



How to improve market performance through competitive strategy and innovation in entrepreneurial SMEs

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Abstract

Despite the limited resources of small and medium-sized enterprises (SMEs), they can still manage to be competitive and survive in the current environment by implementing competitive strategies that lead to innovation and improve their market performance. The aim of this study is to examine and analyse the effect of business strategy on market performance in Spanish small and medium-sized entrepreneurial enterprises, and the mediating effect of innovation is explored as a solution to business crises. In addition, we analyse the moderating effect that the perceived risk of COVID-19 may have on this relationship, as well as whether the commercialisation capacity of SMEs exerts an impact and improves performance based on innovation. Taking 1,842 Spanish entrepreneurial firms with fewer than 250 employees as a reference and using partial least squares structural equation modelling (PLS-SEM), our study shows that entrepreneurial SMEs that apply a competitive strategy can achieve enhanced innovation. Moreover, this innovation has a direct and positive effect on the market performance of SMEs, and this effect is greater under higher marketing capability. Our findings suggest a heterogeneous effect on the impact of the perceived risk of COVID-19 on the strategy-innovation relationship. In entrepreneurial SMEs that adopt a differentiation strategy, the perceived risk has an enhancing impact, while in entrepreneurial SMEs that follow cost strategies, the effect is negative.

Keywords Competitive strategies · Innovation · Market performance · Perceived risk from COVID-19 · Marketing capability · Entrepreneurial SMEs

Introduction

The modern business environment is constantly changing, and it involves high uncertainty and high competition. Companies and, in particular, small and medium-sized enterprises (SMEs) need to exert great efforts to improve their business

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strategies and, in that way, create a competitive advantage that enables them to survive in the market (Munck et al., 2020). Currently, following a good strategy is necessary to be competitive (Islami et al., 2020). Global pressure requires SMEs to develop competitive strategies and implement innovative plans for sustainable development (Kharub et al., 2022).

The literature has found differences in business competitiveness that depend on characteristics of firm size, such as ownership structure, available resources, degree of flexibility or even decision-making processes (Lamberti & Noci, 2012; Russo & Tencati, 2009). Some studies mention SME characteristics that limit their strategic and innovative capacity by resulting in a more conservative approach, a tendency to avoid risks and a lack of proactivity (Dess et al., 2011; Martin & Lumpkin, 2003). In addition, the economic effects of the COVID-19 pandemic have a greater impact on SMEs than on large firms (Bank of Spain, 2021).

However, the smaller size of SMEs is not always a disadvantage. Evidence shows that SMEs have informal strategies, highly flexible structures (Hudson et al., 2001; Qian & Li, 2003), and less bureaucracy, thus enabling them to adapt quickly and agilely (Baumann-Pauly et al., 2013). Lu and Beamish (2001) stated that despite limited resources and capabilities, SMEs that implement an effective strategy for managing their internationalisation process through alliances with local partners can manage to overcome knowledge deficiencies in the host country.

Therefore, the literature suggests that although SMEs have limited resources and capabilities that may hinder the implementation of competitive strategies and constrain their innovative capacity, they are also able to leverage other types of resources to act with greater agility and speed and thereby remain competitive (Zahra, 2005). Indeed, SMEs have a highly reactive and "firefighting" mentality, and this strategic flexibility allows them to achieve better performance (Bashir, 2023). Similarly, Smith and Lewis (2011) showed that SMEs are able to respond quickly to change, especially in regard to reacting to an obvious crisis, which directly affects the company's performance.

Given this complex situation, we highlight the ability to implement competitive strategies that lead to greater innovation in SMEs as one of the most important factors affecting business performance (Cooper, 2000; El Chaarani et al., 2022; Hult et al., 2004; Hurley & Hult, 1998; Porter, 1990). Extant studies also specifically refer to market performance as a particularly important measure of business success (Alam et al., 2013; Homburg & Jensen, 2007; Ingenbleek et al., 2013; Jabbour et al., 2015; Pinheiro et al., 2021), which is a state that implies that the firm has achieved higher market shares and revenues from its product and service sales than its competitors with respect to certain metrics, such as reaction speed to market opportunities, customer satisfaction and loyalty, the quality of services, the effectiveness of innovation and new customer acquisition (Afriyie et al., 2019; Homburg & Jensen, 2007).

However, previous studies that have examined the firm-level strategic capacity for obtaining the performance necessary to compete in the market have primarily focused on large listed companies (e.g., Arsawan et al., 2022; Block, 2012; Gómez-Mejía et al., 2014; Hsu & Chang, 2011), and the number of studies that examine Spanish SMEs is still very low (Al-Hanakta et al., 2021).

In this sense, there is some ambiguity in the findings of previous research that links competitive strategy and business success by considering the role of innovation as applied to SMEs (Rosli & Sidek, 2013). For example, some authors have established a positive relationship (Allocca & Kessler, 2006; El Chaarani et al., 2022; Gudmunson et al., 2003; Price et al., 2013), while others have found no direct relationship (Kharub et al., 2022).

Considering these premises, we pose the following questions: Do entrepreneurial SMEs that implement a better competitive strategy and have a higher innovative capacity than their peers achieve better market performance? How does the perceived degree of COVID-19 risk influence innovation? Finally, does the marketability of SMEs influence the relationship between innovation and market performance?

Based on these gaps, the present research has several objectives: first, it is aimed at testing the impact that competitive strategies specifically have on the market performance of entrepreneurial SMEs; second, it is aimed at examining the mediating role of innovation as a function of SME strategy as well as the market performance obtained; and finally, its goal is to analyse the moderating role that innovation has on the market performance of SMEs. Finally, we analyse the moderating role that the perceived risk of COVID-19 and the commercial capacity of SMEs may have in obtaining higher market performance.

To achieve these objectives, the paper is organised as follows. The first section reviews the theoretical background on competitive strategy, innovation, and market performance in entrepreneurial SMEs, which enables the presentation of the research hypotheses. In this section, additionally analyses are conducted on the role of the perceived risk of COVID-19 and that of marketing capability in the above relationships. The methodology used in this study, the database analysed, the measurement of the variables and the analysis techniques carried out are then described in detail. The results obtained from these analyses are then presented and discussed. Finally, the conclusions, the main contributions of the study and the implications for SME entrepreneurs are evaluated. Finally, limitations and future lines of research are discussed.

