
Strategic Capabilities and Muslim Entrepreneurial Behavior: The Mediating Role of Competitive Advantage on MSME Performance

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ABSTRACT

This study examines the effects of product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of Sharia-based MSMEs, with competitive advantage serving as a mediating variable within the Resource-Based View (RBV) framework. A quantitative explanatory approach was employed using a census of 153 fashion-sector MSMEs. Data was collected through Likert-scale questionnaires and analyzed using Partial Least Squares Structural Equation Modeling (PLS-SEM). The results indicate that product innovation and Muslim entrepreneurial behavior have a positive and significant effect on MSME performance, while digital marketing does not show a significant direct effect. Competitive advantage positively influences performance but only mediates the relationship between Muslim entrepreneurial behavior and performance; it does not mediate the effects of product innovation and digital marketing. These findings suggest that Muslim entrepreneurial behavior functions as an intangible strategic resource that builds Sharia-based reputational capital and enhances firm performance. This study extends the RBV framework within the Islamic economics context by highlighting the strategic role of Islamic values in shaping MSME capabilities and performance.

Keywords: Competitive Advantage, Islamic Economics, Muslim Entrepreneurial Behavior, Sharia-Based MSME Performance, Strategic Capabilities.

1. INTRODUCTION

Micro, Small, and Medium Enterprises (MSMEs) have an important role in economic development because they are able to create jobs, encourage innovation, and support inclusive economic growth. In many developing countries, including Indonesia, MSMEs are the backbone of the national economy. However, MSMEs also operate in a business environment characterized by rapid change, market volatility, and limited resources (Barragan and Becker 2024; Mukhtar, Nasreen, and Khalid 2023). In these conditions, the ability of MSME actors to develop strategic capabilities is an important factor in maintaining business performance and business sustainability (Komalasari et al. 2024).

Although the number of MSMEs continues to increase, the quantitative growth is not always followed by an improvement in the quality of performance. Many MSMEs still face challenges in building sustainable competitiveness due to product homogeneity, limited innovation, and changes in consumer behavior which are increasingly influenced by the development of digital technology. In the context of MSMEs based on Islamic values, these challenges become more complex because business performance is not only measured by economic indicators such as income, assets, and labor growth, but also by the conformity of business practices with ethical and sharia principles. Research shows that Islamic entrepreneurship orientation that includes business and spiritual dimensions can contribute to improving business performance (Raza et al. 2023; Setiawati, Wediawati, and Heriberta 2021; Suginam et al. 2025).

In an increasingly competitive business environment, strategic capabilities are an important factor that allows MSMEs to create added value and maintain a competitive position in the market. Strategic capability refers to the organization's ability to utilize internal resources and competencies to respond effectively to changes in the business environment. Among various forms of strategic capabilities, product innovation and digital marketing are often associated with improved business performance. The ability to innovate allows companies to create product differentiation and strengthen market positions, which ultimately improves business performance (Kamalrulzaman et al. 2021; Otache 2024; Soewarno, Tjahjadi, and PERMATANADIA 2020). Meanwhile, digital marketing capabilities allow MSMEs to expand their market reach and increase customer engagement through the use of digital technology (Hardaningtyas and Sudarmiatin 2024; Ofori-Amanfo, Akonsi, and Agyapong 2022; Umboh and Aryanto 2023).

Based on the Resource-Based View (RBV) perspective, organizational performance is influenced by the company's ability to utilize resources that are valuable, scarce, difficult to replicate, and not easily replaceable. Ployhart (2021) emphasizing that the heterogeneity of internal resources is the main factor that explains the differences in performance between companies. Within this framework, product innovation and digital marketing can be seen as strategic capabilities that allow MSMEs to build a competitive advantage. Barragan & Becker (2024) Demonstrates that digital onboarding does not automatically improve performance without being supported by an organization's ability to manage and integrate resources. Therefore, competitive advantage is an important mechanism that transforms internal capabilities into superior business performance. A number of studies have also shown that competitive advantage often acts as a mediator between innovation capabilities and business performance (Gunawan and Ongkowijoyo 2025; Soewarno et al. 2020).

However, in the context of MSMEs oriented towards Islamic values, strategic resources include not only technological and managerial capabilities, but also ethical and religious values that are reflected in entrepreneurial behavior. Islamic entrepreneurial orientation emphasizes the principles of honesty, trust, and spiritual orientation in business activities (Raza et al. 2023). Research shows that an entrepreneurial orientation based on Islamic values can increase business legitimacy, strengthen relationships with stakeholders, and support the improvement of business performance (Rahmawati et al. 2024; Suginam et al. 2025). In the perspective of RBV, such religious values can be viewed as an intangible resource that has the potential to create a sustained competitive advantage.

Although the literature on innovation and digital marketing capabilities in improving the performance of MSMEs continues to grow, research that integrates strategic capabilities with entrepreneurial behavior based on religious values is still relatively limited. Most previous research focused more on technological and managerial capabilities in explaining the performance of MSMEs (Komalasari et al. 2024; Otache 2024; Umboh and Aryanto 2023). In addition, studies that place Muslim entrepreneurial behavior as a strategic resource that can shape competitive advantage and influence business performance are still limited. This condition shows that the mechanism of the relationship between strategic capabilities, entrepreneurial behavior based on Islamic values, and the performance of MSMEs still requires a more comprehensive empirical explanation.

