

The mediating role of competitive advantage in linking creativity and innovation culture to MSMEs' business performance in Malang City: A mixed-method study

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Abstract

Micro, Small, and Medium Enterprises (MSMEs) operate in increasingly competitive environments that require sustained creativity and innovation to achieve superior performance. This study examined the mediating role of competitive advantage in the relationship between creativity, innovation culture, and business performance of MSMEs in Malang City. A mixed-method explanatory design was employed to provide both contextual depth and empirical validation. The qualitative phase involved semi-structured interviews with key stakeholders, including government representatives, MSME community leaders, and business owners, to explore ecosystem-based innovation dynamics. The quantitative phase collected survey data from 120 MSME actors selected through purposive sampling, using structured questionnaires adapted from validated measurement scales. The data were analyzed using Partial Least Squares Structural Equation Modeling (PLS-SEM). The results demonstrated that creativity and innovation culture did not directly influence business performance; however, both variables significantly affected performance indirectly through competitive advantage. These findings indicate a full mediation effect, suggesting that internal creative and innovative capacities translate into superior performance only when transformed into strategic competitive positioning. The study extends the Resource-Based View and Schumpeterian innovation perspective by empirically validating the mediating mechanism within a local MSME ecosystem context. Practically, the results highlight the importance of strengthening innovation culture and strategic differentiation to enhance MSME competitiveness.

Keywords: *business; competitive; creativity; innovation; mediation; MSMEs; performance*

INTRODUCTION

Micro, Small, and Medium Enterprises (MSMEs) play a pivotal role in Indonesia's economic structure, representing approximately 99% of business entities and contributing significantly to national gross domestic product and

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employment generation (Ministry of Cooperatives and SMEs, 2023; Tambunan, 2019). Their capacity to promote inclusive growth, stimulate local innovation, and sustain economic resilience during periods of crisis underscores their strategic importance (ADB, 2020; OECD, 2018; World Bank, 2021). In response, the Indonesian government has introduced various support mechanisms, including financial access programs such as People's Business Credit (KUR), digital transformation initiatives, and structured entrepreneurship training (Ministry of Cooperatives and SMEs, 2023; OECD, 2022). Despite these interventions, structural constraints remain evident, including limited capital access, uneven technological adoption, and intensified market competition (APINDO, 2024; Malmström et al., 2022). These persistent challenges suggest that internal strategic capabilities—particularly creativity and innovation—are increasingly critical for sustaining MSME competitiveness.

Creativity refers to the ability of business actors to generate novel and useful ideas that can be translated into value-creating initiatives (Amabile, 1996; Kalil & Aenurohman, 2020). Within MSMEs, creativity contributes to product differentiation, adaptive marketing strategies, and the exploration of new market opportunities (Febriansyah, 2020; Manalu, 2022). However, creativity alone does not automatically ensure improved performance; its impact depends on the extent to which creative ideas are effectively implemented and strategically positioned.

Innovation culture extends beyond isolated innovation activities and reflects an organizational environment that systematically encourages experimentation, knowledge sharing, and continuous improvement (Damanpour & Aravind, 2012; Expósito & Sanchis-Llopis, 2019). Firms that cultivate innovation-oriented norms and leadership commitment demonstrate stronger adaptability and responsiveness to environmental shifts (Ndesaulwa & Kikula, 2016). In MSME contexts, innovation culture facilitates operational efficiency, digital integration, and product diversification (Sulistyo & Ayuni, 2020). From a Schumpeterian perspective, innovation becomes a central driver of competitive transformation when new combinations of resources are introduced into the market (Schumpeter, 1934).

Competitive advantage represents the strategic outcome of effectively leveraging internal capabilities to create superior value relative to competitors (Barney, 1991; Porter, 1985). According to the Resource-Based View, firm performance improves when valuable, rare, and inimitable resources are strategically deployed. In MSMEs, competitive advantage may emerge from niche specialization, localized responsiveness, and innovation-driven differentiation (Herman, 2018). Nevertheless, empirical research often examines creativity, innovation, and performance relationships in a direct linear manner, overlooking the possibility that competitive advantage functions as an intervening mechanism through which internal capabilities are converted into measurable performance outcomes.