Theoretical background and hypotheses

Competitive strategy and market performance in entrepreneurial SMEs

The field of strategic management has generated a large body of research that is focused on identifying and understanding strategic orientations at the firm level both within and across industries. Strategic orientation refers to firm adaptation to its external environment and means of competing (Hajar, 2015). The best known and most widely used typologies in research, as well as the most criticised (Parnell, 2006; Wan & Bullard, 2009), are those proposed by Porter (1980) and Miles and Snow (1978). While Porter (1980) established cost leadership, differentiation, and market niche as generic strategies and sources of competitive advantage, Miles and Snow (1978) identified four ideal types of firms, namely, prospectors, analysers, defenders and reactionaries, which depend on how these firms deal with problems. The

literature, regardless of whether it uses one typology or the other, generally considers the impact of strategic orientation on innovation as positive. Hajar (2015), Manurung (2009) and Moore (2005) used Miles and Snow's typology, while recent work by Agyapong et al. (2016) and Oyedijo (2012) resulted in similar findings using Porter's (1980) typology. In our study, we use Porter's typology based on its applicability and viability, as well as the support it has received in the literature (i.e., Bowman & Ambrosini, 1997; Campbell-Hunt, 2000; Miller & Dess, 1993). Following Porter (1980), the cost leadership strategy is not based on offering the lowest price but rather on having the lowest cost and thus increasing the profit margin potential. Differentiation is a strategy based on offering an exclusive product, either by design, branding, technology features or customer service, while a focus strategy is aimed at satisfying the needs of a specific group of customers. In this paper, the first two strategies are analysed, understanding that segmentation can be considered a "simple approach" in which a group of customers whose needs can be satisfied by a single company is selected within the market (Yamin et al., 1997).

Although Porter (1990) suggested that competitive strategies are the engine through which firms strive to outperform their rivals, the strategic orientation of small and medium-sized firms has received little attention from researchers, and further research is needed on the postulates and outcomes of such orientations in different organisational contexts, on market performance, and on understanding the firm's more market- and customer-driven outcomes (Gök & Peker, 2017).

Furthermore, although experts have postulated that small and medium-sized enterprises must develop and follow at least one strategy to survive in a changing business environment, there are studies in the literature that do not find any relationship between competitive strategies and firm performance (Kharub et al., 2022). There are even authors who justify the need for SMEs to implement temporary innovative business models to survive a crisis (Clauss et al., 2022).

Moreover, the empirical results from previous research report different findings. According to Agyapong (2016), firms that apply competitive strategies are more likely to achieve competitive advantage and higher performance than firms that do not, and they further add that this is achieved through innovation. Similarly, Oyedijo (2012) found a significant impact of strategic orientation on market performance. However, studies such as Rosli (2012) show that Porter's (1980) generic strategies, although useful, are not sufficient to ensure the competitiveness of SMEs. In addition, SMEs have their own limitations in their search to achieve superior performance (Lin et al., 2014), a limited level of innovation through information technology (Dibrell et al., 2008) and limited resources (AlQershi et al., 2022).

Considering competitive strategies independently, we highlight the findings of Baum et al. (2001). Based on these authors' empirical findings, we can see that differentiation strategies are positively correlated with firm growth, while low-cost strategies are negatively correlated. In contrast, authors such as Islami et al. (2020) have empirically shown that the impact of cost strategy on performance is positive, although these researchers all demonstrate that the differentiation strategy provides higher performance. A possible explanation for this can be found in the argument presented by Talke and Hultink (2010), which claims that organisations that follow product differentiation strategies can better adjust their strategic resources and

thereby achieve better performance. Meanwhile, authors such as Yanuarti and Murwatiningsih (2019) have studied the direct effect of competitive strategy on market performance, first describing strategy as a function of entrepreneurial orientation and then concluding that such an effect exists. Therefore, companies that achieve competitive advantages through the implementation of a competitive strategy improve their market performance.

We consider the literature to be limited and inconsistent, so it is necessary to empirically analyse the effect of competitive strategy, whether differentiation or cost leadership strategies, on performance (Hughes & Morgan, 2008); thus, we propose the following two hypotheses:

H1a. A differentiation strategy has a positive and direct influence on market performance in entrepreneurial SMEs.

H1b. A cost leadership strategy has a positive and direct influence on market performance in entrepreneurial SMEs.

The mediating role of innovation in entrepreneurial SMEs

Innovation has traditionally been viewed as an activity that leads to competitive advantage and superior profitability (Roberts & Amit, 2003). Studies such as Farida and Setiawan (2022) have confirmed that if innovation did not achieve performance, there would be no possibility for reinvesting the economic benefits achieved through innovation, which is very important to the survival of SMEs. Innovation is the application of new ideas that add value to a firm's products, processes, organisational and marketing systems (Weerawardena, 2003). The OECD (2007) states that innovation is the implementation of a new or significantly improved product (goods and services), process, marketing method or organisational method in business practices, organisations, or workplaces, thus establishing four types of innovations. In this paper, we focus on the first two, which are the best known perspectives on innovation in the innovation literature (Johnes & Davies, 2000; Otero-Neira et al., 2009), who understood these as technological innovations, are opposed to the last two, which are considered nontechnological innovations. Moreover, innovation as the application of new ideas, especially in product and process innovation, is the most important form for SMEs (Ismanu & Kusmintarti, 2019).

Although the relationship between competitive strategies and innovation has been widely discussed in the literature, confirming the effect that innovation has on the relationship between business strategy and market performance is considered to be necessary (Hajar, 2015).

Support for our mediation hypothesis requires several types of evidence. First, there must be a positive relationship between competitive strategy and innovation. Manurung (2009), in his study on the airline industry, found a positive and significant relationship between strategic orientation and innovation. Similarly, Frambach et al. (2003) proposed that cost leadership and differentiation strategies have a direct and positive influence on product innovation. Fathali (2016) analysed this same

relationship in Iran's automotive industry, concluding that Porter's competitive strategies had a positive and significant influence on business innovation.

Both the differentiation strategy and the cost leadership strategy are related to innovation. The differentiation strategy involves anticipating customer needs and behaviours to incorporate one or more new features into a product or to develop a completely new product (Crema et al., 2014). Similarly, Porter (1980) established a possible link between cost leadership strategy and process innovation. To gain a cost leadership advantage, a company needs to carry out various innovative activities and focus on cost reduction (Frohwein & Hansjürgens, 2005). In this way, innovation is conducive to economies of scale, cost reduction and gaining market share (Qin, 2007). Hilman and Kaliappen (2014) concluded that a cost leadership strategy significantly influences process innovation, which, in turn, influences organisational performance. Finally, Bayraktar et al. (2017) showed that competitive strategies, including both cost leadership and differentiation strategies, can lead to innovation and, in turn, increase market performance.

Second, there must be a positive link between innovation and market performance (Chesbrough, 2020; Eggers, 2020; Kraus et al., 2020; Wenzel et al., 2020). This link may form because the impact of innovation on market performance involves strategically vital decisions for modern business organisations (Gök & Peker, 2017) and has special significance for companies with limited resources, such as SMEs (Tutar et al., 2015). Studies show that innovation has a positive and significant influence on business growth (Hoang Nam, 2014) and SME performance (Acquaah & Agyapong, 2015; Aksoy, 2017; Azar & Ciabuschi, 2017; Rogo et al., 2014; Saunila, 2017; Sok et al., 2013). However, Lam and Harker (2015) did not consider market performance to be a dimension of firm performance and rather viewed marketing as a separate concept and an integrated indicator within firm performance.