This research contributes to the development of sharia economics literature by explaining how Muslim entrepreneurial behavior plays a role in improving the performance of MSMEs. This research integrates Islamic entrepreneurial values with business capabilities represented through product innovation and digital marketing in explaining the performance of MSMEs. In addition, this study also places competitive advantage as a mechanism that bridges the relationship between business capabilities, Muslim entrepreneurial behavior, and MSME performance. Thus, this study provides an empirical perspective on how the integration between Islamic entrepreneurial values and modern business capabilities can strengthen competitiveness and improve the performance of MSMEs in the framework of the sharia

economy. Based on this framework, this study aims to analyze the influence of product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values with competitive advantage as a mediating variable.

2. METHOD

Resource-Based View

Resource-Based View (RBV), which is rooted in thinking Wernerfelt (1984) and formalized by Barney (1991), explains that sustainable competitive advantage comes from the ownership and management of valuable, scarce, hard-to-replicate, and irreplaceable resources (VRIN). This perspective emphasizes that the difference in performance between companies is determined by the heterogeneity of internal resources as well as the organization's ability to optimize them to create value (Seriki 2020; Uyanık 2023).

In the framework of sharia economics, the concept of "value" in RBV is not only interpreted as economic value, but also includes moral and social dimensions that are in line with the principles of Maqasid al-Shariah, namely maintaining religion (ḥifẓ al-dīn), soul (ḥifẓ al-nafs), intellect (ḥifẓ al-'aql), offspring (ḥifẓ al-nasl), and property (ḥifẓ al-māl). Thus, resources that are valuable in an Islamic perspective are those that not only generate financial benefits but also support benefits (maslahah) and social sustainability. Values such as trust, ṣidq (honesty), justice ('adl), and social responsibility can be understood as intangible (non-physical) strategic resources that strengthen market legitimacy and trust. When these values are internalized in entrepreneurial behavior, they have the potential to meet the characteristics of VRIN because they are inherent in individuals and difficult for competitors to imitate (Sheikh and Hussain 2024). In the context of MSMEs based on Islamic values, this ethical dimension is part of strategic capital that supports business sustainability.

RBV also emphasizes that resources only have an impact on performance if they are converted through effective organizational capabilities (Mansour et al. 2022). Therefore, halal and value-added product innovation, transparent and ethical digital marketing, and Muslim entrepreneurial behavior can be positioned as strategic capabilities that transform Islamic value-based resources into competitive advantages. In line with the logic of RBV, competitive advantage acts as a mechanism that bridges strategic capabilities and improves the performance of MSMEs (Citraresmi et al. 2021; Keskin et al. 2021). Thus, in this study, RBV is used as a theoretical basis to explain how the strategic capabilities and entrepreneurial behavior of Muslims, which are in line with the principles of Maqasid al-Shariah, can create competitive advantages and improve the performance of MSMEs within the framework of the sharia economy.

MSME Performance in Sharia Economic Perspective

MSME performance is a multidimensional concept that includes financial and non-financial dimensions. The literature shows that comprehensive performance evaluation needs to integrate financial indicators with operational, governance, and adaptability to digital transformation (Jacobs and Kabaso 2025; Kyshakevych et al. 2024). In addition, the dimensions of sustainability and business governance are increasingly recognized as an integral part of the performance assessment of MSMEs (Jones et al. 2023; Kassem and Trenz 2020; Santoso et al. 2023).

In the perspective of sharia economics, performance is not only measured by growth and profitability, but also by the extent to which business activities are aligned with the principles of Maqasid al-Shariah and generate benefits. Maqasid-based studies emphasize that economic achievements need to be balanced with the values of justice, sustainability, and halal asset management (Mahyudin and Rosman 2022; Tarique et al. 2020). Thus, the performance of MSMEs based on Islamic values reflects the integration between economic achievement and moral responsibility in business activities (Sheikh and Hussain 2024). Based on this framework, the performance of MSMEs in this study is positioned as a multidimensional outcome influenced by the strategic capabilities and entrepreneurial behavior of Muslims, both directly and through

the formation of competitive advantage.

Product Innovation and MSME Performance

In the perspective of the Resource-Based View (RBV), product innovation is positioned as a knowledge-based strategic capability that has the potential to create a competitive advantage when it is valuable and difficult to replicate. As an intangible capability, innovation allows MSMEs to develop new products, improve quality, and adjust product characteristics to market dynamics, thereby strengthening differentiation and competitive position.

Empirically, the positive relationship between product innovation and MSME performance has been widely documented. Ali et al., (2020) shows that product innovation capabilities have a significant effect on the financial performance of MSMEs. Similar findings were reported by Loo (2021), Pranowo et al., (2022), and Thy (2024), which emphasizes that innovation capabilities increase competitiveness and have an impact on sales growth and profitability.

