

Strategic Leadership and SMEs Performance in Indonesia: The Mediating Role of Dynamic Human Resource Capability

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ABSTRACT

Drawing on the Dynamic Capability View and Strategic Human Resource Management literature, this study examines the mediating role of dynamic human resource capability (DHRC) in the relationship between strategic leadership and the performance of small and medium-sized enterprises (SMEs) in Indonesia. Data were collected through a cross-sectional survey of 287 SME owners and managers across six provinces in Java and analyzed using Partial Least Squares Structural Equation Modeling (PLS-SEM). The results indicate that strategic leadership is positively associated with DHRC ($\beta = 0.794$, $p < 0.001$) and SME performance ($\beta = 0.192$, $p = 0.021$). DHRC is also positively associated with SME performance ($\beta = 0.622$, $p < 0.001$). Furthermore, DHRC partially mediates the relationship between strategic leadership and SME performance, as demonstrated by a significant indirect effect ($\beta = 0.494$, $p < 0.001$). These findings suggest that the contribution of strategic leadership to SME performance is largely transmitted through adaptive human resource routines involving learning, integration, and reconfiguration. The study extends the Dynamic Capability View by identifying DHRC as a human resource micro-foundation that helps translate strategic leadership into organizational performance in resource-constrained SME contexts.

Keywords: Dynamic human resource capabilities, SME performance, Strategic leadership

1. INTRODUCTION

The contemporary business environment is increasingly characterized by technological disruption, intensifying competition, and rapidly evolving customer expectations, requiring organizations to continuously renew their capabilities to sustain long-term competitiveness (Mani & Mishra, 2020; Somwethee et al., 2025). Under these conditions, competitive advantage is no longer derived solely from operational efficiency; rather, it depends on an organization's ability to anticipate environmental change, adapt strategically, and continuously reconfigure its capabilities before existing advantages erode. Within this context, strategic leadership has become a critical organizational capability that enables SMEs to navigate uncertainty while maintaining superior performance. Defined as top managers' capacity to anticipate future challenges, articulate a strategic vision, preserve organizational flexibility, and mobilize strategic change (Kebede et al., 2024; Schoemaker et al., 2013), strategic leadership is widely recognized as a key driver of innovation, strategic renewal, market responsiveness, and long-term organizational sustainability (Gausmann & Ricci, 2019).

Empirical evidence concerning the relationship between strategic leadership and firm performance continues to present an unresolved theoretical puzzle. A substantial body of research demonstrates that strategic leadership enhances organizational performance by shaping strategic priorities, directing resource allocation, and strengthening organizational capabilities (Ambilichu et al., 2023; Ashkevari & Ghasemi, 2023; Bhardwaj et al., 2020; Jalaludin et al., 2024; Woo, 2025). In contrast, other studies report weak or statistically insignificant direct effects (Najmi, 2018; Quansah et al., 2022; Reniati et al., 2024; Santoso et al., 2019). Rather than representing contradictory evidence, these findings suggest that the effectiveness of strategic

leadership is contingent upon organizational mechanisms capable of transforming strategic intent into sustained organizational performance. From this perspective, the persistent inconsistency observed in previous studies is unlikely to reflect the limited value of strategic leadership itself; instead, it indicates that the leadership and performance relationship cannot be adequately explained through a direct linear association alone. Identifying the organizational capability that bridges this relationship therefore remains an important theoretical challenge.

The unresolved inconsistency surrounding the strategic leadership and performance relationship indicates that leadership effectiveness cannot be adequately understood through a direct cause and effect perspective. Previous studies have proposed a wide range of mediating and moderating mechanisms, including organizational innovation, corporate entrepreneurship, organizational culture, strategic alignment, information technology capability, learning orientation, board power, top management team integration, and organizational climate (Abdulaal & Zoubi, 2025; Al-dhamari et al., 2025; Aljuhmani et al., 2021; Ambilichu et al., 2023; Ashkevari & Ghasemi, 2023; Kusumah et al., 2021; Lamsam & Charoensukmongkol, 2023; Palmer et al., 2020; Para-González et al., 2017; Pucheta-Martínez & Gallego-Alvarez, 2024; Salman & Ibrahim, 2024; Sawaeen & Ali, 2021; Shahzad et al., 2024; Tirastittam et al., 2020; Venugopal et al., 2023; Woo, 2025). Although these studies collectively demonstrate that strategic leadership exerts its influence indirectly, their explanations remain concentrated on structural, behavioural, governance, and technological mechanisms. Consequently, they provide only limited insight into how organizations continuously transform strategic intent into adaptive organizational action through the dynamic deployment of human resources. This omission suggests that the source of the persistent inconsistency may lie not in strategic leadership itself, but in the limited understanding of the organizational capability through which leadership is translated into superior performance.

Building upon this argument, an important theoretical gap remains within the Dynamic Capability View (DCV) (Teece et al., 1997). Although these studies have identified various organizational mediators such as innovation, culture, learning orientation, and strategic alignment comparatively less attention has been devoted to the specific human resource micro-foundation through which strategic leadership is operationalized. More precisely, the three-dimensional mechanism of learning, integration, and reconfiguration which collectively constitute Dynamic Human Resource Capability (DHRC) has not been systematically tested as the transmission mechanism linking strategic leadership to SME performance, particularly in resource-constrained settings. Unlike broader constructs such as general dynamic capabilities or workforce agility, DHRC specifically captures the human resource routines through which organizations learn, integrate, and reconfigure their talent base offering a more granular explanation of the leadership-performance link. Furthermore, the existing body of evidence has been generated predominantly from large organizations operating in relatively resource-abundant environments, whereas SMEs whose competitiveness depends heavily on adaptive capability under resource constraints remain substantially underrepresented (Quansah et al., 2022). As a result, current knowledge provides only a partial explanation of how strategic leadership translates into superior organizational performance in resource-constrained SMEs.