Gök and Peker (2017) analysed the effect of innovation on these two different facets of firm performance (market performance and financial performance), and their results indicated a direct positive relationship between innovation and market performance but a negative relationship between innovation and financial performance. However, market performance was so high in this study that it reversed this negative effect by achieving an overall positive influence through its suppression effect. This finding represents an important contribution to our understanding of the mechanism underlying innovation's influence on financial performance and has generated great interest among experts in analysing the role of innovation on market performance (Chandy & Tellis, 2000). Nevertheless, the literature that examines this dynamic is much scarcer (Aksoy, 2017).

In this line of thinking, studies such as Tutar et al. (2015) have demonstrated a relationship between innovativeness and market performance. In addition, Afriyie et al. (2019) concluded that innovation has a positive effect on market performance and stated that business leaders should recognise market performance and determine its contribution to organisational performance. O'Cass and Weerawardena (2009) stated that superior market performance appears to be strongly linked to innovation intensity. Greater innovativeness enables firms to continuously create breakthroughs in the offerings they bring to market (Kim & Mauborgne, 1997). Even if innovation does not involve market performance, it could indicate that an SME's limited

resources have been exhausted and that these SMEs have become uncompetitive (Farida & Setiawan, 2022).

Taking into account the fact that both competitive differentiation strategy and cost leadership strategy influence innovation and, in turn, that they have an effect on firm performance (Fathali, 2016; Frambach et al., 2003; Manurung, 2009) and that market performance is more critical for smaller firms in the field of innovation (Gök & Peker, 2017), we hypothesise the following:

H2a. Innovation in entrepreneurial SMEs mediates the positive relationship between differentiation strategy and market performance.

H2b. Innovation in entrepreneurial SMEs mediates the positive relationship between cost leadership strategy and consumer service market performance.

The moderating role of the perceived risk from COVID-19

When accounting for the factors that influence innovation, the literature does not exclusively focus on competitive strategies (e.g., cost leadership and differentiation strategy) but rather also emphasises other cognitive elements, such as subjective perceptions (Busenitz, 1999). Perceptions are formed and emerge in the mind and are representations of how the external environment is captured through an individual's senses and cognition (Arafat & Saleem, 2017). Without ignoring their strong subjective basis, such representations also tend to involve an objective dimension that emanates from more objective environmental and informational cues (e.g., the recent COVID-19 pandemic). Hence, these perceptions affect how people understand a situation and play a role in affecting their intention to innovate (cf., Busenitz, 1999). In particular, our model assumes that the risk perceived by entrepreneurial SMEs during the recent COVID-19 pandemic may have a heterogeneous moderating effect on the relationship between competitive strategies (cost leadership and differentiation strategy) and innovation.

As noted, a strategy based on cost leadership drives entrepreneurial SMEs to develop greater innovation. However, this influence is conditioned by the perception of risk that these firms acquire when capturing information regarding their environment, as this may affect the firm's ability to innovate. Specifically, perceived risk in innovation involves assessing the risk expectations of such an act (Monsen & Urbig, 2009), which may result in negative emotions potentially leading to the perception of creating new products or services as risky (Nabi & Liñán, 2013). This may occur because risk perception is considered a central component of innovation and plays a crucial role in the entrepreneurial decision-making process (Elston & Audretsch, 2011). Innovation involves a set of projected outcomes that are difficult to achieve and therefore adds risk to this decision. Thus, perceived risk, which is conceived as the assessment of the risks inherent in undertaking an action (Nabi & Liñán, 2013), is likely to be the basis for the decision to further investments in the development of novel products and services. Therefore, entrepreneurial SMEs that are based on a cost leadership strategy and that, during the COVID-19 crisis, developed high levels of perceived risk may have served as a disincentive to creativity and the

development of new ideas and innovations in products and processes (Faqih, 2022). This is facilitated by firms' opting to pursue cost reduction through job cuts and lower turnover rates.

In contrast, unlike the cost leadership strategy, which can cause firms to perceive risk in innovation, the differentiation strategy can help reduce such perceived risk in innovation (Nienaber & Schewe, 2014). Firms that are driven by a differentiation strategy tend to be proactive and less negatively biased by the influence of an adverse context (Crema et al., 2014). Moreover, differentiation strategies provide these firms with new market opportunities for the development of new products and services (Crema et al., 2014). When firms base their competitive strategy on differentiation, they more strongly express the need to explore novel ideas and innovate as a means of adapting to new market situations (Frambach et al., 2003).

Therefore, we suggest that when the perceived risk of the effects of COVID-19 increases, SMEs that base their strategy on cost leadership can reduce their innovation level. However, the presence of higher levels of perceived risk may encourage greater innovation in those SMEs that follow a differentiation-based strategy, leading us to propose the following hypotheses:

H3a. The perceived risk of COVID-19 moderates the relationship between differentiation strategies and innovation in entrepreneurial SMEs such that a differentiation strategy imparts a more positive effect on innovation in entrepreneurial SMEs when the level of COVID-19 risk management increases.

H3b. The perceived risk of COVID-19 moderates the relationship between cost leadership strategies and innovation in SMEs such that cost leadership strategy imparts a less positive effect on innovation in entrepreneurial SMEs when the level of COVID-19 risk management increases.

The moderating role of marketing capability

The capacity of a marketing company is a relevant factor that can moderate the relationship between innovation and market performance. In this sense, capability theorists seek to explain how different combinations of resources and capabilities can be developed and deployed in response to dynamic business environments (Teece et al., 1997). Capabilities are seen as 'know-how' deployment activities, which can be categorized into different functional areas, including marketing and innovation (Ngo & O'Cass, 2012). Based on the dynamic capabilities theory (Teece et al., 1997), it is argued that higher market performance can be achieved through the integration of those resources and capabilities that are associated with specific functional areas within firms (e.g., innovation and marketing) that provide greater complementarity. In this regard, dynamic capabilities theory (Teece et al., 1997) underscores the importance of the interaction between a firm's 'know-what' knowledge resources and its complementary 'know-how' deployment capabilities (e.g., Bolade, 2022). This suggests that a firm's marketing capability and innovation may interact to enable the firm to better align its resource deployments with its market environment than those of its rivals (Ngo & O'Cass, 2012). There are two main reasons

for expecting such interaction. First, the literature describes marketing capability as involving important market-related mechanisms through which firms can implement their innovations based on better market knowledge and thus ensure the capacity to generate greater levels of market performance (Ngo & O’Cass, 2012). Second, since innovation and marketing capability complement each other in ways that generate economic revenues and each of these can be seen as an individual source of competitive advantage, the interaction between innovation and marketing capability has the characteristic of "asset interconnectedness" (Teece, 2018). This creates an ecosystem of differentiating resources and capabilities that makes it particularly difficult for competitors to disentangle the source of an observed market performance (Gotteland et al., 2020). For these reasons, we expect the following:

H4. Marketing capability moderates the relationship between innovation in entrepreneurial SMEs and market performance such that innovation in entrepreneurial SMEs has a more positive effect on market performance under higher levels of marketing capability.