In the context of MSMEs based on Islamic values, product innovation is not only directed at creating economic value, but also at conformity with halal principles and benefits. Innovative products that are in line with sharia values have the potential to increase consumer confidence and strengthen market legitimacy. Thus, product innovation can be understood as a strategic capability that encourages the performance of MSMEs both through economic differentiation and inherent ethical values. Based on the theoretical arguments and empirical evidence, the following hypotheses are formulated:

H1: Product innovation has a positive effect on the performance of MSMEs based on Islamic values.

Digital Marketing and MSME Performance

Digital marketing is a strategic capability that allows MSMEs to leverage digital technology, social media, and online platforms to create value and expand market reach. In the perspective of the Resource-Based View (RBV), this capability is understood as part of the company's internal resources and capabilities that can produce a competitive advantage if it is valuable, rare, difficult to replicate, and not easily replaceable (Abdurrasyid and Praswati 2023; Cho et al. 2025; Keskin et al. 2021). Digital based marketing capabilities such as market sensing, branding, and digital distribution channel management capabilities have been proven to contribute to improving marketing performance and MSME business performance (Chinakidzwa and Phiri 2020; Oduro and Mensah-Williams 2023; Ofori-Amanfo et al. 2022). In the context of MSMEs, limited resources make the development of digital marketing capabilities an important instrument to increase market visibility, build customer relationships, and strengthen a competitive position. RBV emphasized that when digital marketing capabilities are effectively organized and integrated with other internal resources, these capabilities can be a source of sustainable competitive advantage and have an impact on business performance (Cho et al. 2025; Wahid, Janwari, and Jubaedah 2023).

In MSMEs based on Islamic values, digital marketing practices are not only oriented towards market effectiveness, but must also reflect the principles of honesty, transparency, and social responsibility. These ethical values can strengthen business trust and reputation, thereby increasing the potential for converting digital capabilities into superior performance. Thus, digital marketing can be positioned as a strategic resource that creates economic value as well as ethical value within the framework of the sharia economy. Based on these theoretical arguments, the following hypotheses are formulated:

H2: Digital marketing has a positive effect on the performance of MSMEs based on Islamic values.

Perspective Muslim Entrepreneurial Behavior and MSME Performance

Muslim entrepreneurial behavior integrates innovative, proactive, and risk-taking dimensions with Islamic values such as *ṣidq*, trust, and social responsibility. In the sharia economy, this orientation is not only strategic but also ethical, because it shapes the pattern of

decision-making and business governance (Raza et al. 2023; Riyoko and Mufid 2023). Empirically, entrepreneurial orientation (EO) has been proven to have a positive effect on the performance of MSMEs (Nuvriasari et al. 2020; Taan et al. 2023). In an Islamic value-based context, religiosity strengthens the relationship between EO and performance (Sefnedi 2023), while integrating Islamic values increases competitiveness and business sustainability (Riyoko and Mufid 2023).

In the perspective of RBV, Muslim entrepreneurial behavior can be positioned as an intangible strategic resource that meets the characteristics of VRIN because it is culturally inherent and difficult to replicate. The literature on Islamic Work Ethics (IWE) shows that Islamic work ethics improve performance through trust, motivation, and a positive work climate (Abdelwahed et al. 2024; Badar et al. 2023). In addition, competitive advantage often mediates the relationship between entrepreneurial orientation and MSME performance (Kiyabo and Isaga 2020; Nuvriasari et al. 2020), shows that Islamic values can be translated into differentiation and business reputation. Within the framework of *maqāsid al-sharī'ah*, performance is not only measured by profitability, but also by social benefit and sustainability. Thus, Muslim entrepreneurial behavior is a strategic resource that encourages economic performance as well as sharia compliance.

H3: Muslim entrepreneurial behavior has a positive effect on the performance of MSMEs based on Islamic values.

Competitive Advantage and MSME Performance

From the perspective of RBV, competitive advantage is the result of MSMEs' ability to manage valuable, rare, elusive, and irreplaceable resources and capabilities (VRIN), resulting in superior competitive positions and superior performance. The difference in performance between MSMEs, thus, is determined by the extent to which internal resources are successfully converted into competitive advantages. Empirically, competitive advantage has been proven to have a positive effect on the performance of MSMEs. Kiyabo & Isaga (2020) shows that internal capabilities-based excellence improves the performance of small businesses, while Ratnawati et al., (2021) dan Setini et al., (2023) emphasizing that differentiation and service quality as a form of competitive advantage encourage growth and profitability. These findings are reinforced by Gunawan & Ongkowijoyo (2025) which places competitive advantage as the main determinant of MSME performance in a competitive environment.

In the context of MSMEs based on Islamic values, competitive advantage also comes from ethical reputation and sharia compliance. Values such as *ṣidq*, trust, and justice build trust and social legitimacy that impact the sustainability and performance of the business (Raza et al. 2023; Suginam et al. 2025). Thus, competitive advantage in the sharia economy reflects the integration between strategic capabilities and moral values as intangible resources that strengthen the performance of MSMEs. Based on these arguments, a hypothesis is formulated:

H4: Competitive advantage has a positive effect on the performance of MSMEs based on Islamic values.