To address these theoretical and empirical limitations, this study integrates the Dynamic Capability View (DCV) with Strategic Human Resource Management (SHRM) by positioning Dynamic Human Resource Capability (DHRC) as the human resource micro-foundation linking strategic leadership to organizational performance. Rather than conceptualizing DHRC as a static organizational resource, this study views it as an adaptive capability through which organizations continuously acquire, integrate, and reconfigure human resources in response to environmental change (Apascaritei & Elvira, 2022; Garavan et al., 2016). Viewed from this perspective, DHRC comprises three mutually reinforcing dimensions learning and knowledge-building capability, integration capability, and reconfiguration capability (Chadwick & Flinchbaugh, 2021; Lavie, 2006; Pillai & Srivastava, 2022) that collectively enable organizations to convert strategic intent

into coordinated organizational action. Accordingly, the present study argues that the contribution of strategic leadership to SME performance is realized not through a simple direct relationship, but through its capacity to cultivate adaptive human resource capabilities that strengthen organizational responsiveness, resilience, and sustained competitive advantage.

The proposed theoretical framework is examined within the context of SMEs operating across Java, Indonesia, providing an appropriate empirical setting for evaluating the relationships among strategic leadership, Dynamic Human Resource Capability (DHRC), and organizational performance. SMEs constitute the backbone of the Indonesian economy, contributing approximately 60.5% of the national gross domestic product and accounting for nearly 97% of total employment (Andayani et al., 2026). Despite their economic significance, many Indonesian SMEs continue to operate under persistent resource constraints, institutional heterogeneity, and intensifying competitive pressures. Under these conditions, organizational adaptability becomes a prerequisite for sustained competitiveness rather than merely a strategic choice.

Although the six provinces of Java share a common national policy framework, they exhibit substantial heterogeneity in economic structure, labor market conditions, and digital infrastructure. DKI Jakarta and West Java, for instance, benefit from greater access to technology, financial services, and government support programs, whereas SMEs in Central Java and East Java often rely more heavily on traditional industries and informal networks. The sample distribution in this study reflects these regional differences, with the majority of respondents concentrated in DKI Jakarta (31.0%), West Java (26.5%), and Banten (20.2%), while Yogyakarta (3.5%) and East Java (3.8%) are comparatively underrepresented. This uneven distribution while partly attributable to the actual concentration of SMEs across provinces should be considered when interpreting the findings, as regional variations in institutional support and market conditions may influence the observed relationships. Future research with more balanced provincial sampling would help determine the extent to which these contextual factors moderate the proposed relationships.

Consequently, the Indonesian SME sector offers a particularly relevant context for examining whether adaptive human resource capability serves as the organizational mechanism through which strategic leadership is translated into superior performance. Against this backdrop, the present study develops and empirically tests an integrated framework that explains how strategic leadership contributes to SME performance through the development of Dynamic Human Resource Capability. Specifically, the study examines the direct relationship between strategic leadership and SME performance, investigates the influence of strategic leadership on DHRC, and evaluates the mediating role of DHRC in linking strategic leadership to organizational performance.

The study advances the literature in three important respects. First, it extends the Dynamic Capability View by identifying DHRC as the human resource micro-foundation through which strategic leadership influences organizational performance, thereby offering a theoretically grounded explanation for the inconsistent findings reported in previous studies. Second, by integrating the Dynamic Capability View with Strategic Human Resource Management, the study develops a more comprehensive explanation of how organizations convert strategic intent into adaptive organizational capability. Third, evidence drawn from Indonesian SMEs broadens the contextual scope of strategic leadership research beyond the large organizations and resource-abundant settings that have dominated prior scholarship, while simultaneously providing practical insights for managers and policymakers seeking to strengthen organizational resilience through adaptive human resource capability.

1.1. Literature review and hypothesis development

1.1.1. Strategic leadership

The strategic leadership notion dates back to Child (1972), who introduced the idea of 'strategic choices,' highlighting How executive actions affect an organization's future trajectory, expansion, and structural configuration (Kebede, 2024). Strategic leadership has been described a leader's capacity to predict, interpret, learn, stay able to adapt, engage in strategic reasoning, and engage collaborates with others to drive adjustments that ensure the organization's sustainable future (Schoemaker, 2013). Furthermore, strategic leadership pertains to the responsibilities carried out by top-tier personnel within an enterprise such as CEOs Executive members committee of supervisors, and broader managers worked to produce strategic outcomes for the organization. Strategic leadership concentrates on cross-functional tasks that are inherently ambiguous and complicated, with the goal of aligning internal and external environments to improve the company's performance (Samimi et al., 2022). According to Kebede et al., (2024), strategic leadership It is typically regarded as the function of senior executives who are accountable for steering an organization's long-term direction and outcomes. These leaders make determinations that synchronize the organizational vision with both external and internal forces, thereby securing lasting competitive advantage.

Studies on strategic leadership extends beyond the basic function of top executives in creating goals and providing strategic counsel as well as managing strategy creation and execution. It also includes a variety of procedures and strategies, including an instrument distribution, Competitiveness growth, agility in the market, innovation encouragement, and employee involvement (Shannassy, 2021). Jaleha & Machuki, (2018) claim that strategic leadership improves productivity by encouraging organizational transformation and rivalry, which necessitates adaptation people and institutional systems to an uncertain environment. As makers of decisions with broad duties, strategic leaders have a significant impact on company results by their opinions and actions (Ozgen et al., 2025).