Figure 1 summarises the hypotheses proposed in this paper. The combination of these hypotheses forms the theoretical model that is tested in subsequent sections.

Material and methods

Sampling procedure and data collection

We randomly selected entrepreneurial SMEs operating in Spain from the INE (2021) database. The selection framework utilized was the SABI database through Faedpyme (2021). The reason for the selection was convenience. Spanish SMEs

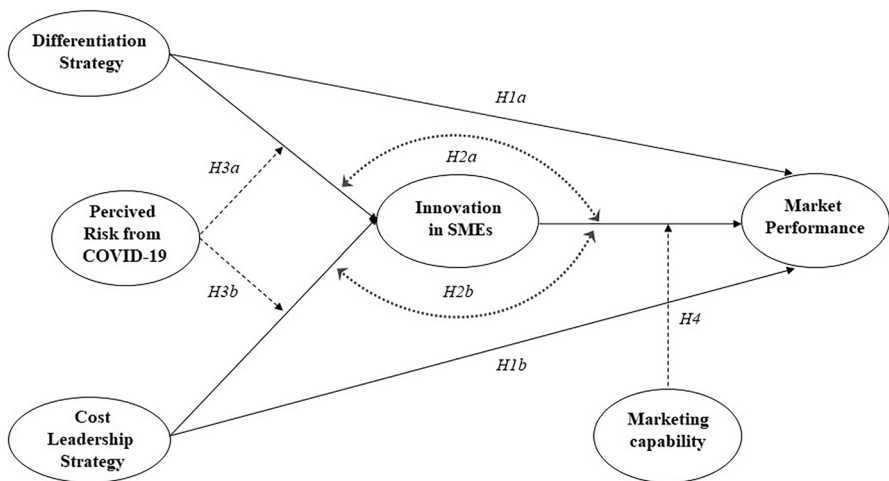


Fig. 1 Theoretical model

are very important to the country's economy, and their number exceeds 99% of the total pool of Spanish companies (Spanish Ministry of Industry, Commerce and Tourism, 2022). Spain is a relevant country in the European Union (it has the fourth largest economy in the European Union in terms of GDP, ICEX 2022), and given this relevance, Spain is suitable for empirical study. Additionally, according to a recent report on improving competitiveness that was prepared by Faedpyme (2023), Spanish SMEs consider their achievements in terms of customer and employee satisfaction, product quality and responsiveness to market changes to be the most favourable among enterprise types. However, profitability, sales speed and growth are still areas that call for improvement. This prompts the need to analyse Spanish entrepreneurial SMEs.

The sampling for this study was conducted by stratifying the population according to the aims of the study and the information available about the population structure.

The overall sample design is based on the principles of stratified sampling. The selection within each stratum was made by simple random sampling, using up to a total of 2000 questionnaires. Subsequently, any incomplete questionnaires were eliminated. A total of 1,842 completed surveys were retained and used for further analysis (response rate: 29.48%, sampling error: 2.9%, for a confidence level of 95% and the least favourable situation for $p=q=0.5$).

The largest group of participating firms was taken from the services sector (35%), followed by industry (33%), retail (19%), and construction (14%). Additionally, most firms were small, with fewer than 50 employees (52%), followed by micro-SMEs with 6–9 employees (35%), medium SMEs with 50–249 employees (12%), and those without employees (1%). According to company type, 29.5% were nonfamily SMEs and 70.5% were family SMEs.

Because the research design was cross-sectional and involved various self-report measures, common method variance and social desirability bias were potential concerns, and several recommended procedural remedies were used to address them (cf. Podsakoff et al., 2003, 2012). The findings of the marker test (e.g., Khosravi et al., 2020) showed that method variance was not a concern. Specifically, a marker item (i.e., the gender of the CEO of the company) was unrelated to any of our targeted constructs. The mean correlation between the marker item and each of the study variables was 0.03, which is below the 0.05 threshold (Rönkkö & Ylitalo, 2011). Moreover, there were no meaningful changes in parameter estimates in a model in which the marker was related to the study variables. Thus, common method variance was unlikely to be a concern in our data.

Measurement instrument

Following the relevant literature, the study questionnaire was designed by selecting variables and the links among them. In the first section, the competitive strategy of SMEs was measured through two indicators. The second section of the survey relates to the measurement of innovation in firm product, process, and management dimensions, which used a total of six indicators. The third section highlights the moderating variables, perceived risks, and marketing capability. The responses for each of these

sections were measured using a 5-point Likert scale (1 = strongly disagree, 5 = strongly agree). Finally, the fourth section is based on a collection of descriptive information regarding the SMEs, such as firm size (number of employees), sector (industry, retail, construction, type of company (family or nonfamily) and sales achieved.

Variables

Dependent variables

Market performance is the main endogenous variable. It is a specific measure that considers the more market and customer-oriented performance of the company (Gök & Peker, 2017). For its measurement, indicators previously used by other authors (e.g., Delaney & Huselid, 1996; Pekovic & Vogt, 2021), namely customer satisfaction, rapid adaptation to markets and market growth, were validated. The dependent variable *innovation* is a construct consisting of specific indicators measuring product/service, process, and management innovation (Weerawardena, 2003). The indicators used in this construct have been validated by Burdon et al. (2015), Cegarra-Navarro et al. (2016), Harel et al. (2021), Lichtenthaler (2017) and Oke et al. (2007).

Independent variables

With respect to the independent variables, the differentiation strategy variable is a construct that measures by means of an indicator the production of the product/service under quality criteria. In this way, SMEs that follow this strategy try to obtain a competitive advantage over their competitors, based on offering exclusivity (Porter, 1980). The variable cost leadership strategy is the second construct that measures through an indicator how the company is more efficient in the internal process (e.g., Bayraktar et al., 2017; Hilman & Kaliappen, 2014) and thus achieves a competitive advantage based on lower costs (Porter, 1980).

Moderators

Following authors such as Ganzach et al. (2008), Frias et al. (2020) and Hoogendoorn et al. (2019), the *perceived risk variable from COVID-19* is defined. This construct is measured through an indicator that captures risk management associated with the COVID-19 pandemic. Secondly, the variable *marketing capacity* is measured through an indicator that assesses the commercial adaptive capacity of the SME (Gotteland et al., 2020; Ngo & O' Cass, 2012).