This theoretical gap is particularly relevant in regional ecosystems such as Malang City, where structured collaboration among government institutions, academia, business communities, and industry actors has fostered a dynamic creative economy environment (Muljaningsih et al., 2023; Trianti et al., 2024). MSMEs in Malang have demonstrated notable development in creative industries, culinary innovation, and digital entrepreneurship (Wardhani & Putra, 2023). Although previous studies highlight the importance of creativity and innovation in regional competitiveness, limited empirical investigation has examined whether competitive advantage mediates the relationship between creativity, innovation culture, and MSME business performance within such an ecosystem context.

Addressing this research gap, the present study investigates the mediating role of competitive advantage in linking creativity and innovation culture to MSME business performance in Malang City. By integrating qualitative insights regarding ecosystem support with quantitative structural modeling analysis, this research provides a comprehensive explanation of how internal creative and innovative capacities are transformed into strategic competitive positioning and performance outcomes. The study contributes theoretically by extending the Resource-Based View and innovation theory through a mediation-based framework and contributes practically by offering evidence-based recommendations for strengthening regional MSME competitiveness.

This study develops a mediation-based conceptual framework that explains how internal strategic capabilities are transformed into measurable performance outcomes. Specifically, creativity and innovation culture are positioned as foundational organizational capabilities that enable firms to generate novel ideas and systematically implement improvements. However, these internal capacities do not automatically translate into superior business performance. Instead, their performance implications depend on the extent to which they are converted into competitive advantage.

Drawing upon the Resource-Based View (Barney, 1991), internal resources create value when they are strategically deployed to achieve differentiation or cost efficiency. Creativity contributes to idea generation and strategic renewal, while innovation culture supports the institutionalization of experimentation, learning, and continuous improvement. Competitive advantage functions as the mediating mechanism that captures the firm's ability to transform these capabilities into superior market positioning. Business performance is conceptualized as the observable outcome reflected in growth, market expansion, and operational effectiveness.

Accordingly, this framework proposes that creativity and innovation culture influence business performance indirectly through competitive advantage. By positioning competitive advantage as a mediator rather than merely an outcome variable, the model provides a more nuanced explanation of how MSMEs leverage internal capabilities within competitive environments.

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This mediation perspective strengthens theoretical clarity by integrating capability-based and market-based explanations of firm performance within a single structural model.

The conceptual model illustrating these relationships is presented in Figure 1.

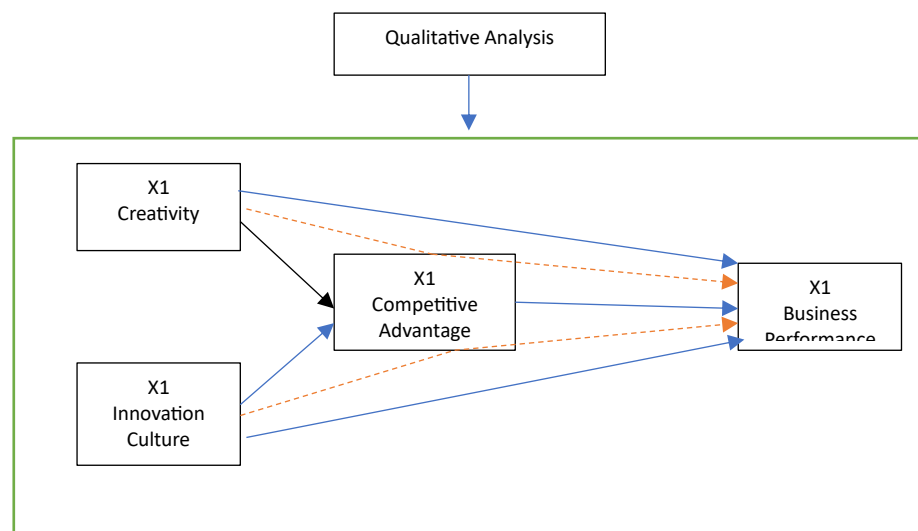


Figure 1. Conceptual framework illustrating the mediating role of competitive advantage in the relationship between creativity, innovation culture, and business performance.