1.1.2. Dynamic Capability and strategic human resource management

Resource-Based Theory (RBT) investigates how capabilities are developed to generate economic competitiveness for a company. This theory emphasizes the creation of an economic advantage over competitors through the utilization and deployment of strategic resources both Domestic and external environments, in addition to the development of capabilities (Kim et al., 2024; Pillai & Srivastava, 2022; Teece et al., 1997). Dynamic capabilities originate from the resource-based view (RBV) (Barney, 1991) and are described as a company's capacity to combine, grow, and restructure both internal and external skills as a means to manage with a quickly changing environment (Teece, 2012). Strategic dynamic capabilities assist organizations in adapting to environmental changes by emphasizing capabilities related to change and learning. These capabilities improve resource utilization, reduce the likelihood of business failure, foster learning, and support the attainment of competitive advantage (Teece et al., 1997). Investigations into dynamic capabilities and associated HRM matters have been undertaken within the framework of HRM (Apascaritei & Elvira, 2022); smart HRM (Pillai & Srivastava, 2022); talent handling strategies (Glaister et al., 2018); HRIS (Pillai & Srivastava, 2023); Administrative Mobility (Nijssen & Paauwe, 2012); transnational HRM systems (Festing & Eidems, 2011); responsible workforce reduction strategies (Milhem et al., 2024; Tsai & Shih, 2013); highly efficient work processes (Úbeda García et al., 2018); and quality management strategies concerning human resources. (Gutierrez-gutierrez et al., 2018).

According to previous research, dynamic human resource capabilities are based on a three-dimensional construct (learning and knowledge-building capability), integrating capability, and reconfiguring capability, all of which contribute to company performance (Apascaritei & Elvira, 2022; Chadwick & Flinchbaugh, 2021; Lavie, 2006; Lengnick-Hall et al., 2021; Pillai & Srivastava, 2023; Teece et al., 1997; Zahra et al., 2020) Building (Learning Capabilities and Knowledge Building): the capacity to learn is an organisation's ability To improve efficiency and effectiveness of operations by acquiring, transforming and disposing of resources

in line with environmental changes. (Lavie, 2006; Teece et al., 1997; Zahra et al., 2020). Integration capabilities: Integration capabilities indicate the organization's ability to analyze the worth of current resources and integrate them to produce new capabilities and resources that ensure the firm's competence in dealing with a demanding environment. (Lengnick-Hall et al., 2021; Teece et al., 1997). The reconfiguration capacity describes a business's capacity to rearrange and alter its existing resources, enabling it to accommodate evolving conditions in the market and react to competition and market swings (Chadwick & Flinchbaugh, 2021; Lavie, 2006; Teece et al., 1997).

1.1.3. SMEs Performance

This study assesses firm performance using subjective performance derived from self-reported performance by SME owners and managers. The reported measures of firm performance include financial and non-financial performance adopted from (Delaney & Huselid, 1996; Fu et al., 2016; Ho et al., 2024; Kim et al., 2024). In this study, objective data on financial performance was not readily available, primarily because owners/managers are typically not legally obligated to publish this data. Furthermore, owners and managers, as respondents, are generally assumed to have knowledge of their company's performance (Lubatkin et al., 2006).

1.1.4. Strategic leadership on SMEs performance

Prior research consistently demonstrates a positive association between strategic leadership and organizational performance across various contexts. Ambilichu et al., (2023) found that strategic leadership directly enhances firm performance while also generating indirect benefits through the cultivation of a supportive organizational climate that enables simultaneous exploitative and exploratory activities. Similarly, (Woo, 2025) reported that strategic leadership fosters corporate entrepreneurship at both individual and organizational levels, which in turn strengthens performance outcomes. In the SME context specifically, (Jalaludin et al., 2024) confirmed that strategic leadership exerts a positive and significant influence on SME performance, with dynamic capabilities serving as a partial transmission mechanism. Reniati et al., (2024) further demonstrated that specific strategic leadership traits including vision articulation, strategic resource allocation, market positioning, and trust-building collectively contribute to improved business performance. Although the magnitude of the direct effect varies across studies, the weight of evidence supports the theoretical expectation grounded in the Resource-Based View (RBV), which positions strategic leadership as a valuable, rare, and inimitable intangible resource that enables firms to configure internal processes and seize market opportunities (Barney, 1991). Accordingly, we hypothesize:

H1. Strategic leadership has a positive effect on an SME performance.

1.1.5. Strategic leadership on dynamic human resource capability

The relationship between strategic leadership and dynamic human resource capabilities is theoretically grounded in the Dynamic Capability View (DCV), which posits that organizational capabilities are actively shaped by managerial cognition and strategic choices (Teece et al., 1997). Empirical evidence supports this proposition: (Abdeen et al., 2025) found that strategic leadership significantly enhances a firm's dynamic capabilities, including sensing, learning, and integration capabilities, which in turn contribute to sustainable competitive advantage. Pitelis & Wagner, (2019) demonstrated that strategic shared leadership characterized by deliberate decision-making processes among the dominant coalition directly fosters organizational dynamic capabilities. More specifically, (Durán et al., 2023; Li et al., 2022; Milhem et al., 2024). reported that strategic leadership drives the enhancement of dynamic human resource capabilities by boosting employee engagement, stimulating HR innovation, and enabling organizations to navigate the complexities of a diverse workforce. In the context of Indonesian SMEs where formal HR systems are often limited the leader's role as a de facto HR architect becomes particularly salient, as strategic leaders must directly model, incentivize, and embed adaptive routines through daily interactions. This body of evidence suggests that strategic leadership serves as a critical

antecedent to the development of learning, integration, and reconfiguration routines that collectively constitute DHRC. Therefore, we hypothesize:

H2. Strategic leadership has a positive effect on Dynamic human resource capabilities.

