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EFFECT OF GREEN INNOVATION AND DIGITAL TRANSFORMATION ON SOLO RAYA SMEs

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Abstract: This study is motivated by the low awareness among SMEs in Solo Raya regarding the importance of environmental factors and digitalization for firm performance. Although stakeholder pressure and environmental concerns are increasing, few studies have explored how stakeholder pressure, green dynamic capability, green innovation, and digital transformation jointly influence the performance of SMEs, particularly in developing regions like Solo Raya. The aim of this research is to explore the combined impact of these factors on the performance of SMEs in Solo Raya. This research employs a quantitative approach, collecting data through a survey of 131 respondents from various SMEs in Solo Raya. The data was analyzed using Smart PLS 4. The results indicate that stakeholder pressure, green dynamic capability, green innovation, and digital transformation, all have a positive and significant effect on firm performance. In conclusion, although awareness of these critical factors remains low, SMEs in Solo Raya that respond to stakeholder pressure by enhancing their green dynamic capabilities, implementing green innovations, and adopting digital transformation strategies are better positioned to significantly improve their performance. This highlights that integrating environmental sustainability with digitalization can be a key driver of competitive advantage in the region.

Keywords: Stakeholder Pressure, Green Innovation, Digital Transformation, Firm Performance

1. Introduction

Environmental issues in Indonesia are one of the main focuses in implementing SDGs. One of the roles involved in sustainable environmental development is through SMEs (Wicaksono, 2023). SMEs contribute to National GDP by 61%, indicating that SMEs have strong potential to be further developed, so that they can contribute even more to the economy (DJPb, 2023). However, SMEs have a negative impact that accompanies them, namely impacting the environment because most of these companies have not included the adoption of sustainable practices in their processes, strategies or long-term vision (Coelho et al., 2018). There is still little attention to how SMEs manage sustainable innovation (Castillo-Esparza et al., 2024).

In facing global environmental challenges and digitalization demands, SMEs need to adapt to a more sustainable and innovative approach. Stakeholder pressure, originating from the government, consumers, or the wider community, is an important driver for SMEs to switch to more environmentally friendly practices (D. Zhang et al., 2019). This pressure encourages SMEs to adopt green innovation to increase the competitiveness and sustainability of their businesses (Singh et al., 2022).). Furthermore, green dynamic capability refers to a company's ability to manage and adapt to environmental changes through a learning process and developing adaptive green strategies (Hanelt et al., 2021). This capability helps SMEs respond to pressure from various stakeholders and innovate in environmentally friendly practices (Singh et al., 2022).). In the digital era, digital transformation is also a key factor for the success of SMEs (Harebasur, 2023). Digitalization allows SMEs to increase operational efficiency, expand market reach, and strengthen innovation processes, including green innovation

(Mansouri et al., 2022). With the right digital transformation, SMEs can respond more quickly to market changes and demands from stakeholders (Verhoef et al., 2021).
The results of research Budiyanto et al., (2022) in Surakarta City show that waste management is still less effective. This condition is a challenge for SMEs, in the case of plastic food waste it is estimated to contribute 20-30% of waste (Farrukh & Sajjad, 2023). In this way, SMEs must start implementing business sustainability (Domaracká et al., 2023). It is worth mentioning that SMEs must have skills, external involvement, and government support in growing their business (Indah & Risma Deviyati, 2022). However, there is little literature that provides guidance on how to proceed (Singh et al., 2022).
In research (Zhang et al., 2019) and (Xie et al., 2019) this research shows that pressure from stakeholder pressure related to environmental sustainability has a positive effect on company performance. However, in Smulowitz (2020) shows the negative impact of stakeholder pressure on the sustainability practices of SMEs performance. In line with research (S et al., 2020) and (Cheng et al., 2024) showing the negative impact of stakeholders, which results in low adoption of sustainability practices on SMEs performance. Based on the background description above, researchers tried to find the influence of stakeholder pressure, green dynamic capability, green innovation and digital transformation on the performance of SMEs with the research title "Effect of Green Innovation and Digital Transformation on Solo Raya SMEs".
The formulation of the problem in this research is: do stakeholder pressure, green dynamic capability, green innovation, and digital transformation influence the performance of SMEs. The aim of this research is to determine the influence of stakeholder pressure, green dynamic capability, green innovation, and digital transformation on company performance, using the following research schematic diagram of the study.