Method

This study employed a mixed-method explanatory design integrating qualitative and quantitative approaches to obtain a comprehensive understanding of the factors influencing MSME development in Malang City. A mixed-method strategy was selected because it enables the integration of contextual exploration and statistical testing, thereby enhancing the validity and depth of research findings (Creswell & Plano Clark, 2018). The combination of qualitative and quantitative data allowed for triangulation, strengthening interpretive robustness and reducing potential methodological bias (Tashakkori & Teddlie, 2010).

Qualitative Phase

The qualitative phase was conducted to explore ecosystem dynamics and stakeholder perspectives regarding creativity, innovation culture, and competitiveness. Data were collected through semi-structured, in-depth interviews with key informants representing multiple stakeholder groups. These included government officials from the Department of Industry and Trade, representatives of MSME communities such as Pelangi Nusantara (Pelanusa), and selected MSME owners from various sectors. Informants were selected based on their strategic involvement in MSME development and their experience

in entrepreneurial and policy-related activities, consistent with purposive sampling principles in qualitative inquiry (Patton, 2015).

The interviews were guided by thematic protocols focusing on creativity practices, innovation processes, competitive positioning, and ecosystem support mechanisms. All interviews were transcribed and analyzed using the interactive model proposed by Miles, Huberman, and Saldaña (2014), which involves data condensation, data display, and conclusion drawing with iterative verification. Through systematic coding and thematic categorization, recurring patterns were identified to construct contextual insights that informed the quantitative phase.

Quantitative Phase

The quantitative phase aimed to empirically test the structural relationships among creativity, innovation culture, competitive advantage, and business performance. Data were collected through a structured questionnaire distributed to 120 MSME owners operating in Malang City. Respondents were selected using purposive sampling to ensure that participants met predefined criteria, including active business operation and sectoral representation in culinary, craft, fashion, and digital-based industries. Purposive sampling was deemed appropriate for studies focusing on specific population characteristics relevant to research objectives (Hair et al., 2019).

The questionnaire measured four latent constructs: Creativity (CRE), Innovation Culture (INN), Competitive Advantage (CA), and Business Performance (BP). Measurement indicators were adapted from established empirical studies to ensure content validity. Responses were recorded using a five-point Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree), consistent with standard behavioral research practices.

Data Analysis

Quantitative data were analyzed using Partial Least Squares Structural Equation Modeling (PLS-SEM) with SmartPLS software. PLS-SEM was selected because it is suitable for predictive research models, complex mediation structures, and studies with relatively small to medium sample sizes (Hair et al., 2019; Henseler et al., 2009). The analysis followed a two-stage procedure consisting of measurement model evaluation and structural model assessment.

In the measurement model evaluation, internal consistency reliability was assessed using Cronbach's Alpha and Composite Reliability (CR), while convergent validity was evaluated using Average Variance Extracted (AVE). Discriminant validity was assessed through the Fornell-Larcker criterion and cross-loading analysis. All constructs met established threshold criteria, confirming measurement adequacy.

In the structural model evaluation, hypothesized relationships were examined using path coefficients, t-statistics, and p-values derived from bootstrapping procedures with resampling. The explanatory power of endogenous constructs was assessed using R^2 values, and mediation effects

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were tested by examining indirect path significance following contemporary mediation assessment procedures (Hair et al., 2019).

By integrating qualitative exploration with quantitative structural modeling, this methodological design provided both contextual interpretation and empirical validation. The use of triangulation and rigorous statistical testing enhanced the reliability, validity, and theoretical robustness of the study's findings.

Results and Discussion**Qualitative Findings**

The qualitative findings revealed a structured innovation ecosystem in Malang City that supports MSME development through coordinated institutional and community-based mechanisms. Analysis of interview data identified three dominant themes: institutional ecosystem support, community-driven capability enhancement, and innovation-oriented strategic behavior among MSME actors. Together, these themes provide contextual explanation for how creativity and innovation culture are transformed into competitive advantage.

Institutional Ecosystem Support and Competitive Positioning

Interviews with representatives from the Cooperative and Industry Office and the Malang Creative Center (MCC) indicated that the local government has institutionalized MSME development through structured programs emphasizing digitalization, product standardization, capacity building, and market expansion. Rather than operating as isolated interventions, these programs function as integrated mechanisms aimed at strengthening firms' strategic positioning.