Table 1 shows the variables and indicators according to the literature.

Data analysis

To test our hypotheses, structural equation modelling (SEM) based on partial least squares (PLS) and Smart PLS 3.3.3 (Ringle et al., 2015) was used. PLS-SEM is a robust statistical technique that allows for mediation and moderation (Hair et al.,

Table 1 Description of the variables, indicators and authors

Variable	Indicator	Definition	References
Cost Leadership Strategy	CS1	Efficiency of internal processes	(Qin, 2007; Frohwein & Hansjürgens, 2005; Hilman & Kaliappen, 2014; Qin, 2007; Bayraktar et al., 2017)
Differentiation Strategy	DS1	Production of the product/provision of the service under quality criteria	(Hilman & Kaliappen, 2014; Bayraktar et al., 2017)
Innovation in SMEs	IS1	Product innovation assesses changes or improvements in existing products/services	(Oke et al., 2007; Burdon et al., 2015; Cegarra-Navarro et al., 2016; Lichtenthaler, 2017; Harel et al., 2021)
	IS2	Launch of new products on the market	
	IS3	Changes or improvements in the production process	
	IS4	Acquisition of new equipment	
	IS5	Changes or improvements in the organisation	
	IS6	Changes or improvements in purchasing or procurement	
Market Performance	MP1	Customer satisfaction	(Clark, 2000; Bocquet et al., 2013; Rasoulzadeh et al., 2013; Saeidi et al., 2015; Sridhar & Mehta, 2018; Pekovic & Vogt, 2021)
	MP2	Rapid adaptation to market changes	
	MP3	Business growth	(Delaney & Huselid, 1996; Christensen et al., 2003; Pipheropoulos & Scase, 2009; Richard et al., 2009; Vaccaro et al., 2010; Börjesson & Löfsten, 2012; Szczygielski et al., 2017; Pinheiro et al., 2021)
Perceived Risk from COVID-19	PR1	Risk management associated with the COVID-19 pandemic	(Ganzach et al., 2008; Frias et al., 2020; Hoogendoorn et al., 2019)
Marketing Capability	MCI	Marketing capacity to adapt to the market	(Ngo & O' Cass, 2012; Gotteland et al., 2020)

2017). A power analysis developed using G*Power 3 (Faul et al., 2007) for the regression with the greatest number of independent variables in our model (i.e., 5) yielded a power ranging from 97.4% to 99.99%. Thus, the sample of this study is sufficient to test the predicted relationships, as it allows.

Medium effect sizes to be detected (Cohen, 1988) without incurring Type II errors. Moreover, it ensures that the R² and significant path coefficients obtained from our regression analyses differ from zero.

Finally, our PLS analysis used 5,000 subsamples to generate standard errors and bootstrap t-statistics with $n - 1$ degrees of freedom to evaluate the statistical significance of the path coefficients (cf., Hair et al., 2017).

Results

Evaluation of the measurement model

Item reliability was satisfactory, as the values were above the recommended 0.707 threshold (Hair et al., 2017). The internal consistencies, composite reliability indices and Cronbach alphas also all exceeded the 0.70 cut-off (Hair et al., 2017). Convergent validity was supported, as the average variance extracted (AVE) for the constructs was above 0.50 (Hair et al., 2017, Table 2). Additionally, discriminant validity was supported, with the AVE exceeding the square correlations between the composites in all cases (Hair et al., 2017, Table 3). Moreover, the HTMT indexes were below 0.85, as recommended (Henseler et al., 2015, Hair et al., 2018, see Table 2). Finally, VIF values for the complete model range between 1.00 and 2.15, far below the 5.0 cut-off (Hair et al., 2017, see Table 2), so path coefficients do not suffer from multicollinearity problems.

Evaluation of the structural model for the overall sample

H1a was supported since, in an unmediated model, differentiation strategy was positively associated with market performance ($\beta = 0.326$, $p < 0.001$; see Fig. 2a). Cost leadership strategy was also significantly related to market performance ($\beta = 0.349$, $p < 0.001$; H1b; see Fig. 2b). As anticipated, innovation in SMEs was also positively linked to market performance ($\beta = 0.062$, $p < 0.05$; see Fig. 2c). Finally, the mediation effect of innovation in entrepreneurial SMEs on the positive relationship between differentiation strategy and market performance was significant (indirect effect = 0.006 $p < 0.05$; see Fig. 2c) supporting H2a. Similarly, innovation in entrepreneurial SMEs significantly mediates the relationship between cost leadership strategy and market performance (indirect effect = 0.008 $p < 0.05$; see Fig. 2c), supporting H2b. Although the size of both individual betas was substantial, the mediation linked to innovation in SMEs in the relationship between differentiation strategy and cost leadership strategy has a small effect ($f^2 = 0.021$ and $f^2 = 0.022$ respectively; Table 4).

The findings also provided support for H3a and H3b, on the moderating role of COVID-19 risk management in the relationship between differentiation strategy/

Table 2 Item loadings, variance inflation factor, construct reliability

Construct	Item/First order construct	Loading	VIF	Construct reliability			AVE
				Cronbach's Alpha	Dillon-Goldstein (ρ_c)	Dijkstra-Henseler (ρ_A)	
Cost Leadership Strategy (CS)				1	1	1	1
	CS1	1	1				
Differentiation Strategy (DS)				1	1	1	1
	DS1	1	1				
Innovation in SMEs (IS)				0.86	0.87	0.90	0.59
	IS1	0.80	2.14				
	IS2	0.74	1.84				
	IS3	0.83	2.13				
	IS4	0.72	1.35				
	IS5	0.82	2.15				
	IS6	0.77	1.95				
Market Performance (MP)				0.71	0.74	0.84	0.63
	MP1	0.83	1.37				
	MP2	0.84	1.61				
	MP3	0.71	1.34				
Perceived Risk from COVID-19 (PR)				1	1	1	1
	PR1	1	1				
Marketing Capability (MC)				1	1	1	1
	MC1	1	1				

VIF variance inflation factor, AVE average variance extracted

cost leadership strategy and innovation in entrepreneurial SMEs. The results revealed that, after mean-centring the independent variables and the moderator (Aiken & West, 1991), the resulting interaction term was positive and significant in the case of differentiation strategy ($\beta = 0.068$, $p < 0.05$; Fig. 2c), and negative in the case of cost leadership strategy ($\beta = -0.051$, $p < 0.05$; Fig. 2c). The graph resulting from plotting high versus low-risk management COVID-19 regression lines (+ 1SD and -1SD, Aiken & West, 1991) shows, for the case of differentiation strategy, that the positive impact of innovation in entrepreneurial SMEs was stronger in high (the slope is more pronounced) than in low COVID-19 risk management conditions (Fig. 3). Thus, H3a can be confirmed.