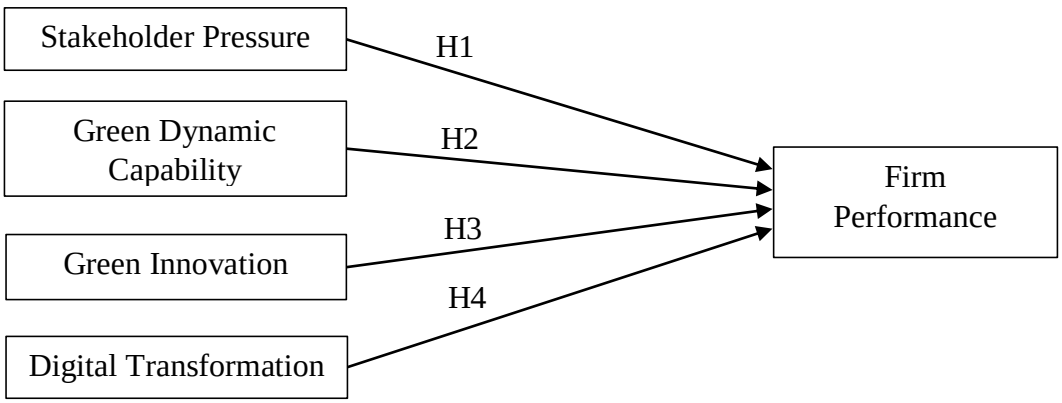

Figure 1: Schematic Diagram of the Study

2. Literature Review

2.1 Stakeholder Theory

Stakeholder theory expressed by Freeman (1994), assumes that company performance is determined by related parties who have an interest. Manage the information needs required by various powerful stakeholders such as shareholders, company employees, consumer investors, regulators, and so on (Indah & Risma Deviyati, 2022). Stakeholder pressure proves that pressure from different stakeholders has its own influence on decisions in adopting sustainability performance (Ruhiyat et al., 2022). The performance of SMEs and their relationships with owners, employees, suppliers, consumers and government is influenced by financial literacy, accounting information systems and information technology (Lubis et al.,

2024). Therefore, SMEs that have open and implied contracts with various stakeholders must be responsible for honoring all contracts (Singh et al., 2022).

2.2 Resource Based View (RBV) Theory

Resource based view (RBV) Theory is an approach that emphasizes the importance of internal resources in creating competitive advantages and improving company performance. The resource-based view, developed by Wernerfelt (1984) and expanded by Barney (1991), identifies that resources that are rare, irreplaceable, and difficult to imitate can be the basis for sustainable competitive advantage. In the context of green innovation, green innovation can be considered a resource that is difficult to imitate and valuable, because it requires special knowledge and environmentally friendly technologies that only a few companies have (Xie et al., 2019).

Effective implementation of green innovation allows companies to achieve higher operational efficiency and a good reputation in the eyes of consumers, which ultimately improves company performance (Nsiah et al., 2022). Research conducted by (Singh et al., 2022) shows that SMEs that have innovation capabilities ultimately improve their sustainability performance. At the same time, green dynamic capabilities enable companies to adapt to environmental changes quickly and effectively, providing the ability to continue to create sustainable competitive advantages (Domaracká et al., 2023).

Meanwhile, digital transformation is also related to RBV because digital technology is a strategic resource that provides a competitive advantage for companies (Verhoef et al., 2021). Digital transformation allows companies to increase efficiency, product and service innovation, which ultimately strengthens business performance (Hanelt et al., 2021).