The Role of Mediation of Competitive Advantage

In the Resource-Based View perspective, internal resources and capabilities do not directly improve performance, but must first be converted into valuable and hard-to-replicate competitive advantages (Barney 1991; Seriki 2020). Thus, competitive advantage functions as a strategic mechanism that bridges the company's capabilities with the performance of MSMEs. Studies have shown that innovation capabilities improve performance through the formation of competitive advantage, both through product differentiation and increased added value for customers (Alshahrani, Yaqub, and Alabdali 2024; Rhee and Stephens 2020; Soewarno et al. 2020). In the digital context, digital marketing capabilities also strengthen the competitive position before it has an impact on performance, so that competitive advantage acts as a crucial mediating variable (Erlany et al. 2023; Huddin 2025; Otache 2024).

In the Islamic economy, competitive advantage is not only built through innovation and technology, but also through ethical values such as honesty, trust, and social responsibility.

Muslim entrepreneurial behavior results in reputation, trust, and moral legitimacy that become intangible resources of strategic value. Based on RBV's logic, reputation and trust are assets that strengthen competitive advantage and encourage MSME performance in a sustainable manner (Alshahrani et al. 2024; Han, Zhou, and Lu 2022). Thus, within the framework of the Islamic economy, competitive advantage is positioned as a mediation mechanism that explains how product innovation, digital marketing, and Muslim entrepreneurial behavior translate into improving the performance of MSMEs based on Islamic values. Based on these arguments, the following hypothesis is formulated:

H5: Competitive advantage is able to mediate the influence of product innovation on the performance of MSMEs based on Islamic values.

H6: Competitive advantage is able to mediate the influence of digital marketing on the performance of MSMEs based on Islamic values.

H7: Competitive advantage is able to mediate the influence of Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values

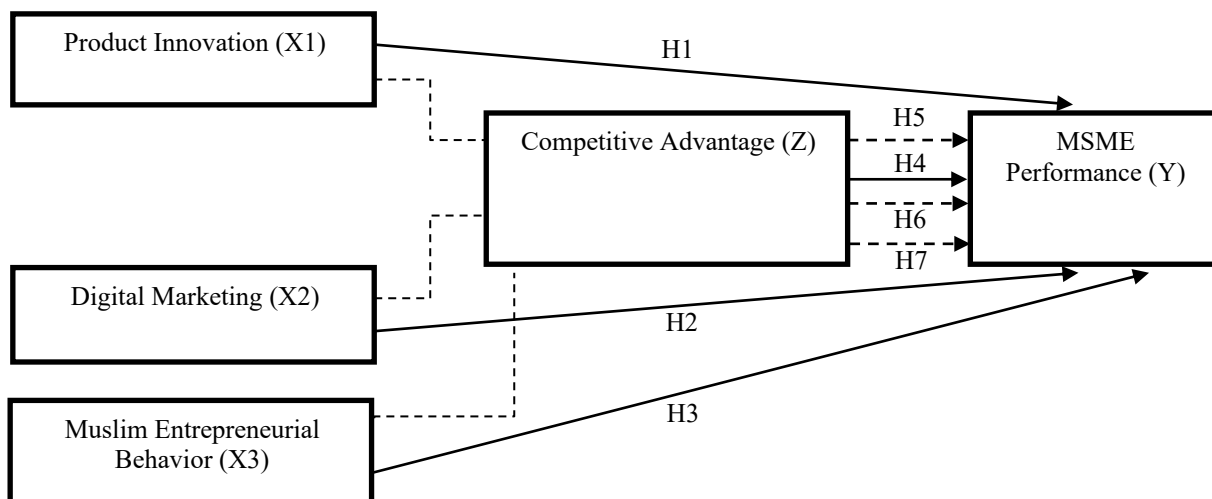


Figure 1. Frame of Mind

3. RESULT AND DISCUSSION

This study uses an explanatory quantitative approach to examine the influence of product innovation, digital marketing, and Muslim entrepreneurial behavior on the competitive advantage and performance of MSMEs based on Islamic values. The research population is all MSMEs in the fashion sector in the Senggol Market, Parepare City as many as 153 units. Because the population is relatively small and clearly identified, this study uses census techniques (total population study), so that the entire population is used as respondents. This approach enhances internal validity in a limited population context, with generalizations limited to the population framework being studied. Primary data were collected through a Likert scale questionnaire of 1–5. Data analysis was carried out using Partial Least Squares Structural Equation Modeling (PLS-SEM) with the help of SmartPLS. This approach was chosen because it is prediction-oriented, able to handle structural models involving mediating variables, and is suitable for relatively limited sample sizes and data distributions that are not necessarily normal (Hair et al. 2021; Legate et al. 2021). Evaluation was carried out on measurement models and structural models to test the validity, reliability, and relationships between constructs.

This section analyzes the influence of product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values with competitive advantage as a mediating variable. The analysis was carried out using PLS-SEM to test the direct and indirect influences, as well as the mediating role of competitive advantage.

