumers due to the ever changing nature of fashion trend and the service needs to be increase because this is the only way SME could compete."

"What we have to do is always search information about product demanded by the buyers and inform it I to the employee or the craftsmen and after that produce new models that is, attracting buyer and with quiet steps to avoid. Other SMEs copying what we had. This step was proven to increase our production.

This research has some limitation that was 1) it was conducted on Leather industry SMEs, therefore there are probabilities of not generalized result in other SMEs; and it was only used samples from SMEs of leather SMEs central, with no SMEs outside of the central that was taken.

CONCLUSION

1. Knowledge sharing behavior was not proven to influence the business performance of the SMEs in East Java. This was an interesting finding on SMEs, that is, the knowledge sharing behavior still have a large role but it was informal, it did not have to be written, relatively simple related to the structural relationship between the entrepreneur and the workers. This relationship that was conducted without any bureaucracy line, unwritten but with direct communication, and with the problem solving relying on experience and intuition, with direct communication with trusted people or marketing department, and also by using that information as the basics to construct a strategy in innovation will automatically increase the performance. The point is that this interesting finding showed that knowledge sharing behavior will have significant influence towards performance if innovation was used as an antecedent variable.
2. The environment change has no influence to the business performance of SMEs. To influence the business performance it has to go through strategic planning process as the intervening variable. This was an

interesting finding from this research that is, they have already have a networking with their customers and their product have already based on order (there were 87 respondents, with almost 60%). There was also uniqueness in their business, where every SME's has 5-15 craftsmen as their partners, besides their certain amount of employees. In a low market demand condition, the SMEs will continue to produce their product to fill in their product stock, and to maintain their employee payroll and jobs. SMEs have realized that their business have many limitation and obstacles. This condition have required them to maintain the continuity of their business with sacrificing some or part of their profit when the environment changes. This means they are willing and able to accept the impact from those environment changes. They can not react directly and recklessly by increasing their price right away, but they will adjust it at later period by explaining to their customers.

SUGGESTION

1. The capability of SMEs in preserving their existence and their strength in facing environmental changes and the tight competition have to be improved continuously in order to maintain their business continuity, their ability in creating employment and also developing the ever increasing local economy.
2. SMEs need to strengthen their relationship through their existing organization to increase their bargaining position with the leather supplier, and to extend their market.
3. As an effort to strengthen their market position and access various government funding, the SMEs need to strengthen their association organization such as cooperative, etc.
4. For future research, it is necessary to develop this research by adding local culture to analyze further factors which could increase creativity and performance.
5. To conduct a more effective innovation, Leather industry SMEs central in East Java needs to focused their attention to: (1) the search of market and research information; (2) identifying and using market opportunities and (3) calculate the cost and risk occurred because of the market changes.

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