2.3 Hypothesis Development

Stakeholder Pressure and Firm Performance

Stakeholder pressure positively influences SMEs performance, because this pressure encourages SMEs to improve the quality of products and services in order to meet stakeholder expectations and maintain good business relationships (Reza Juanda et al., 2023). Research result (Analia, 2020) show that stakeholders or the Department of Cooperatives and SMEs have a very large role in improving the performance of SMEs. In line with research. (Anastasia et al., 2020) and (Sari et al., 2022) which show a positive influence on the performance of SMEs.

H1: Stakeholder pressure has a positive effect on SMEs performance

Green Dynamic Capability and Firm Performance

Green dynamic capability positively influences the performance of MSME businesses, can reduce the environmental impact of their business activities, increase resource efficiency, and meet the demands of an increasingly environmentally conscious market (Mansouri et al., 2022). Research (H. Li, 2022) shows that green dynamic capability is positively correlated and has a significant impact on company performance. Research results (Muzaffar et al., 2024) found that green dynamic capability has a significant positive influence on the performance of SMEs. The results of this research (Zehir & Allaham, 2022) show that the adoption of environmentally friendly practices provides a significant competitive advantage and has a positive impact on business performance. In line with research (Isa & Ar Rahmah, 2023); (C. Li et al., 2023); (Liu & Liu, 2024) which also has a positive effect on company performance.

H2: Green dynamic capability has a positive effect on SMEs performance

Green Innovation and Firm Performance

Green innovation has a positive influence on the performance of SMEs, innovation allows SMEs to develop more sustainable products, services and business processes, increase competitiveness and attract customers who increasingly care about the environment (De Marchi et al., 2022). In line with research (Yuha Auliana & Luthfi Alhazami, 2023) and (Liu & Liu, 2024) which shows that green innovation has a significant effect on the performance of SMEs.

H3: Green innovation has a positive effect on SMEs performance.

Digital Transformation and Firm Performance

The implementation of digital transformation positively influences the performance of SMEs, because digital transformation allows SMEs to increase operational efficiency, reach a wider market through online platforms, increase interactions with customers, and gain better insights through data analysis (Schniederjans et al., 2020). In line with research (Verhoef et al., 2021); (Hanelt et al., 2021); (Oubrahim & Sefiani, 2023); (Harebasur, 2023) which shows that digital transformation has a positive effect on the performance of SMEs.

H4: Digital transformation has a positive effect on SMEs performance.

3. Method

This research uses a quantitative approach carried out in the Greater Solo area. The method used is a survey method by distributing questionnaires online via Google Form with a Likert scale of 1-5. The population in this research are SMEs in the Solo Raya area that implement digital transformation and environmentally friendly innovation in their businesses. Meanwhile, the sample in this research will be taken from the population, namely 131 respondents. The sampling technique is non-probability sampling with a purposive sampling method, namely selecting samples using certain criteria or considerations that are relevant to the research objectives.

The data analysis technique in this research uses the SEM-PLS 4 application. As a test tool. Data analysis techniques were carried out using descriptive statistical tests, outer models (convergent validity, discriminant validity and reliability tests), inner models (structural model tests), and hypothesis tests (path coefficient and p-value).

4. Result and Discussion

Descriptive Analysis

Table 1 presents the dermographic data of respondents in this study. From the results displayed in the table, it can be observed that the number of genders who filled out the questionnaire were men (41.2%) and women (58.8%), with the majority having a final education level of high school at 64.1% consisting of owners. and workers at Solo Raya SMEs. Judging from the type of business run, the majority are culinary businesses at 41.2% with an average monthly income of <10 million and 94.7% use digital technology.