Outer and Inner Assessment Model Results

The evaluation of the measurement model was carried out to ensure that the research construct of product innovation, digital marketing, Muslim entrepreneurial behavior, competitive advantage, and the performance of MSMEs based on Islamic values has met the validity and reliability before the testing of the structural model. In the PLS-SEM approach, the assessment of the reflective measurement model refers to Chin (1998) yaitu indikator valid jika loading factor $\geq 0,60$, konstruk reliabel jika composite reliability $\geq 0,70$ dan Cronbach's alpha $\geq 0,60$, serta validitas konvergen terpenuhi jika AVE $\geq 0,50$.

The results in Table 1 show that the entire construct has an outer loading value above the required minimum limit. Product innovation and digital marketing have high indicator loading, while Muslim entrepreneurial behavior, MSME performance based on Islamic values, and competitive advantage also show adequate loading even though some indicators are close to the minimum limit. All constructs also have an AVE value above 0.50, so that the convergent validity is fulfilled because each construct can explain more than half of the variance of its indicators.

Reliability tests using Cronbach's alpha and composite reliability showed that all variables had Cronbach's alpha above 0.60 and composite reliability above 0.70. Thus, the indicators in this study have good internal consistency and acceptable construct reliability according to the standard (Chin 1998).

Table 1. Measurement Model Calculation

Variables	Items	Outer Loading	Cronbach's Alpha	Rho_C	AVE
Product Innovation	PI1	0.829	0.791	0.876	0.703
	PI2	0.862			
	PI3	0.823			
Digital marketing	DM3	0.803	0.684	0.858	0.752
	DM4	0.927			
Muslim Entrepreneurial Behavior	MEB1	0.866	0.828	0.885	0.660
	MEB2	0.851			
	MEB3	0.847			
	MEB4	0.671			
MSME Performance	MP1	0.732	0.760	0.848	0.582
	MP2	0.704			
	MP3	0.830			
	MP4	0.781			
Competitive Advantage	CA1	0.858	0.658	0.792	0.562
	CA2	0.678			
	CA3	0.699			

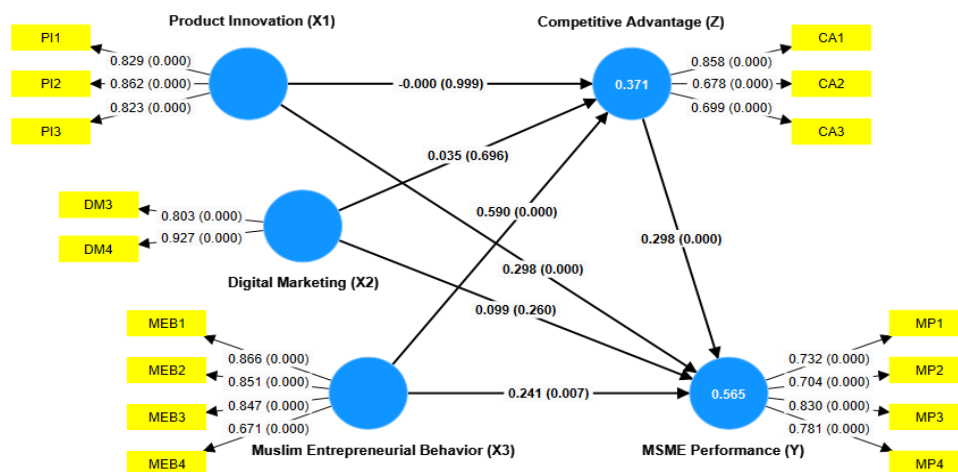


Figure 2. Measurement Model Test

The validity of the discriminator was then evaluated using two approaches, namely the Fornell–Larcker criteria. Based on the Fornell–Larcker criteria in Table 2, the square root value of AVE in each construct is greater than the correlation between other constructs, which indicates that each variable has different characteristics and does not overlap with each other.

Table 2. Discriminant Validity

Variables	PI	DM	MEB	CA	MP
Product Innovation (PI)	0.838				
Digital marketing (DM)	0.521	0.867			
Muslim Entrepreneurial Behavior (MEB)	0.607	0.546	0.813		
Competitive Advantage (CA)	0.376	0.357	0.609	0.749	
MSME Performance (MP)	0.608	0.492	0.657	0.592	0.763

R-square Test

The evaluation of the structural model in this study was carried out by looking at the value of the determination coefficient or R-square (R^2). The R-square value indicates how much the independent variable is capable of explaining the variation of the dependent variable. In the PLS-SEM approach, R-square values are generally categorized as strong, moderate, or weak, where values around 0.75 are considered strong, 0.50 moderate, and 0.25 weak.

Based on the test results in Table 1, the R-square value for the competitive advantage variable is 0.371 with an adjusted R-square value of 0.358. This shows that product innovation, digital marketing, and Muslim entrepreneurial behavior were able to explain 37.1% of the variation in competitive advantage, while the rest was influenced by other factors outside the research model.

Furthermore, the MSME performance variable based on Islamic values (MSME performance) has an R-square value of 0.565 with an adjusted R-square of 0.553. These results indicate that product innovation, digital marketing, Muslim entrepreneurial behavior, and competitive advantages together are able to explain 56.5% of the variation in MSME performance based on Islamic values. Thus, this research model has moderate to quite strong predictive capabilities in explaining the performance of MSMEs based on Islamic values.