The Malang Creative Center emerged as a central innovation hub facilitating mentoring, co-working collaboration, business incubation, and market matchmaking. Informants emphasized that access to mentoring and collaborative networks enabled MSMEs to refine product differentiation strategies and improve branding effectiveness. From a theoretical perspective, these findings suggest that ecosystem-level support enhances the conversion of creative ideas into tangible competitive advantage. Thus, creativity and innovation culture are reinforced through institutional infrastructure that enables strategic implementation rather than remaining at the ideational level.

Community-Based Empowerment and Capability Development

The role of Pelangi Nusantara (Pelanusa) was identified as a critical intermediary mechanism in strengthening entrepreneurial capacity. Community leaders described how structured mentoring programs supported business ideation, operational management, and digital marketing skills. Importantly, the empowerment approach was adaptive, addressing specific constraints faced by MSME actors, including women entrepreneurs and home-based businesses.

The qualitative evidence indicates that community-based mentoring contributes to the development of innovation culture by fostering continuous learning, experimentation, and collaborative problem-solving. These practices enhance managerial capability and operational differentiation, which in turn

strengthen competitive advantage. The findings imply that innovation culture is not solely an internal organizational phenomenon but is socially reinforced through ecosystem-based learning networks.

Innovation Orientation and Strategic Adaptation Among MSMEs

Interviews with MSME actors revealed high awareness of digital transformation and competitive adaptation. Entrepreneurs reported adopting e-commerce platforms, refining product design, implementing cost-efficiency strategies, and utilizing storytelling and local identity branding to differentiate products. These actions reflect proactive strategic behavior rather than reactive survival responses.

Importantly, MSME actors consistently linked creative product development and innovation practices to improved market visibility and customer retention. However, informants emphasized that performance improvements were achieved when creativity and innovation resulted in clear differentiation or efficiency gains. This insight aligns with the mediation logic proposed in this study: creativity and innovation culture influence business performance only when they generate competitive advantage.

Synthesis of Qualitative Findings

Overall, the qualitative findings indicate that creativity and innovation culture contribute to MSME performance indirectly through strategic positioning mechanisms. Institutional support, community mentoring, and entrepreneurial adaptation collectively function as enabling conditions that facilitate the transformation of internal capabilities into competitive advantage. While stakeholders consistently associated innovation practices with improved competitiveness, the qualitative evidence suggests that the performance effect is contingent upon successful differentiation and strategic deployment.

These findings provide contextual justification for the quantitative mediation analysis. The qualitative phase clarifies the mechanisms underlying the hypothesized relationships, while the subsequent structural modeling empirically tests the magnitude and significance of these indirect effects.

Quantitative Findings

Descriptive Statistics

The majority of respondents were small business owners (68%), with business age ranging between three and ten years. Most enterprises operated in the culinary and craft sectors, reflecting the dominant structure of Malang's creative economy. Respondents represented varied educational backgrounds and levels of digital adoption, indicating a heterogeneous yet moderately digitally engaged MSME population. This profile supports the contextual relevance of examining creativity, innovation culture, and competitive advantage within a dynamic entrepreneurial environment.

Measurement Model Evaluation

The measurement model was assessed to ensure construct reliability and validity prior to structural analysis.

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Table 1: Outer Loadings of Indicators

Construct	Indicator	Loading Factor
Creativity	CRE1	0.77
	CRE2	0.81
	CRE3	0.74
	CRE4	0.76
Innovation Culture	INN1	0.80
	INN2	0.79
	INN3	0.79
	INN4	0.82
Competitive Advantage	CA1	0.84
	CA2	0.81
	CA3	0.81
Business Performance	BP1	0.80
	BP2	0.76
	BP3	0.78

Source : Research Data 2025

All indicator loadings exceeded the recommended threshold of 0.70, confirming adequate indicator reliability. The loading structure demonstrates strong convergent validity, indicating that each indicator meaningfully reflects its respective latent construct. The absence of weak loadings suggests that the measurement items are both conceptually aligned and statistically robust.