1.1.6. Dynamic human resource capability on SMEs performance

The Dynamic Capability View posits that firms achieve superior performance not merely through the possession of valuable resources, but through their capacity to reconfigure resources in response to environmental change (Teece et al., 1997). Empirical studies consistently confirm that dynamic capabilities positively influence organizational performance across sectors and contexts (Apascaritei & Elvira, 2022; Gupta et al., 2018; Nguyen et al., 2024; Pillai & Srivastava, 2022). More specifically, the three dimensions of DHRC each contribute to performance in distinct ways. First, learning and knowledge-building capability ensures that employees receive timely training, reduces knowledge-sharing barriers, and enhances workforce competence, thereby providing a competitive edge (Apascaritei & Elvira, 2022; Lavie, 2006; Pillai & Srivastava, 2022). Second, integration capability enables organizations to coordinate existing HR practices and refine them in response to external changes, supporting data-driven decision-making, automation of routine processes, and improved HR efficiency (Pillai & Srivastava, 2022; Puhovichova & Jankelova, 2020). Third, reconfiguration capability facilitates the reorganization of HR processes and practices, supporting employee competence development for innovation and product creation (Apascaritei & Elvira, 2022; Milhem et al., 2024; Tsai & Shih, 2013). In the resource-constrained SME context, where formal HR infrastructures are often absent, these adaptive capabilities become especially critical for survival and growth. Accordingly, we hypothesize:

H3. Dynamic Human Resource Capabilities has a positive effect on SMEs Performance

1.1.7. The mediating role of dynamic human resource capability on the effect of strategic leadership on SMEs performance.

The preceding arguments collectively suggest a mediating mechanism: strategic leadership does not directly translate into superior performance; rather, its influence is channeled through the development of organizational capabilities that enable learning, integration, and reconfiguration. (Quansah et al., 2022) provided initial evidence for this proposition by demonstrating that dynamic capabilities including empowerment, resilience, and agility mediate the effect of strategic leadership on SME performance. Similarly, (Najmi, 2018) found that dynamic capabilities serve as a mediating variable in the relationship between strategic leadership and corporate performance, with the mediating effect strengthening as dynamic capabilities increase. The integration of DCV and SHRM further clarifies this mechanism: strategic human resource management practices enhance dynamic capabilities, which in turn positively influence innovation and performance in SMEs (Ho et al., 2024). More specifically, studies indicate that strategic leadership exerts both a strong direct effect on human resource management and a significant indirect effect on competitive advantage, with HRM serving as a critical mediator in enhancing strategic leadership effectiveness (Alshehadeh et al., 2025; Syed et al., 2024). These findings suggest that strategic leaders must prioritize the development of human resource capabilities that support learning, integration, and reconfiguration the three dimensions of DHRC to optimize performance outcomes. Building on this theoretical logic, we propose:

H4. Dynamic human resource capability mediates the positive effect of strategic leadership on firm performance.

2. METHOD

This study investigated the proposed associations using a quantitative research approach and a cross-sectional survey research design. The target population comprised SMEs across six Java provinces. Consistent with (Government of Indonesia, 2008), SMEs were defined as

enterprises with net assets of IDR 50 million–10 billion or annual sales of IDR 300 million–50 billion; micro-enterprises were excluded. Eligibility was verified through self-reported firm characteristics, including asset and revenue data. A purposive sample was drawn using two criteria: (1) operating ≥ 3 years, and (2) owners/managers directly involved in strategic decisions. Data were collected via online questionnaire from February to May 2026. Contact details were sourced from business directories and government databases. Of 300 invitations, 287 usable responses were retained after screening for missing values and straight-lining patterns (95.6% response rate). Non-response bias was assessed by comparing early and late respondents, revealing no significant differences (Abdeen et al., 2025). This study received institutional ethics approval (or exemption); all respondents provided informed consent, participated voluntarily, and were assured of anonymity and confidentiality.

All measurement instruments were adapted from established scales: strategic leadership (12 items; Schoemaker et al., 2013). Dynamic human resource capabilities comprising learning, integration, and reconfiguration dimensions (12 items; Eisenhardt & Martin, 2000; Pillai & Srivastava, 2023; Singh & Rao, 2016; Teece et al., 1997), and SME performance (6 items; Ambilichu et al., 2023; Arend, 2014; Schilke, 2014). Following the back-translation procedure (Woo, 2025), the original English items were translated into Bahasa Indonesia by bilingual experts and independently back-translated to ensure conceptual equivalence. All items were rated on a five-point Likert scale (1 = strongly disagree to 5 = strongly agree). We collected data on six firm- and respondent-level characteristics (firm age, firm size, sector, province, respondent role, and education). However, only firm size was included as a single-item covariate in the structural model to account for firm-level heterogeneity. The remaining five variables firm age, sector, province, respondent role, and education are reported descriptively in Table 1 but were excluded from PLS-SEM to preserve model parsimony, as treating sector (7 categories) and province (6 categories) as dummies would overcomplicate the model given our sample size (Hair et al., 2019). Procedural remedies (anonymity, item separation) and Common method bias was mitigated through procedural remedies, including respondent anonymity and the separation of predictor and criterion variables in the questionnaire (Podsakoff et al., 2003). To assess common method bias (Kock, 2015), we calculated construct-level full-collinearity VIF by inverting the latent variable correlation matrix following the procedure recommended by Kock, (2015). The results showed that all VIF values were below the conservative threshold of 5.0 (Hair et al., 2022), ranging from 1.00 to 3.71. Although the DHRC value (3.71) slightly exceeded the strict 3.3 cutoff, it remained well below 5.0, indicating that common method bias does not pose a serious threat to the validity of our findings (Hair et al., 2022; Kock, 2015).

Data were analyzed using PLS-SEM (SmartPLS 3.0), chosen over CB-SEM for its predictive focus, robustness to non-normal data, and mediation-testing capability (Hair et al., 2019). All constructs were modeled as reflective. The analysis followed a two-stage approach, first assessing the measurement model (reliability, convergent validity, and discriminant validity) and then evaluating the structural model (path coefficients, R^2 , Q^2 , and effect sizes). The significance of direct and indirect (mediation) effects was tested using a bootstrapping procedure with 5,000 resamples, generating bias-corrected and accelerated (BCa) 95% confidence intervals (Hair et al., 2019).