Table 3. R-square Test

Items	R-square	R-square Adjusted
Competitive Advantage (CA)	0.371	0.358
MSME Performance (MP)	0.565	0.553

Overall, the R-square values of both endogenous variables indicate that the structural model in this study has sufficient elucidation and can be used for further hypothesis testing.

F-square Test

In this study, the effect size (f-square) test was determined based on the criteria of small influence if the f-square value ≥ 0.02 , moderate influence if ≥ 0.15 , and large influence if ≥ 0.35 . The test results showed that the value of product innovation on the performance of MSMEs based on Islamic values (MSME performance) was 0.119, which was included in the category of small influence. The value of product innovation against competitive advantage is 0.000, which indicates no influence. Furthermore, the value of digital marketing on the performance of MSMEs based on Islamic values is 0.014, which indicates a very small influence, while the value of digital marketing on competitive advantage is 0.001, which also shows a very small influence. The results of the next test showed that the value of Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values was 0.057, which was included in the category of small influence. Meanwhile, the value of Muslim entrepreneurial behavior towards competitive advantage is 0.309, which is included in the category of moderate to close to large influence. Finally, the value of competitive advantage to the performance of MSMEs based on Islamic

values is 0.129, which shows a small to close to medium influence.

Table 4. F-square Test

Items	F-square
PI → MP	0.119
PI → CA	0.000
DM → MP	0.014
DM → CA	0.001
MEB → MP	0.057
MEB → CA	0.309
CA → MP	0.129

Overall, the results of the effect size test show that Muslim entrepreneurial behavior has the greatest contribution in increasing the competitive advantage of MSMEs, compared to other variables in this research model.

Discussion

This study highlights the influence of product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values, which is predicted to be mediated by competitive advantage. Based on the results of the hypothesis testing that has been carried out (see Table 5), this study aims to clarify the relationship between variables in the research model. Hypothesis testing was carried out to find out whether independent variables have a direct or indirect influence on dependent variables through intervening variables.

The researcher used two main approaches in testing the hypothesis. First, direct effect analysis is carried out through path coefficient testing with a bootstrapping procedure to test the relationship between independent variables and dependent variables. In this test, the p-value was used as the basis for decision-making, where the p-value < 0.05 showed a significant influence.

Second, an indirect effect analysis was carried out to assess the role of competitive advantage as a mediating variable in the relationship between product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values. If the test results show a p-value of < 0.05, then it can be concluded that the intervening variable has a significant mediating role in the research model. Thus, this study provides an empirical understanding of the factors that affect the performance of MSMEs based on Islamic values, both directly and through the formation of competitive advantage.

Table 4. Hypothesis test results

Hypothesis	Model	Standard deviation	T-Statistics	P values	Results
H ₁	PI → MP	0.085	3.522	0.000	Significant
H ₂	DM → MP	0.088	1.127	0.260	Insignificant
H ₃	MEB → MP	0.089	2.698	0.007	Significant
H ₄	CA → MP	0.083	3.573	0.000	Significant
H ₅	PI → CA → MP	0.031	0.001	0.999	Insignificant
H ₆	DM → CA → MP	0.029	0.360	0.719	Insignificant
H ₇	MEB → CA → MP	0.051	3.482	0.001	Significant

The Influence of Product Innovation on the Performance of MSMEs Based on Islamic Values

Product innovation represents strategic capabilities in creating quality updates, variations, and product designs that generate added value for customers (Kotler and Armstrong 2018; Sukmadi 2016). In the context of MSME competition, innovation is not just a creative activity, but a differentiation mechanism that allows businesses to maintain market relevance

and respond to demand dynamics (Tjiptono and Chandra 2016).

The test results show that product innovation has a positive and significant effect on the performance of MSMEs based on Islamic values, so H1 is accepted. These findings indicate that innovation capabilities directly increase business growth, revenue, assets, and workforce. In other words, continuous product updates are the main causes of business performance.

Theoretically, these findings are consistent with RBV which places innovation capabilities as a valuable and elusive resource that results in competitive advantage and superior performance. In the context of MSMEs based on Islamic values, product innovation also serves as an instrument to strengthen the value proposition based on halal, transparency, and benefits, which deepens customer trust and loyalty. Cross-contextual empirical evidence also confirms that innovation capability and product quality are significant determinants of MSME performance (Harini, Silaningsih, and Putri 2022; Kamalrulzaman et al. 2021; Okangi 2023). Nonetheless, the literature emphasizes that the impact of innovation will be stronger when embedded in broader capability systems, such as organizational learning and technology utilization. This means that isolated innovations may improve performance, but innovations that are integrated in strategic capability configurations tend to produce more sustainable impacts. Thus, this study emphasizes that product innovation is a direct and strategic determinant for improving the performance of MSMEs based on Islamic values.