Table 2: Measurement Model Evaluation (PLS-SEM)

Construct	Cronbach's Alpha	Composite Reliability	AVE
Creativity (CRE)	0.82	0.88	0.61
Innovation Culture (INN)	0.84	0.89	0.65
Competitive Advantage (CA)	0.80	0.87	0.60
Business Performance (BP)	0.81	0.88	0.63

Source : Research Data 2025

All constructs demonstrated strong internal consistency, with Cronbach's Alpha and Composite Reliability values exceeding 0.70. Average Variance Extracted (AVE) values were above 0.50 for all constructs, confirming convergent validity. These results indicate that the measurement model met established psychometric standards and provided a reliable basis for structural model assessment.

Structural Model Evaluation

The structural model analysis examined both direct and indirect relationships to evaluate the mediating role of competitive advantage.

Direct Effects**Table 3.** Path Coefficient (Direct Effect)

Path	Path Coefficient	T-Statistic	p-Value
CRE → CA	0.312	3.58	< 0.001
INN → CA	0.438	4.118	< 0.001
CA → BP	0.487	5.42	< 0.001
CRE → BP	0.105	1.422	> 0.05
INN → BP	0.132	1.71	> 0.05

Source : Research Data 2025

The results reveal that both creativity and innovation culture significantly influenced competitive advantage. Innovation culture exhibited a stronger effect ($\beta = 0.438$) compared to creativity ($\beta = 0.312$), suggesting that systematic

innovation practices contribute more substantially to strategic positioning than ideational creativity alone. Competitive advantage demonstrated a strong and highly significant impact on business performance ($\beta = 0.487$), confirming its central role in driving performance outcomes.

However, the direct effects of creativity and innovation culture on business performance were not statistically significant. This finding indicates that internal capabilities do not directly translate into improved performance. Instead, their impact depends on whether they are effectively transformed into competitive advantage. This result directly supports the proposed mediation hypothesis and strengthens the theoretical argument that strategic deployment of capabilities is essential for performance realization.

Indirect Effects (Mediation Analysis)

Table 4: Path Coefficient (Indirect Effect)

Path	Path Coefficient	T-Statistic	p-Value
CRE → CA → BP	0.152	3.215	< 0.001
INN → CA → BP	0.213	3.998	< 0.001

Source : Research Data 2025

The indirect effects were positive and statistically significant for both paths. Creativity influenced business performance through competitive advantage ($\beta = 0.152$), while innovation culture showed an even stronger mediated effect ($\beta = 0.213$). Because the indirect effects were significant while the direct effects were not, the results indicate full mediation. This confirms that competitive advantage serves as the critical mechanism through which creativity and innovation culture enhance business performance.

These findings align with the Resource-Based View, which argues that internal resources generate value only when strategically deployed. Creativity and innovation culture function as strategic inputs, but competitive advantage represents the mechanism that converts these capabilities into tangible performance outcomes.

Model Explanatory Power (R-Square)

The R^2 value for competitive advantage (0.519) indicates that creativity and innovation culture explain 51.9% of its variance. This represents a moderate-to-strong explanatory level, suggesting that internal capabilities are substantial predictors of strategic positioning.

Table 5: R Square

Variables	R Square
Competitive Advantage (CA)	0.519
Business Performance (BP)	0.445

Source : Research Data 2025

The R^2 value for business performance (0.445) indicates that 44.5% of performance variance is explained by the model. This demonstrates moderate predictive power and confirms that competitive advantage meaningfully contributes to performance outcomes within MSMEs.

Overall, the structural model exhibits substantial explanatory relevance, reinforcing the theoretical proposition that internal creative and innovation

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capabilities improve business performance primarily through competitive positioning mechanisms.

DISCUSSION

This study aimed to examine whether competitive advantage mediates the relationship between creativity, innovation culture, and business performance within the MSME ecosystem of Malang City. The findings provide consistent evidence—across qualitative and quantitative phases—that internal creative and innovation capabilities do not directly enhance performance; rather, their performance effect operates through competitive advantage.

The structural model results demonstrate full mediation, indicating that creativity and innovation culture contribute to business performance only when they are successfully translated into differentiation, strategic positioning, or operational superiority. This finding refines prior empirical studies that predominantly report direct positive relationships between creativity, innovation, and performance (Expósito & Sanchis-Llopis, 2019; Ndesaulwa & Kikula, 2016). While previous research confirms that innovation-oriented firms tend to perform better, the present study clarifies the mechanism underlying this relationship. Specifically, creative and innovative activities generate performance gains only when they create defensible competitive advantages.