3. RESULTS AND DISCUSSION

3.1. Results

Characteristic Respondent

The majority, approximately 31.0%, of the SMEs included in this study are located in the DKI Jakarta. This indicates that this region has a dominant concentration of SMEs compared to West Java (26.5%), Banten (20.2%), Central Java (15.0%), East Java (3.8%) and Yogyakarta

(3.5%). However, when viewed from the demographic perspective of the SME representatives who completed the questionnaire, the majority around 59.2% of respondents were female, compared to 40.8% male. The most represented age groups were 20 to 29 years (52.5%) and 30 to 39 years (18.3%). This suggests that SMEs representatives are predominantly young people of working age. Furthermore, the majority, around 42.7%, were undergraduate graduates, suggesting that undergraduate graduates are more interested in becoming entrepreneurs. In terms of roles, around 76.5% of respondents were owners and managers, indicating that they have full control over business operations and are well-suited to act as SME representatives in this study. Regarding the length of operation, the majority around 64.5% have been in operation for three to eight years, indicating that many are probably in the beginning phases or in development. In terms of staff, the majority 55.1% have between one and five employees, reflecting the small scale of the businesses, which are typically run by individuals or families. Furthermore, responses were received from various types of businesses: 20.9% were trading businesses, followed by the food and beverage sector at 19.3%, manufacturing at 17.2%, services at 14.4%, other businesses at 13.1%, fashion at 10.5%, and agriculture/farming/livestock at 3.8%, as shown in Table 1.

Table 1. Characteristics Respondents

Characteristic	(N)287	Percentage
Gender		
Male	117	40.8
Female	170	59.2
Respondents Age		
20 – 29 Tahun	158	55.0
30 – 39 Tahun	53	18.5
40 – 49 Tahun	39	13.6
50 – 59 Tahun	28	9.8
>60 Tahun	9	3.1
Job Title		
Owner	222	77.4
Manager	65	22.6
Business Experience		
3 – 8 Years	184	64,1
9 – 14 Years	46	16.0
15 – 20 Years	28	9,8
> 20 Years	29	10.1
Educational Background		
Non Academic	8	2,9
Elementary/Middle/High School/Equivalent	113	39.3
Diploma	13	4.5
Bachelor	126	43.9
Postgraduate	27	9.4
Business Sector		
Fashion	30	10,5
Service	42	14,6
Culinary	56	19,5
Manufacture	50	17,5
Trading	60	20.9
Agriculture/animal husbandry/fisheries	11	3,8
Other businesses	38	13,2

Number of employees

1 – 5 people	157	54.7
6 – 10 People	36	12.5
11 – 15 People	18	6.3
16 – 20 People	15	5.3
> 20 People	61	21.2

Residence

Banten	58	20.2
DKI Jakarta	89	31,0
West Java	76	26,5
Central java	43	15,0
Yogyakarta	10	3,5
East Java	11	3,8

Source(s): Authors'own work

Measurement Model Evaluation (Outer Model)

The measurement model was rigorously validated using Partial Least Squares Structural Equation Modeling (PLS-SEM) through analysis of outer loadings, internal consistency reliability, convergent validity, and discriminant validity, referring to (Hair et al., 2019). As detailed in Table 2, the Cronbach's alpha, Dijkstra-Henseler's rho (ρ_A), and composite reliability (CR) coefficients for all constructs consistently exceeded the recommended threshold of 0.70, indicating a very good level of internal consistency. Convergent validity was also met, considering that the Average Variance Extracted (AVE) value for each latent variable was above the minimum threshold of 0.50 (Hair et al., 2019). Discriminant validity was assessed using Fornell-Larcker and HTMT criteria, including control variables. While Fornell-Larcker revealed a marginal overlap between SL and DHRC ($\sqrt{AVE_{SL}} = 0.762 < 0.794$) common for theoretically linked predictor-mediator pairs the more robust HTMT criterion confirmed discriminant validity. All hypothesized construct values were below 0.85, peaking at 0.840 (SL↔DHRC; DHRC↔FP)(Dijkstra & Henseler, 2015). The control variable FirmSize exhibited low correlations with all constructs (HTMT < 0.06), confirming its distinctiveness.

Table 2. Validity and reliability test result

Constructs	Item	Loading Factors	Croncach alpha	rho_A	CR	AVE
Strategic Leadership (Schoemaker et al., 2013)	SL1	0.793	0.934	0.935	0.943	0.581
	SL2	0.794				
	SL3	0.711				
	SL4	0.763				
	SL5	0.714				
	SL6	0.784				
	SL7	0.779				
	SL8	0.815				
	SL9	0.737				
	SL10	0.715				
	SL11	0.800				
	SL12	0.735				

Dynamic Human Resource Capability (Eisenhardt & Martin, 2000; Pillai & Srivastava, 2023; Singh & Rao, 2016; Teece et al., 1997).	DHRC1	0.794	0.942	0.943	0.949	0.611
	DHRC2	0.807				
	DHRC3	0.751				
	DHRC4	0.779				
	DHRC5	0.720				
	DHRC6	0.823				
	DHRC7	0.787				
	DHRC8	0.785				
	DHRC9	0.832				
	DHRC10	0.794				
	DHRC11	0.748				
	DHRC12	0.748				
SMEs Performance (Ambilichu et al., 2023; Arend, 2014; Schilke, 2014)	FP1	0.821	0.899	0.899	0.922	0.664
	FP2	0.852				
	FP3	0.806				
	FP4	0.809				
	FP5	0.817				
	FP6	0.784				

Source(s): Authors'ownwork

Table 3. Discriminant validity

	Dynamic HR Capability	Firm Performance	Firm Size	Strategic Leadership
Dynamic HR Capability	0.781			
Firm Performance	0.775	0.815		
FirmSize	0.001	0.051	1.000	
Strategic Leadership	0.794	0.687	0.003	0.762
Heterotrait-Monotrait Ratio (HTMT) with BCa 95% CI				
		HTMT	2.5%	97.5%
Dynamic HRCapability ↔ Firm Performance		0.840	0.756	0.902
Dynamic HRCapability ↔ FirmSize		0.042	0.030	0.041
Dynamic HRCapability ↔ Strategic Leadership		0.840	0.757	0.901
Firm Performance ↔ FirmSize		0.053	0.012	0.091
Firm Performance ↔ Strategic Leadership		0.748	0.623	0.835
FirmSize ↔ Strategic Leadership		0.059	0.035	0.063