The Influence of Digital Marketing on the Performance of MSMEs Based on Islamic Values

Digital marketing refers to the use of internet-based platforms to build communication, branding, and relationships with consumers through accessibility, interactivity, entertainment, trust, and information quality (Chakti 2019; Kotler and Armstrong 2018; Nasdini 2012). Conceptually, digital marketing is seen as a strategic capability that expands market reach and strengthens customer relationships so that it has the potential to improve the performance of MSMEs. However, the test results showed that digital marketing did not have a significant effect on the performance of MSMEs based on Islamic values, so H2 was rejected. These findings indicate that the use of digital channels by respondents has not been able to be configured as an internal resource that actually encourages business, income, assets, and labor growth.

Although a number of studies report a positive relationship between digital marketing capability and performance (Chinakidzwa and Phiri 2020; Munir et al. 2023; Sultoni et al. 2022), Recent literature shows that such influences are often indirect and depend on complementary capabilities such as innovation, brand capability, absorptive capacity, and more mature digital capabilities (Hoang and Hien 2024; Moschogianni 2024; Purnamasari et al. 2024). Thus, digital marketing is more accurately understood as an enabler that requires the integration of strategies and organizational readiness to produce performance impacts. In the context of this study, the insignificance shows that digital marketing is still at the operational level as promotional activities have not developed into strategic capabilities that are integrated with differentiation, customer relationship management, and sharia-based value propositions. Therefore, improving performance through digital marketing requires strengthening digital literacy, IT/CRM capabilities, and alignment of strategy and business values so that it can be translated into sustainable performance.

The Influence of Muslim Entrepreneurial Behavior on the Performance of MSMEs Based on Islamic Values

Muslim entrepreneurial behavior reflects an entrepreneurial orientation based on shiddiq, amanah, tabligh, and fathanah sharia values that form integrity, professionalism, and quality of decision-making in business (Hendayana, Lisnawati, and Machmud 2017; Suryana 2009). Conceptually, the internalization of these values strengthens the trust, reputation, and effectiveness of business management, which is ultimately reflected in the growth of the business, revenue, assets, and workforce (Rafsanjani 2022; Taufiq, Prihatni, and Gurendrawati

2020). The test results showed that Muslim entrepreneurial behavior had a positive and significant effect on the performance of MSMEs based on Islamic values, so H3 was accepted. This means that the stronger the application of sharia-based ethical values and professionalism, the higher the business performance achievements.

These findings are in line with the entrepreneurial orientation literature that places value-based orientation as a driver of performance, both directly and through strengthening managerial practices (Daniel and Chukwuemeka 2023; Kee and Rahman 2020). Within the framework of RBV, ethical and reputational value serves as an intangible asset that strengthens market legitimacy and lowers transaction risk. Empirical evidence in the context of Islamic entrepreneurial orientation and Islamic work ethics also shows that religious orientation and Islamic work ethics are positively correlated with performance through increased commitment, motivation, and business credibility (Suginam et al. 2025; Udin et al. 2022; Zainuddin et al. 2023). Thus, this study emphasizes that Muslim entrepreneurial behavior is not just a normative dimension, but a strategic determinant that directly contributes to improving the performance of MSMEs based on Islamic values.

The Influence of Competitive Excellence on the Performance of MSMEs Based on Islamic Values

Competitive advantage refers to the ability of a business to create superior value to competitors through effective resource management (Barney & Hesterly, 2020; Hajar & Sukaatmadja, 2016). In this study, competitive advantage is reflected in the uniqueness of the product, quality, and competitive price as a form of value proposition that is difficult to match (Subagja 2021). The test results show that competitive advantage has a positive and significant effect on the performance of MSMEs based on Islamic values, so H4 is accepted. This means that MSMEs that are able to build strong differentiation and market positioning show higher business, revenue, assets, and labor growth.

Theoretically, these findings are consistent with RBV placing competitive advantage as a result of configuring valuable internal resources and capabilities in creating superior performance. Studies have shown that innovation capabilities, market orientation, and effective resource management improve performance through the establishment of competitive advantage as a strategic path (Mongkol 2022; Otache 2024). The differentiation approach has also been shown to be positively correlated with improving the performance of MSMEs in various contexts (Choo 2024; Navaia, Moreira, and Ribau 2023). In the context of Islamic values-based MSMEs, competitive advantage comes not only from functional aspects such as quality and price, but also from the consistency of values, trust, and business reputation that strengthen the market position. Thus, this study emphasizes that competitive advantage is a strategic determinant and a direct path to improving the performance of MSMEs based on Islamic values.

The Role of Competitive Excellence in Mediating the Influence of Product Innovation on the Performance of MSMEs Based on Islamic Values

Theoretically, the relationship between product innovation, competitive advantage, and performance can be explained through RBV. Innovation is seen as a strategic capability that enables market differentiation and adaptation, which further shapes competitive advantage and drives performance (Barney & Hesterly, 2020). A number of studies show that innovation improves performance through the establishment of a superior competitive position (Mongkol 2022; Otache 2024). However, the results of this study show that competitive advantage is not able to mediate the influence of product innovation on the performance of MSMEs based on Islamic values, so H5 is rejected. These findings indicate that the innovations carried out have not been fully converted into sustainable competitive differentiation because they have not resulted in unique positioning that is difficult for competitors to replicate.