Table 3 Descriptive statistics, correlation matrix and discriminant validity

Constructs	Mean	SD	1	2	3	4	5	6
1. Cost Leadership Strategy	3.61	0.80	1	0.62 [0.48, 0.76]	0.20 [0.16, 0.25]	0.55 [0.43, 0.67]	-0.04 [-0.01, -0.08]	0.15 [0.09, 0.21]
2. Differentiation Strategy	3.73	0.76	0.62**	1	0.18 [0.11, 0.26]	0.54 [0.41, 0.68]	-0.05 [-0.02, 0.08]	0.14 [0.05, 0.23]
3. Innovation in SMEs	2.12	1.41	0.21*	0.20*	0.77	0.21 [0.15, 0.28]	-0.19 [-0.07, -0.31]	0.69 [0.52, 0.86]
4. Market Performance	3.75	0.82	0.65**	0.62**	0.27**	0.79	-0.09 [-0.03, -0.15]	0.17 [0.08, 0.27]
5. Perceived Risk from COVID-19	3.01	1.47	0.04	0.21**	0.20*	0.11*	1	-0.11 [-0.06, -0.17]
6. Marketing Capability	1.97	1.35	0.15*	0.05	0.64**	0.20*	0.12*	1

Bold values on the diagonal are the square roots of the AVE. Off-diagonal elements below the diagonal are correlations between the constructs. Off-diagonal elements in italics and above the diagonal are the HTMTs and their 95% confidence intervals (CI). As the HTMTs are below 0.85 and CIs do not include 1, there is discriminant validity (Hair et al., 2017)

SD standard deviation

* $p < 0.05$; ** $p < 0.01$ or better (two-tailed test)

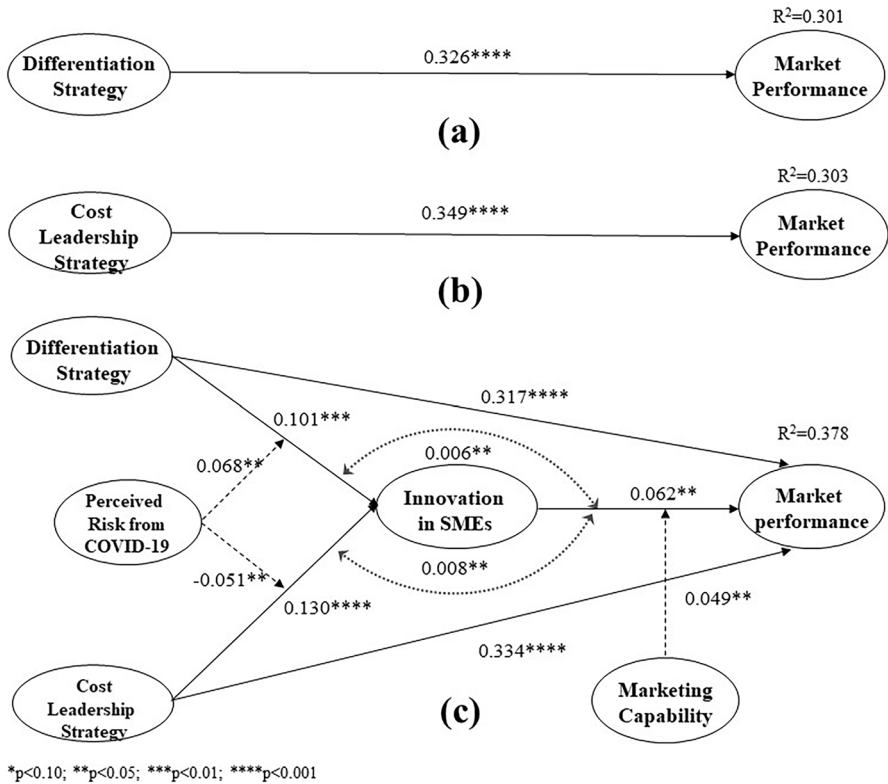


Fig. 2 Results model

In contrast, in the case of cost leadership strategy, the graph resulting from plotting high versus low COVID-19 risk management regression lines shows that the positive impact of innovation in SMEs was weaker in high than in low COVID-19 risk management conditions (Fig. 4). H3b can therefore be confirmed.

We proceeded similarly in the analysis of H4, and as predicted, the relationship between innovation in SMEs and market performance was strengthened by commercial adaptive capacity ($\beta=0.049$, $p<0.05$; Fig. 2c). In Fig. 5, we also plot high versus low commercial adaptive capacity regression lines (+1 and -1 standard deviation from the mean), showing the positive relationship between innovation in SMEs and market performance is stronger (the slope is more pronounced) when commercial adaptive capacity is high rather than low.

Finally, Table 5 summarizes the assumptions made in the research model, including the standardized beta, t-value, p-value and confidence intervals.

Table 4 Mediation effect size of innovation in entrepreneurial SMEs

Indirect effect	Variance explained			Size of the mediation effect (f^2)
	R ² included	R ² excluded	R ² variance explained	
Cost leadership strategy → Innovation in SMEs → Market performance	0.318	0.303	0.015	0.022 (small effect)
Differentiation strategy → Innovation in SMEs → Market performance	0.315	0.301	0.014	0.021 (small effect)

$f^2 = (R^2 \text{ included} - R^2 \text{ excluded}) / (1 - R^2 \text{ included})$; effect sizes of $f^2 \geq 0.02$, ≥ 0.15 , and ≥ 0.35 are small, medium, and large, respectively (Cohen, 1988)

Discussion

The competitive strategies defined by Porter (1990) are utilized by firms in an effort to outperform their rivals. In the case of SMEs, this dynamic, particularly in contexts of uncertainty, has received little attention from researchers. Nevertheless, global pressure requires small and medium-sized enterprises to develop competitive strategies aimed at ensuring success (Snowdon & Stonehouse, 2006; Verbeeten & Boons, 2009).