The qualitative findings reinforce this interpretation. Stakeholders consistently emphasized that product innovation, branding strategies, and digital transformation initiatives became economically meaningful only when they improved market visibility, customer retention, or cost efficiency. This ecosystem-level evidence supports the mediation logic identified in the structural model and demonstrates that internal capability alone is insufficient without strategic deployment.

From a theoretical standpoint, these findings extend the Resource-Based View (Barney, 1991) by empirically demonstrating that creativity and innovation culture function as strategic resources whose value depends on their conversion into competitive advantage. The results also align with Schumpeter's innovation theory, which argues that innovation drives economic progress when new combinations of resources reshape market competition. However, this study advances the argument by showing that innovation's economic impact is conditional upon its capacity to create competitive differentiation.

Importantly, the study contributes to the entrepreneurial ecosystem literature by integrating institutional and community dimensions into the mediation framework. Government initiatives through the Malang Creative Center and mentoring support from Pelangi Nusantara were found to strengthen the capability-to-advantage transformation process. These institutional mechanisms enhance knowledge sharing, digital literacy, and market access, thereby increasing the likelihood that creative ideas become strategic assets. This suggests that ecosystem support does not directly produce performance improvements but facilitates the strategic conversion of internal capabilities into competitive positioning.

The results also respond to the broader debate regarding why some innovation-oriented MSMEs fail to achieve performance gains despite engaging in creative practices. The findings suggest that innovation intensity alone is insufficient; strategic alignment and competitive positioning are decisive. This insight provides a more nuanced explanation of MSME competitiveness in emerging economies, where resource constraints require efficient capability deployment.

Overall, this study demonstrates that the relationship between creativity, innovation culture, and business performance is structurally mediated rather than directly linear. By empirically validating the mediating role of competitive advantage within a localized MSME ecosystem, the research advances theoretical clarity and offers actionable implications for policymakers and practitioners. Strengthening competitive positioning mechanisms—rather than merely encouraging creative activity—appears essential for enhancing MSME performance sustainability.

Theoretical Implications

The theoretical implications of this study indicate that efforts to enhance creativity and innovation as strategies for increasing the added value of MSMEs in Malang City are strongly aligned with contemporary entrepreneurial theories. The findings provide empirical support for the Schumpeterian Innovation Theory, which highlights the central role of innovation in driving economic transformation and competitive differentiation. MSMEs in Malang have demonstrated this by developing new products and improving existing ones, enabling them to better meet market needs and strengthen their competitive position.

This research also affirms the relevance of the Resource-Based View (RBV), suggesting that MSMEs are effectively leveraging internal resources—such as creative capabilities, entrepreneurial skills, and access to digital technologies—to generate competitive advantage. These internal strengths are shown to contribute significantly to business outcomes, particularly when mediated through competitive positioning. The study further supports the Dynamic Capabilities Theory, as MSMEs in Malang display not only the ability to respond to external changes but also to proactively shape opportunities through continuous learning, innovation training, and strategic collaboration.

In line with the Entrepreneurial Orientation (EO) framework, the results emphasize the importance of innovation, proactiveness, and risk-taking as behavioral dimensions that support sustained competitiveness. MSMEs that adopt a forward-looking and opportunity-driven orientation are more likely to convert their creative and innovative potential into market success. Moreover, the study contributes to the Social Network Theory, demonstrating that collaboration between MSMEs, local government, and community actors—such as through the Pelanusa community—facilitates the exchange of resources, knowledge, and strategic partnerships. These networks serve as a critical enabler of innovation diffusion and capability development.

Altogether, the findings underscore that the strategic management of creativity and innovation—supported by internal capabilities and external

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partnerships—plays a vital role in enhancing MSME competitiveness. This study not only confirms theoretical propositions but also offers practical insights into how entrepreneurial ecosystems can be structured to support sustainable small business growth in dynamic market environments.