Table 1. Respondent Data

Characteristics	Category	Total	Percentage
Gender	Man	54	41,2%
	Woman	77	58,8%
Last education	Junior High School	4	3,1%
	High School/Equivalent	84	64,1%
	Diploma/S1	43	32,8%
Type of business	Fashion	23	17,6%
	Culinary	53	41,2%
	Craft	21	16%
	Beauty	8	6,1%
	Retail	4	3,1%
	Grocery stall	9	6,9%
	Printing	5	3,8%
	Services/rentals	7	5,3%
Income per month	<10 million	68	51,9%
	20-30 million	48	36,6%
	30-60 million	13	9,9%
	>60 million	2	1,5%
Have you used digital technology?	Yes, currently using	124	94,7%
	Yes, But now not using	7	5,3%

Sources: Output Smart-PLS 4.0, 2024

Measurement Model Test

The results of convergent validity and reliability testing show that all items are valid and meet the specified criteria. Table 2 shows that all cross loading, Cronbach's alpha, Rho-A, CR, AVE values are more than 0.7, which means it can be concluded that this research is reliable.

Table 2 Convergent Validity and Reliability

Construct	Item	Cross Loading	Cronbach 's Alpha	Rho-A	CR	AVE
Stakeholder Pressure	SP1	0.938	0.952	0.962	0.965	0.873
	SP2	0.935				
	SP3	0.928				
	SP4	0.936				
Green Dynamic Capability	GDC1	0.859	0.949	0.981	0.960	0.827
	GDC2	0.907				
	GDC3	0.917				
	GDC4	0.930				
	GDC5	0.932				
Green Innovation	GI1	0.954	0.960	0.975	0.969	0.863
	GI2	0.930				
	GI3	0.933				

Construct	Item	Cross Loading	Cronbach 's Alpha	Rho-A	CR	AVE
	GI4	0.886				
	GI5	0.939				
Digital Transformation	DT1	0.949	0.953	0.991	0.965	0.874
	DT2	0.925				
	DT3	0.944				
	DT4	0.920				
Firm Performance	FP1	0.906	0.956	0.958	0.965	0.820
	FP2	0.897				
	FP3	0.869				
	FP4	0.927				
	FP5	0.913				
	FP6	0.920				

Sources: Output Smart-PLS 4.0, 2024

Table 3 presents the results of the discriminant validity test, showing each construct is greater than the correlation between constructs, which indicates that each construct has good discriminant validity. Apart from that, the results of cross loadings show that each indicator has a higher loading on its construct compared to other constructs. Therefore, it can be concluded that the discriminant validity in this model has been fulfilled well, so that the constructs in this research are able to differentiate one another clearly.

Table 3. Discriminant Validity

	DT	FP	GDC	GI	SP
DT	0.935				
FP	-0.388	0.905			
GDC	-0.811	0.483	0.909		
GI	-0.574	0.549	0.532	0.929	
SP	-0.655	0.593	0.574	0.375	0.934

Sources: Output Smart-PLS 4.0, 2024

Structural Model Test

Based on hypothesis testing, it can be seen that 4 hypotheses are significantly supported. Because all statistical t values are greater than 1.96 and p values are smaller than 0.05, it means that all hypotheses have a significant positive effect. Table 4 illustrates that the relationship between the four constructs, namely stakeholder pressure, green dynamic capability, green innovation, and digital transformation, has a significant positive influence on firm performance.

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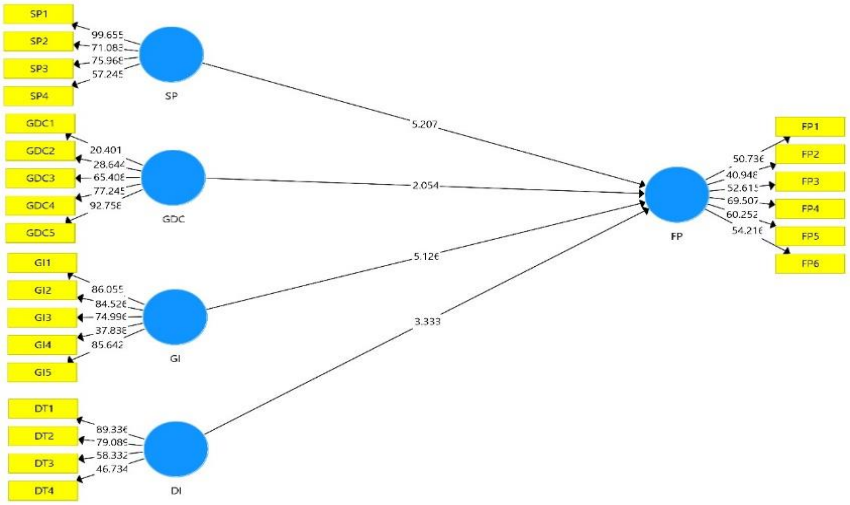

Figure 2: Goodness of Fit Result Model
Sources: Data Analysis

The suitability results of this model are presented in the following table.