The literature emphasizes that innovation is a necessary but not sufficient condition in

building competitive advantage; The impact relies heavily on integration with complementary capabilities such as market orientation, knowledge management, and strategic leadership (Kafetzopoulos and Gotzamani 2021; Yan, Rahman, and Tong 2022). In the context of Islamic value-based MSMEs, innovations that are not accompanied by a clear value proposition both functionally and ethically tend to only temporarily increase product attractiveness, without establishing a consistent reputation or differentiation in the market. This shows that the innovations carried out are likely to be incremental and operational, so that they have a direct impact on performance (e.g. increased sales or consumer interest) but have not been able to build competitive advantage as a sustainable mediation mechanism. Thus, this study emphasizes that in the framework of RBV and Islamic economics, innovation needs to be configured strategically and in line with business values so that it can be transformed into a stable competitive advantage.

The Influence of Competitive Excellence in Mediating Muslim Entrepreneurial Behavior on the Performance of MSMEs Based on Islamic Values

Digital marketing is understood as a technology-based strategic capability that allows market expansion, customer interaction, and branding strengthening (Chakti 2019; Kotler and Armstrong 2018). In the framework of RBV, effective management of digital resources should create a competitive advantage that then drives performance (Barney & Hesterly, 2020). However, the results of the study show that competitive advantage is not able to mediate the influence of digital marketing on the performance of MSMEs based on Islamic values, so H₆ was rejected. This means that digital marketing in the context of this study has not been proven to have a significant influence on performance through the formation of strong competitive differentiation.

The literature shows that digital marketing capability often impacts performance through indirect channels and relies heavily on complementary capabilities such as innovation capability, absorptive capacity, relationship marketing, and dynamic capabilities (Erlany et al. 2023; Hoang et al. 2025; Liu et al. 2022). Without strategic integration with product differentiation, market orientation, and business positioning, digital capabilities tend to function as operational promotion tools, rather than as internal resources capable of creating a sustainable competitive advantage (Mainardes et al. 2021). Thus, these findings confirm that in the context of MSMEs based on Islamic values, digital marketing has not been optimally managed as a strategic resource, so it is not able to form a competitive advantage and the mediation path to performance has not proven to be significant.

The Influence of Competitive Excellence in Mediating Muslim Entrepreneurial Behavior on the Performance of MSMEs Based on Islamic Values

Muslim entrepreneurial behavior represents an entrepreneurial orientation based on sharia values such as shiddiq, amanah, tabligh, and fathanah which is in line with the dimensions of entrepreneurial orientation (EO) such as proactivity and innovation (Bahri 2018; Suryana 2009). The literature shows that EO improves performance not only directly, but also through strategic mechanisms such as innovation and competitive advantage (Kee and Rahman 2020; Yang, Xun, and Chong 2022). From an RBV perspective, ethical values, reputation, and legitimacy are intangible assets that can be a source of sustainable competitive advantage (Barney & Hesterly, 2020). In the context of Islamic economics, the internalization of these values forms trust-based advantage reputational capital that is difficult for competitors to imitate because it comes from moral commitment and consistency of business behavior.

Empirically, business ethics have been proven to strengthen competitive advantage which then improves business performance (Asyhari, Pudjihastuti, and Kurdaningsih 2018). These findings are relevant in the context of Islamic value-based MSMEs, where integrity, transparency, and sharia compliance form a differentiation based on trust, credibility, and market legitimacy. Reputations built through trustworthy and fair business practices become

intangible capital that strengthens customer loyalty and expands the network of business relationships.

The results of the study show that competitive advantage significantly mediates the influence of Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values. This means that the internalization of Islamic entrepreneurial values does not directly improve performance, but first forms business differentiation and positioning through reputation, service quality, and value consistency reflected in uniqueness, quality, and competitive prices, which then encourages business growth. Thus, this study received H7 and affirmed that competitive advantage is a key mechanism that transforms Muslim entrepreneurial behavior into superior MSME performance through the formation of sharia reputational capital as a source of sustainable competitive advantage.

4. CONCLUSIONS AND SUGGESTION

This study analyzes the influence of product innovation, digital marketing, and Muslim entrepreneurial behavior on the performance of MSMEs based on Islamic values with competitive advantage as a mediation variable. The results of PLS-SEM show that product innovation and Muslim entrepreneurial behavior have a positive and significant effect on the performance of MSMEs, while digital marketing has no significant effect. Competitive advantage has been shown to have a positive effect on performance, but the mediation role is selective. Competitive advantage only mediates the relationship between Muslim entrepreneurial behavior and performance but does not mediate the influence of product innovation or digital marketing on performance. These findings show that product innovation plays a role as a direct driver of performance, while digital marketing has not been configured as a strategic capability that results in competitive differentiation. Theoretically, this study strengthens the Resource-Based View in the context of sharia economics by showing that Muslim entrepreneurial behavior is an intangible resource that forms sharia-based reputational capital and becomes a strategic mechanism in improving the performance of MSMEs

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