Practical Implications

The practical implications of this study offer clear direction for MSME actors in Malang City seeking to enhance their competitiveness through innovation and creativity. The findings emphasize that strengthening innovation capacity and fostering creative thinking can serve as a strategic foundation for developing high-value-added products. For MSME practitioners, this underscores the need to invest in targeted training, technological adoption, and market insights to produce offerings that align with evolving consumer demands. Recognizing innovation as a long-term strategic priority, rather than a short-term solution, is essential for sustaining growth in increasingly dynamic markets.

For policymakers and supporting institutions, the study highlights the importance of creating an enabling environment that nurtures innovation among MSMEs. Strengthening facilities like the Malang Creative Center (MCC) by expanding access to innovation-focused training, promoting digital literacy, and facilitating inter-business collaboration will significantly enhance the innovation ecosystem. Government support should focus not only on infrastructure but also on fostering a culture of continuous learning and creative experimentation among entrepreneurs.

The private sector and financial institutions also have a pivotal role to play in this ecosystem. The study indicates the need for more accessible and flexible financing mechanisms specifically designed for innovation-driven MSMEs. Tailored funding schemes, such as low-interest loans or technology-based financing, can reduce barriers for MSMEs to pursue bold, creative ventures. Furthermore, fostering stronger networks and partnerships among MSMEs, government agencies, and private sector actors will promote knowledge sharing and collaborative innovation.

Ultimately, MSMEs should prioritize strategies that translate creativity and innovation into tangible competitive advantages. This includes investing in capacity-building programs such as quality management, branding, and digital marketing. The combined efforts of business actors, government institutions, and private stakeholders are essential to cultivating a resilient and innovation-oriented MSME sector capable of contributing to inclusive and sustainable economic growth.

CONCLUSION

This study examined whether competitive advantage mediates the relationship between creativity, innovation culture, and business performance within the MSME ecosystem of Malang City. The results demonstrate that creativity and innovation culture do not exert a direct influence on business performance. Instead, their impact operates entirely through competitive advantage, confirming a full mediation mechanism. These findings indicate that internal

creative and innovative capacities enhance performance only when strategically translated into differentiation or superior market positioning.

Importantly, this result contrasts with prior empirical studies that report direct positive relationships between creativity, innovation, and firm performance. The present study clarifies this discrepancy by showing that internal capabilities alone are insufficient to generate performance outcomes unless they are effectively converted into competitive advantage. This mediation-based explanation provides a more precise understanding of how capability-driven performance actually occurs in MSMEs.

Theoretically, this study advances the Resource-Based View by empirically validating a capability–advantage–performance pathway within an emerging economy context. Unlike previous research that assumes linear effects, this study demonstrates that competitive advantage functions as the critical transformation mechanism linking internal resources to outcomes. By integrating ecosystem-level qualitative insights with structural modeling, the research offers a novel, multi-layered explanation of MSME competitiveness.

Practically, the findings suggest that policy interventions should move beyond encouraging creativity and innovation alone. Greater emphasis should be placed on strategic positioning, branding, digital leverage, and differentiation mechanisms that enable MSMEs to transform innovation into sustained competitive advantage. Ecosystem actors should therefore focus on strengthening the capability-to-advantage conversion process.

Future research may extend this mediation model to other regional ecosystems, employ longitudinal designs to capture dynamic capability development, or incorporate additional moderators such as digital maturity or environmental turbulence. Such research would deepen understanding of sustainable MSME performance under varying competitive conditions.

AUTHOR STATEMENTS

Muhammad Hidayat was responsible for the research conceptualization, design of the methodology, formal analysis, and the initial drafting of the manuscript. **Andi Ririn Oktaviani** contributed to the literature review, data collection process, and interpretation of findings. **Hardianty Askar** was involved in the validation of research instruments, coordination of field data, and proofreading of the manuscript. **Murtianingsih** contributed to the statistical analysis, visualization of data, and assisted in structuring the discussion section. **Lussia Mariesti Andriany** provided critical revisions to the content, supported the theoretical framework development, and ensured adherence to journal submission guidelines. **Widya Dewi Anjaningrum** participated in reviewing the final version, organizing references, and contributed to the final editing and formatting of the manuscript. All authors have read and agreed to the published version of the manuscript.

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