Table 4. Structural Model Test

Hypothesis	Original Sample	T Statistics	P-Values	Information
SP -> FP	0.568	5.259	0.000	Supported
GDC -> FP	0.332	2.165	0.030	Supported
GI -> FP	0.453	5.344	0.000	Supported
DT -> FP	0.513	3.421	0.001	Supported

Sources: Output Smart-PLS 4.0, 2024

This research examines the relationship between stakeholder pressure, green dynamic capability, green innovation, digital transformation and firm performance. H1 shows that stakeholder pressure has a significant positive effect on firm performance with a p value of 0.000. This is in line with previous research conducted by (Analia, 2020); (Anastasia et al., 2020); which states that stakeholder pressure has a positive effect on firm performance. H2 shows a p value of 0.030, which shows that green dynamic capability has a significant positive effect on firm performance. This is in line with research conducted by (Muzaffar et al., 2024); (C. Li et al., 2023) which states that green dynamic capability has a positive effect on firm performance. H3 shows that green innovation has a significant positive effect on firm performance with a p value of 0.000. This is in line with research conducted by (Singh et al., 2022); (Yuha Auliana & Luthfi Alhazami, 2023); (Liu & Liu, 2024) which states that green innovation has a positive effect on firm performance. H4 shows that digital transformation has a significant positive effect on firm performance with a p value of 0.001. This is in line with research conducted by (Verhoef et al., 2021); (Hanelt et al., 2021); (Oubrahim & Sefiani, 2023); (Harebasur, 2023) which states that digital transformation has a positive effect on firm performance.

In discussing the findings, this research found that stakeholder pressure, green dynamic capability, green innovation, and digital transformation have a significant effect on the

performance of SMEs. This shows that pressure from stakeholders has an influence on SMEs to adopt sustainability in their businesses by implementing environmentally friendly practices accompanied by implementing digital transformation in their businesses. This means that by implementing the adoption of business sustainability, the performance of SMEs will increase. This emphasizes the importance of green dynamic capability, green innovation and digital transformation in improving the performance of SMEs. Even though pressure from stakeholders encourages the adoption of sustainable and environmentally friendly strategies, SMEs still face challenges in the form of limited resources and technological understanding, support in the form of training and funding is needed so that SMEs can optimize their potential to further develop. The results of this research provide insight into the synergy between external pressures, innovation and digital transformation, as well as opening up opportunities for further study regarding other factors that can influence SMEs performance.

5. Conclusions

This research aims to examine the influence of stakeholder pressure, green dynamic capability, green innovation, and digital transformation on the performance of SMEs in Solo Raya, using the theoretical framework of stakeholder theory and resource-based view (RBV) theory. The results of the analysis show that pressure from stakeholders has a positive and significant influence on the performance of SMEs, meaning that these results support stakeholder theory which emphasizes the importance of stakeholders in determining organizational strategy.

These findings are also consistent with RBV theory, where green dynamic capabilities, green innovation, and digital transformation are proven to be strategic resources that can improve the quality of products produced and improve the performance of SMEs. Thus, SMEs need to manage stakeholder pressure effectively and utilize internal resources such as green capabilities and digital technology to improve their performance. The results of this research are in accordance with the hypothesis that has been formulated, namely that all constructs, stakeholder pressure, green dynamic capability, green innovation, and digital transformation have a positive and significant effect on firm performance.

However, this research has limitations, this research only uses direct influence testing and samples used in the Greater Solo area. Therefore, future research is recommended to explore mediation or moderation effects, as well as expand the coverage area to obtain more comprehensive results.

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