Note: Diagonal values (in bold) in the Fornell-Larcker section represent the square root of the Average Variance Extracted (AVE). BCa = Bias-corrected and accelerated bootstrap confidence intervals based on 5,000 resamples. All HTMT values are below the conservative threshold of 0.85, and the upper bounds of all confidence intervals are below 1.0, confirming discriminant validity

Structural Model Evaluation

The next step involves checking the R-squared and Q-square values, which reflect the predictive power of the model by showing the percentage of differences in endogenous variables explained by exogenous variables. Table 6 shows that the evaluation of the structural model through the coefficient of determination (R^2) and predictive relevance (Q^2), it is known that Strategic Leadership is able to explain 63.1% of the variation in Dynamic Human Resource Capability (with the remaining 36.9% influenced by other variables), then Dynamic Human Resource Capability, Strategic Leadership is able to explain 61.7% of the variation in SMEs Performance (with the remaining 38.3% influenced by external factors). In addition, the results of the Blindfolding procedure show that all endogenous constructs have a Q^2 value > 0 , which indicates the model has good predictive power.

Table 4. PLSpredict Results for Out-of-Sample Predictive Power

Model	RMSE	MAE	MAPE	Q2_Predict
PLS model	0.743	0.590	17.144	0.300
Naive LM Benchmark	0.831	0.641	21.014	0.332

Note: RMSE = Root Mean Square Error; MAE = Mean Absolute Error; MAPE = Mean Absolute Percentage Error.

To assess the out-of-sample predictive power of the PLS model, we conducted PLSpredict with 10 folds and 10 repetitions (Shmueli et al., 2019). As shown in Table 4, the PLS model yielded lower prediction errors than the naive linear model (LM) benchmark, with RMSE values of 0.743 (PLS) vs. 0.831 (LM) and MAE values of 0.590 (PLS) vs. 0.641 (LM). These results indicate that the PLS model outperforms the naive benchmark in terms of predictive accuracy. Although the Q^2_{predict} for the PLS model (0.300) is slightly lower than that of the LM benchmark (0.332), the primary decision criterion—the comparison of RMSE and MAE—clearly supports the predictive superiority of the PLS model (Shmueli et al., 2019). Indicator-level results are provided in the Appendix for a more detailed assessment.

Thus, the developed structural model is considered adequate and suitable for use to explain the statistically significant associations between variables in this study. Prior to testing the hypotheses, we assessed collinearity among the predictor constructs using the Variance Inflation Factor (VIF). All VIF values were well below the conservative threshold of 5, ranging from 1.000 to 2.711, indicating no multicollinearity concerns (Hair et al., 2019).

To rule out alternative explanations, we included firm size as a control variable in the structural model. The result indicated that firm size did not exert a significant effect on SME performance $\beta = 0.049$, $t = 1.200$, $p = 0.230$. Furthermore, the inclusion of this control resulted in only a marginal increase in the R^2 value of SME performance (from 0.602 to 0.617), confirming that the observed relationships are robust and not artifacts of firm-level heterogeneity.

Finally, this study evaluates model fit using an overall model evaluation, as suggested by (Henseler et al., 2016). Model fit was assessed using the standardized root mean square residual (SRMR), along with d_{ULS} and d_{G} . Table 5 displays the model fit indicators. The SRMR value of the estimated model was 0.051, which is below the conservative threshold of 0.08, indicating a good model fit (Hair et al., 2019).

Table 5. Fit Model

	Saturated Model	Estimated Model
SRMR	0,051	0,051
d_{ULS}	1,278	1,278
d_{G}	0,635	0,635
Chi-Square	971,316	971,346
NFI	0,850	0,850

Source(s):Authors'ownwork

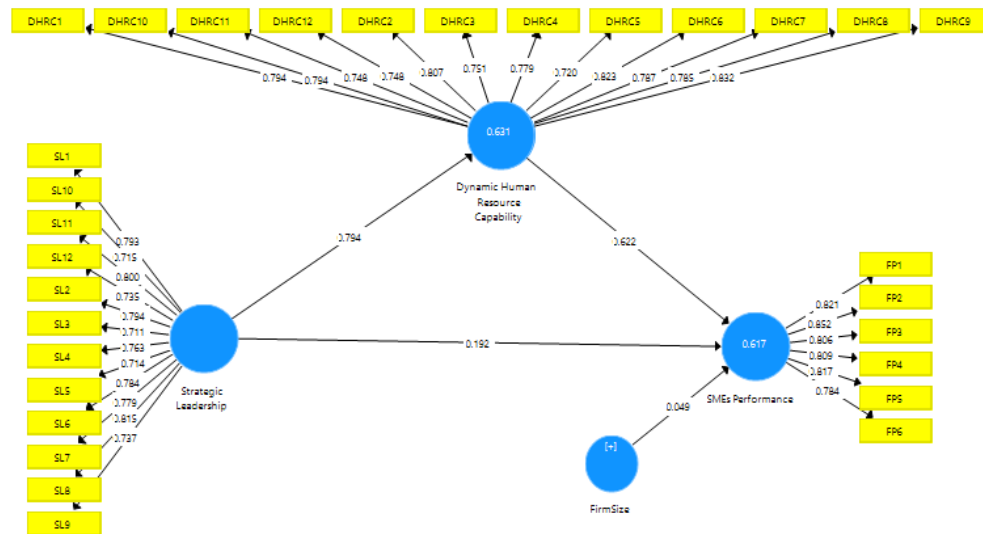


Figure 2. Path Analysis

Table 6. R-square

Endogenous variable's	R Square	R Square Adjusted	Q ²
Dynamic HR Capability	0,631	0,630	0.376
SMEs Performance	0,617	0,613	0.401

Source(s):Authors'ownwork

As shown in Table 7, the bias-corrected and accelerated (BCa) 95% confidence intervals for all hypothesized direct and indirect paths did not contain zero, further confirming the statistical significance of H1, H2, H3, and H4. In contrast, the confidence interval for FirmSize (control variable) contained zero, confirming its non-significant influence.