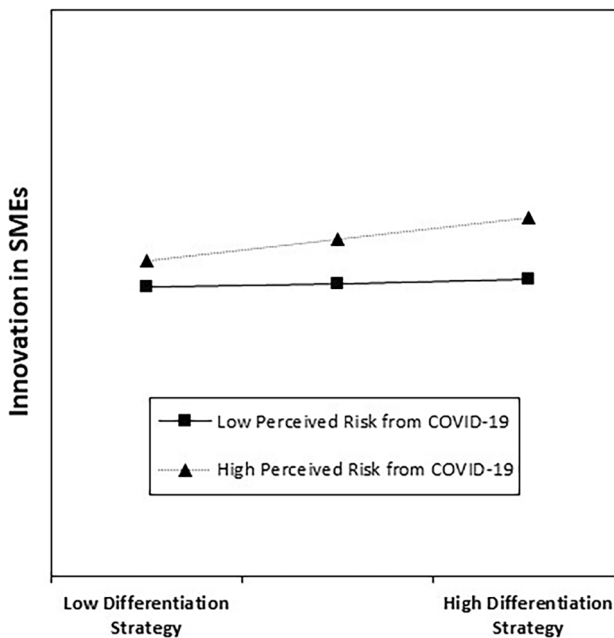


Fig. 3 Interactive effect of differentiation strategy and perceived risk from COVID-19 on innovation in entrepreneurial SMEs

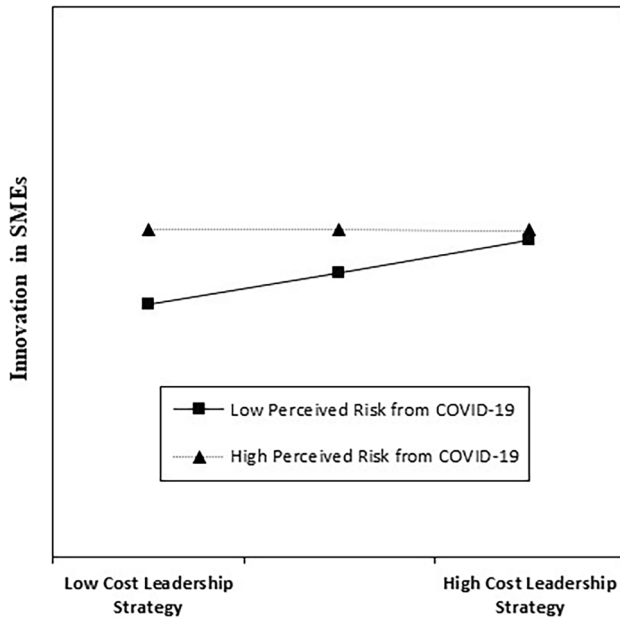


Fig. 4 Interactive effect of cost leadership strategy and perceived risk from COVID-19 on innovation in entrepreneurial SMEs

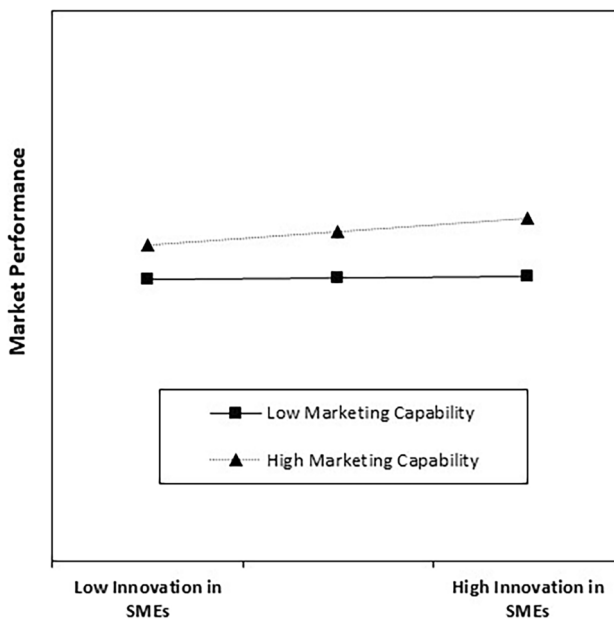


Fig. 5 Interactive effect of innovation in entrepreneurial SMEs and marketing capability on market performance

Table 5 Structural path analysis: hypothesis tests

Hypothesis	Relationship	Std. Beta	t-value	p-value	LL CI	UL CI	Decision
H1a	Differentiation Strategy → Market Performance	0.326	12.414	0.000	0.271	0.371	Supported
H1b	Cost Leadership Strategy → Market Performance	0.349	13.753	0.000	0.288	0.383	Supported
H2a	Differentiation Strategy → Innovation in SMEs → Market Performance	0.006	2.104	0.047	0.001	0.013	Supported
H2b	Cost Leadership Strategy → Innovation in SMEs → Market Performance	0.008	2.135	0.045	0.002	0.018	Supported
H3a	Perceived Risk from Covid19 X Differentiation Strategy	0.068	2.176	0.043	0.033	0.104	Supported
H3b	Perceived Risk from Covid19 X Cost Leadership Strategy	-0.051	2.421	0.016	-0.085	-0.017	Supported
H4	Marketing Capability X Innovation in SMEs	0.049	2.363	0.019	0.011	0.087	Supported

LL CI lower limit confidence interval, *UL CI* upper limit confidence interval

The present study addresses this research gap by providing empirical knowledge on how the competitive strategy that is followed by SMEs in turbulent times affects SME performance, while considering the impact of innovation in this relationship. For this reason, a series of hypotheses are established to pursue the specific study objectives that have been described.

First, we consider the relationship between competitive strategies and market performance. In doing so, Hypotheses 1a and 1b, which capture the direct and significant relationship between differentiation and cost leadership and market performance, respectively, are proposed and confirmed. We follow the assumptions of Agyapong et al. (2016), who found that firms that pursue differentiation and cost leadership strategies are more likely to achieve market-oriented competitive advantage than firms that do not, thus resulting in higher market performance. In contrast to the findings of authors such as Baum et al. (2001) and Islami et al. (2020), who identified the differentiation strategy as the most appropriate strategy for success, according to our findings, both competitive strategies lead to business success.

Second, to understand the complex relationship between competitive strategies (cost leadership vs. differentiation) and market performance, the mediating role of innovation in entrepreneurial SMEs is analysed in our study. Hypotheses 2a and 2b are thus proposed. The results show that for both strategies, the presence of greater innovation in SMEs helps to explain this relationship. In this sense, there are precedents in the literature that examines the effect of innovation on firm performance (Amit & Zott, 2012; Roberts & Amit, 2003). Authors such as Febrianti and Herbert (2022) argue that innovation is a very important factor for improving SME business performance. However, the study of this relationship specifically in entrepreneurial SMEs has not yet been addressed in depth, and the previous research that accounts for firm size reports different results (Onufrey & Bergek, 2021). Through our empirical study, we confirm these findings and demonstrate that innovation in SMEs has a significant mediating effect on the link between competitive strategy (cost leadership vs. differentiation) and market performance. Therefore, to use innovation to achieve market performance, SMEs particularly need to achieve marketing capability; otherwise, market performance is not achieved.