The structural model results indicate that all hypothesized direct relationships are statistically significant, providing empirical support for H1, H2, and H3. Hypothesis 1 (H1), which posits that Strategic Leadership (SL) positively influences SME Performance (FP), is supported with a path coefficient of $\beta = 0.192$ ($t = 2.305$; $p < 0.05$). However, the effect size ($f^2 = 0.036$) is categorized as small according to (Mfarrej et al., 2025) criteria, suggesting that the direct contribution of strategic leadership to SME performance remains relatively limited after accounting for other predictors. Hypothesis 2 (H2), which proposes that SL positively influences Dynamic Human Resource Capability (DHRC), demonstrates a remarkably strong and dominant influence, with a path coefficient of $\beta = 0.794$ ($t = 22.303$; $p < 0.001$) and a large effect size ($f^2 = 1.711$), thereby confirming that strategic leadership constitutes a strong predictor in cultivating adaptive and dynamic human resource capabilities. Meanwhile, Hypothesis 3 (H3), which examines the effect of DHRC on SME performance, is also supported with a path coefficient of $\beta = 0.622$ ($t = 8.168$; $p < 0.001$) and a large effect size ($f^2 = 0.373$), substantiating that dynamic human resource capability serves as a substantive contributor of SME performance enhancement.

Table 7. Hypotheses Testing Results

Path	VIF	Original Sampel	STDEV	T Statistic	P Value	2.5 %	97.5 %	f ²	Result
Direct effect									
H1 SL→FP	2.711	0,192	0,083	2,305	0,021	0.016	0.344	0,036	Supported

H2	SL→DHRC	1.00	0,794	0,036	22.303	0,000	0.757	0.901	1,711	Supported
H3	DHRC→FP	2.711	0,622	0,076	8.168	0,000	0.756	0.902	0,373	Supported
Indirect effect										
H4	SL→DHRC→FP		0,494	0,064	7,666	0,000	0.367	0.624		Supported
Control variable										
	FirmSize→FP	1.00	0,049	0,041	1,205	0,288	-0.028	0.132	0.006	Not Supported

Note. STDEV =Standard Deviation. The significant $p < 0.05$ path coefficients (β) * $p < 0.05$ The significant *** $p < 0.001$. BCa = Bias-corrected and accelerated bootstrap confidence intervals based on 5,000 resamples. CI that does not contain zero indicates statistical significance at $p < 0.05$

Hypothesis 4 proposed that DHRC mediates the strategic leadership–SME performance relationship. The indirect effect was significant ($\beta = 0.494$, $t = 7.666$, $p < 0.001$), and because the direct effect remained significant ($\beta = 0.192$, $p = 0.021$), the mediation is partial (Fatima et al., 2026). The VAF value of 0.72 indicates that 72% of SL's total effect is transmitted through DHRC. Regarding effect sizes, SL demonstrated a large effect on DHRC ($f^2 = 1.711$), DHRC exhibited a large effect on FP ($f^2 = 0.373$), while SL's direct effect on FP was small ($f^2 = 0.036$). This pattern confirms that SL's primary contribution to performance operates indirectly via DHRC, aligning with the partial mediation finding.

3.2. Discussion

This study set out to resolve the inconsistent findings in the literature regarding the relationship between strategic leadership and SME performance by proposing and testing a mediation model anchored in the Dynamic Capability View (DCV) and Strategic Human Resource Management (SHRM). The empirical results offer partial support for our framework, revealing that DHRC serves as a significant partial mediation in the leadership-performance nexus. Importantly, the findings illuminate *why* strategic leadership does not always translate directly into superior performance particularly in resource constrained SME environments and underscore the critical role of adaptive human resource routines in channeling strategic intent into tangible outcomes.

Based on the hypothesized research model, our findings confirm a positive association between strategic leadership and SME performance, aligning with prior studies in both large corporations and SME contexts (Ambilichu et al., 2023; Ashkevari & Ghasemi, 2023; Bhardwaj et al., 2020; Jalaludin et al., 2024; Woo, 2025). This result is theoretically consistent with the Resource-Based View (RBV), which posits that strategic leadership as a valuable, rare, and inimitable intangible resource enables firms to configure their internal processes and seize market opportunities (Barney, 1991). In the Indonesia SME context, where formal strategic planning systems are often absent, the leader's capacity to anticipate environmental shifts, interpret ambiguous signals, and align organizational efforts becomes particularly salient for navigating competitive pressures and sustaining business viability. However, the magnitude of this direct effect is relatively modest, suggesting that strategic leadership alone is insufficient to fully explain performance variations among SMEs. Regarding the relative strength of direct versus indirect pathways, which we discuss in greater detail below.

Second, the findings of this study show that the strong positive association between strategic leadership and DHRC indicates that effective leaders play a decisive role in cultivating the organization's capacity for learning, integration, and reconfiguration of human resources. This

finding resonates with the DCV, which emphasizes that dynamic capabilities are not spontaneously generated but are actively shaped by managerial cognition and strategic choices (Teece et al., 1997). Strategic leaders, by articulating a compelling vision, fostering psychological safety, and encouraging experimentation, create the enabling conditions under which employees learn, collaborate, and adapt their routines. In the informal and resource-scarce SME settings of Java, where formal HRM infrastructure is limited, the leader's role as a *de facto* HR architect is amplified; they must directly model, incentivize, and embed adaptive routines through daily interactions rather than through formal policies. This interpretation extends prior work by (Abdeen et al., 2025; Durán et al., 2023; Li et al., 2022; Milhem et al., 2024; Pitelis & Wagner, 2019), who similarly found that strategic leadership energizes dynamic capabilities but did not specifically examine the human resource dimension in developing-economy SMEs.