Third, cognitive elements, such as the perceived risk during the recent COVID-19 pandemic and the subsequent adaptive capacity, are also analysed in this study. To study the moderation of the first variable, Hypotheses 3a and 3b are posed, which depend on the competitive strategy followed and its direct influence on innovation. The results show a heterogeneous moderating effect of SMEs' competitive strategies on their relationship with innovation. Thus, while for entrepreneurial SMEs that opt for a differentiation strategy, the perceived risk of COVID-19 exerts a positive leverage effect, for SMEs that base their strategy on cost leadership, it has a negative effect. This finding is in line with the very nature of SMEs' competitive strategies. Thus, while a differentiation strategy is focused on new products and business opportunities, a cost leadership strategy tends to be inwards-looking and reduces a firm's innovative orientation (Faqih, 2022). By analysing this moderating mechanism, our study sheds light on the different effects of each of these strategies in driving innovation in SMEs.

Finally, in the study of the second moderating variable, namely, marketing capability, Hypothesis 4 is proposed regarding the possible existence of a positive moderating effect of marketing capability on the relationship between SME innovation and market performance. In this way, we empirically confirm the premises established in dynamic capabilities theory (Teece et al., 1997), which examines how combinations of resources and capabilities can be articulated in complex dynamic environments (Teece et al., 1997), such as that experienced during the recent COVID-19 pandemic. In this way, the presence of complementary resources and capabilities within SMEs, such as innovation and marketing, have enabled the enhancement of higher levels of marketing performance.

Therefore, a differentiating ecosystem that makes it more complex for competitors to determine the source of a firm's competitive advantage has been created (Gotteland et al., 2020).

Conclusions

In this paper, a series of research questions are proposed to allow us to clarify how the competitive strategies of entrepreneurial SMEs during the pandemic affected their innovative capacity and, in turn, their performance in the market. Concrete information is provided on how the implementation of competitive strategy affects SMEs, and empirical research is applied to address this underexplored topic.

Theoretical implications

To explain the generation of market performance in SMEs in times of crisis, it is crucial to understand the role played by competitive strategies (Miller & Dess, 1993). In this respect, the dichotomous distinction between cost leadership and differentiation strategy is an important issue. Although both types of strategies are known to inspire the development of higher market performance via the competitive advantages achieved thereby, research is still needed to verify the specific contribution of each type of competitive strategy (Hughes & Morgan, 2008). By analysing the mechanisms that may help to explain this relationship, our study is one of the few to shed light on the different mechanisms (moderation and mediation) by which competitive strategy (cost leadership and differentiation strategy) drives higher levels of market performance in entrepreneurial SMEs.

We have made progress regarding our literature review, considering that there is a significant gap in those studies focusing on SMEs (Al-Hanakta et al., 2021), and there is a need to examine whether the theories that have been developed for large firms are also applicable to SMEs (De Arsawan et al., 2022).

The findings of Agyapong (2016) and Oyedijo (2012) are confirmed as being applicable to SMEs, and they reveal how firms that follow a clear competitive strategy are more likely to achieve a competitive advantage through innovation than firms that do not, thus resulting in higher performance. In addition, based on the

mediating role of innovation in our model, we provide further insight into previous studies that only captured the influence of innovation on performance (i.e., Acquaah & Agyapong, 2015; Aksoy, 2017).

Practical implications

The findings of this study are of interest to SME entrepreneurs for making decisions that can improve their market performance in uncertain environments, such as that of the recent pandemic.

Based on the results obtained, the following implications are suggested for SME entrepreneurs to consider in decision-making. First, our findings suggest that entrepreneurs should have a clear strategic orientation enabling them to make innovation decisions, as such an orientation is a source of competitive advantage (Agyapong et al., 2016; Rubio-Andrés, et. al., 2015). We show that competitive strategies have a positive impact on market performance (Oyedijo, 2012; Yanuarti & Murwatiningsih, 2019); thus, choosing between differentiation or cost leadership strategies is important for SME entrepreneurs seeking to improve their business growth, their customer satisfaction and their rapid market adaptation.

Second, according to our findings, SME entrepreneurs should consider innovation as a key variable for improving market performance, regardless of the competitive strategy adopted. Our study confirms the findings that show the need for superior market performance when the level of innovation intensity is high (O’Cass & Weerawardena, 2009). We confirm the claim that such market performance is necessary to survive in complex times of economic recession, and that firms should rely on innovation to improve their performance (Aghion et al., 2005; Pece et al., 2015). We therefore posit that SME entrepreneurs should focus on innovation in times of crisis.

Third, we highlight the importance of the ways that entrepreneurs perceive the risk of COVID-19 and how such perceptions differentially affect the strategy-innovation relationship. For example, we find that SME entrepreneurs who base their strategy on differentiation can manage perceived risk as treating it as an opportunity for innovation, so our recommendation is to continue along these lines. In contrast, under low-cost strategies, the level of perceived risk has led entrepreneurs to make decisions that have undermined the development of their innovations, which is counterproductive. As Faqih (2022) suggested, risk acts as a disincentive to both creativity and the development of new product and process ideas. Therefore, entrepreneurs need to be able to recognise this perception of risk in a more favourable light and continue to invest in process innovation.

Finally, we highlight the role of marketing capability in the relationship between innovation and SME market performance. Following Ngo and O’Cass (2012), we know that firms with superior market knowledge can generate higher returns, so our empirical study confirms this premise, and we recommend that SME entrepreneurs strive to improve their marketing capabilities due to the particular circumstances of entrepreneurial SMEs, which have a greater lack of resources and management skills than large firms (Lee et al., 2016).

Limitations and further research directions

The study is not without limitations. The first is the use of a questionnaire to obtain empirical information by surveying SME entrepreneurs. Although commonly used in social research (Nejati et al., 2017; Rubio-Andrés et al., 2022), this method has limitations arising from its use of self-diagnosis and personal opinion (Ramos-González et al., 2022).

Second, our empirical study was conducted in Spain, so it would be of interest to extend it to a European or Latin American scale, where SMEs are the engine of national economies.

Our findings suggest a positive relationship among competitive strategy, innovation and performance, so we suggest new questions for future research. These questions include whether these strategies are useful in the new environment referred to as the new normal? Some authors, such as Clauss et al. (2022), consider the temporary innovative business model necessary only for addressing the economic crisis, so we question whether such strategies are valid only for surviving the COVID-19 crisis.

Through our study, we show that the higher that the level of perceived risk of COVID-19 by SME entrepreneurs is, the greater the impact of a differentiation strategy on innovation due to the decision making of such entrepreneurs. This finding also suggests that future research should examine whether SMEs with differentiation strategies feel more pressure to innovate than SMEs with cost leadership strategies.

In addition, it would be useful to continue to conduct empirical studies along these lines to confirm these hypotheses by implementing the same measures in other samples and extending the models to include additional variables such as those incorporated in our study, namely, strategic orientation and innovation. We also propose incorporating the measure of the impact of perceived risks other than COVID-19, such as the economic situation, political uncertainty or environmental problems.

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Declarations

Conflict of interest The authors declare that they have no conflict of interest.

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