Third, the findings of this study show that the positive association between DHRC and SME performance ($\beta = 0.622$; $f^2 = 0.373$, approaching large effect) confirms that organizations capable of continuously learning, integrating diverse knowledge sources, and reconfiguring their human resource routines outperform those that lack such adaptive capacities. This finding aligns with a growing body of evidence that dynamic capabilities are especially consequential in volatile environments (Apascaritei & Elvira, 2022; Gupta et al., 2018; Nguyen et al., 2024; Pillai & Srivastava, 2023; Puhovichova & Jankelova, 2020). In the Indonesian context, where SMEs face frequent disruptions from supply chain shocks to regulatory changes, the ability to rapidly upskill employees, coordinate cross-functional efforts, and redeploy talent to emerging opportunities becomes a key differentiator between survival and failure. Notably, the path coefficient of DHRC on performance is approximately twice that of the direct leadership effect ($\beta = 0.623$ vs. 0.192), suggesting that operationalizing strategic intent through concrete HR routines is more impactful than strategic vision alone—a point we elaborate further below.

Furthermore, the findings further strengthen the mediating role of dynamic human resource capabilities in the relationship between strategic leadership and SME performance. The indirect pathway substantially exceeds the direct pathway, thus underscoring the substantive mediating role of DHRC in transmitting the influence of leadership to SME performance. This pattern offers a plausible explanation for previous inconsistencies, as studies limited to direct effects may systematically underestimate the total influence of leadership by ignoring mediating mechanisms, particularly in SME contexts where formal structures are underdeveloped and leadership is exercised through daily routines (Jalaludin et al., 2024; Quansah et al., 2022). The dominance of the indirect pathway can be attributed to two complementary explanations. First, in resource-constrained environments, leaders rely on employees to translate vision into action through routines of learning, integration, and reconfiguration, in line with the Dynamic Capabilities View's emphasis on managerial cognition shaping dynamic capabilities (Abdeen et al., 2025; Teece et al., 1997). Second, the distinct informal characteristics of Indonesia SMEs imply that leadership influence is maintained through continuous capability building and social integration rather than formal authority, extending previous research on strategic leadership in emerging economic contexts (Kebede et al., 2024; Pitelis & Wagner, 2019). Consequently, leaders who invest in employees' adaptive capacity achieve more sustained performance improvements than those who rely solely on directive decision-making.

Despite the robustness of our findings, the cross-sectional design of this study precludes definitive causal inference. A plausible alternative explanation is reverse causality: SMEs with superior performance may be more likely to attract and retain capable leaders, and their positive performance trajectory may color respondents' evaluations of leadership effectiveness and HR capabilities. This interpretation suggests a virtuous cycle in which performance and leadership quality reinforce each other over time. Future longitudinal research could help disentangle the direction of causality and further validate the mediating mechanism proposed in this study.

Positioning our findings within the broader entrepreneurship literature, we argue that

DHRC serves as a critical micro-foundation for resource bricolage—the creative reconfiguration of existing resources to address new challenges (Baker & Nelson, 2005). In the absence of abundant financial capital, SME owners and managers must rely on human capital development and social integration to sense and seize entrepreneurial opportunities. The learning dimension of DHRC enables continuous skill upgrading, which in turn supports opportunity recognition the ability to identify and exploit market gaps before competitors. The integration capability facilitates the coordination of diverse knowledge sources, essential for developing innovative products and services with limited resources. The reconfiguration capability underpins organizational resilience, allowing SMEs to pivot their business models in response to external shocks—a capacity vividly illustrated during the COVID-19 pandemic, when many Indonesia SMEs survived by rapidly shifting to digital platforms and adjusting their workforce deployment.

Despite the robustness of our findings, we acknowledge that unobserved heterogeneity across sectors, provinces, and firm sizes may influence the observed relationships. For instance, manufacturing SMEs may prioritize reconfiguration capabilities differently than culinary or service firms, while SMEs in DKI Jakarta face distinct digitalization pressures compared to those in Central Java. Similarly, the role of the respondent—whether owner or manager may affect perceptions of strategic leadership and HR capabilities. While we controlled for firm size statistically and reported these descriptive differences in Table 1, our sample size precluded a more granular moderation analysis. Future research with larger, more balanced samples could explore these contextual factors as potential moderators of the strategic leadership–performance relationship.

Thus, beyond confirming theoretical predictions, this study offers practical guidance for SME owners and managers in emerging economies: invest in building adaptive HR routines not through costly formal systems, but through leader-modeled behaviors such as regular knowledge-sharing sessions, cross-training, inclusive decision-making, and flexible role assignments. Policymakers should consider supporting SME capability-building programs that emphasize leadership development and HR capability enhancement, particularly in regions where access to formal management training is limited.

4. CONCLUSIONS AND SUGGESTION

This study provides evidence of dynamic human resource capability (DHRC) partially mediating the relationship between strategic leadership (SL) and SME performance, extending the Dynamic Capabilities View within the under-explored context of SMEs in developing economies. While the indirect relationship is statistically significant and theoretically consistent with the Dynamic Capabilities View, it should be interpreted as an association rather than a causal effect, given the cross-sectional design of this study. The findings, based on 287 SME owners and managers in Java, demonstrate that DHRC encompassing learning, integration, and reconfiguration routines serves as a critical conduit for leadership influence on SME performance. For practitioners, this underscores the importance of investing in adaptive human resource capabilities, particularly in resource-constrained and informal settings where formal systems are weak, as such investments offer a more sustainable pathway to performance enhancement than directive leadership alone. Several limitations warrant acknowledgment: the cross-sectional design precludes causal inference; self-reported, single-source data may introduce common method bias; purposive sampling limits generalizability; empirical overlap between SL and DHRC raises conceptual concerns; subjective performance measures and geographic concentration on Java further constrain applicability. Future research should employ longitudinal designs, multi-source data, objective performance indicators, and cross-regional or cross-sectoral comparisons to strengthen causal claims and contextual understanding, while exploring moderators such as environmental dynamism or organizational culture.

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