

The Effectiveness of Capabilities and Malaysian SMEs' Performance: Mediated by Innovation

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Abstract

Purpose: The Malaysian government has set ambitious targets for economic expansion. SMEs, being the backbone of the economy, are essential contributors to the country's overall growth, making substantial contributions to the GDP. SMEs are vital in generating employment opportunities, promoting innovation, and contributing to national revenue. However, there are numerous challenges hinder SMEs from increasing export activities in the global market. This study aims to identify the capabilities that can enhance Malaysian small and medium enterprises' export performance. **Design/methodology/approach:** This study employs contingency theory together with resource-based and market-based perspectives to provide a multidimensional understanding of the issue. By combining these approaches, the research highlights how organizational performance is not only shaped by internal resources and capabilities but also influenced by external market conditions and contextual factors. **Findings:** The study contributes valuable insights that enable organizations to evaluate their current practices, adopt innovative approaches, and refine their strategic decision-making processes, which in turn enhances efficiency and leads to stronger export outcomes. **Research limitations/implications:** This research seeks to fill the existing gap in the literature by examining how the capabilities of Malaysian SMEs influence their export performance, while also investigating the role of innovation as a mediating factor that links organizational strengths with international success. **Practical implications:** The study provides valuable implications for SMEs by showing how systematic improvements in decision-making during export activities can translate into better performance in international markets. It further establishes that capability enhancement serves as a fundamental factor influencing the overall export competitiveness of SMEs. **Originality/value:** To bridge the existing research gap concerning the export performance of SMEs, this study seeks to establish a holistic conceptual framework. The proposed model positions technological and managerial capabilities and innovation as mediating elements that shape SMEs' ability to perform

effectively in international markets, while simultaneously fostering long-term growth and strengthening competitiveness.

Keywords: Export Performance, Small and Medium Enterprises, Managerial Capability, Technological Capability, Capability, Innovation

Introduction

Small and Medium Enterprises (SMEs) are integral to Malaysia's economic framework, contributing significantly to employment, innovation, and national revenue. According to the National Entrepreneur and SME Development Council (2024), SMEs comprise approximately 1.2 million businesses, accounting for 97.4% of total business establishments. Their economic impact includes 38.4% of the gross domestic product (GDP), 35% of total exports, and 48.2% of national employment. In Malaysia specifically, SMEs represent 98.5% of all business entities, underscoring their role in driving GDP and labour market participation (Lim & Teoh, 2021).

The onset of the Fourth Industrial Revolution (IR 4.0) and the rapid pace of digital transformation have introduced both opportunities and challenges for SMEs. While digital technologies offer avenues for operational efficiency and market expansion, many SMEs face barriers such as limited digital infrastructure and inadequate strategic planning. Sharma, Kraus, Talan, Srivastava, and Theodoraki (2024) argue that the COVID-19 pandemic intensified these challenges, compelling SMEs to accelerate digital adoption and reevaluate business models to ensure long-term sustainability.

As global markets become increasingly competitive and technologically advanced, the performance and sustainability of SMEs hinge on their ability to leverage internal capabilities particularly managerial and technological competencies.

Managerial capabilities refer to the strategic, operational, and leadership skills that enable firms to navigate complex environments, allocate resources effectively, and foster innovation. Technological capabilities, on the other hand, encompass the ability to adopt, integrate, and utilize digital tools and systems to enhance productivity and market responsiveness. Both dimensions are critical in shaping organizational agility and long-term performance outcomes (Khaw & Chelliah, 2023).

Technological capability refers to a firm's ability to acquire, assimilate, and apply digital tools and systems to enhance operational efficiency, product quality, and market responsiveness. For SMEs, this includes the adoption of information and communication technologies (ICT), automation, and digital platforms that facilitate internationalization and cross-border transactions. Empirical evidence suggests that SMEs with strong technological capabilities are better positioned to identify export opportunities, manage logistics, and comply with international standards, thereby improving their export performance (Khaw & Chelliah, 2023).

Despite its importance, many Malaysian SMEs face challenges in leveraging technology for export growth. These include limited financial resources, inadequate digital infrastructure, and a lack of skilled personnel. Addressing these barriers is essential for enhancing Malaysia's export competitiveness, especially in the context of regional integration initiatives such as the

ASEAN Economic Community (AEC), which aim to create a unified and dynamic trade environment.

Innovation serves as a mediating mechanism that translates these capabilities into tangible performance gains. Empirical studies have shown that SMEs with strong managerial and technological foundations are more likely to innovate successfully, thereby improving financial performance, customer satisfaction, and competitive positioning (Singh & Hanafi, 2020). However, the extent to which innovation mediates the relationship between capabilities and performance remains underexplored in the Malaysian context.

Export performance is a critical indicator of competitiveness and sustainability for Small and Medium Enterprises (SMEs), particularly in emerging economies such as Malaysia. As globalization intensifies and regional trade agreements expand, SMEs are increasingly expected to contribute to national export growth. In Malaysia, SMEs account for approximately 35% of total exports, reflecting their strategic role in international trade (National Entrepreneur and SME Development Council, 2024).

For SMEs, achieving strong export performance is often contingent upon internal capabilities, including managerial expertise, technological readiness, and innovation capacity (Awang Tuah et al., 2021). These capabilities enable firms to identify foreign market opportunities, adapt products to international standards, and manage cross-border operations effectively. This study explores the determinants of export performance among Malaysian SMEs, with a particular focus on how technological and managerial capabilities with mediated by innovation toward the enhancement of export performance.

Literature Review

Small and Medium Enterprises (SMEs)

According to Yuena and Nga (2020), small and medium-sized enterprises (SMEs) are among the key contributors to Malaysia's economy, accounting for approximately 98.5 percent of overall economic activities. Many large corporations originate as SMEs, highlighting their role as the foundation for future business growth. The success of SMEs can therefore act as a catalyst for the advancement of larger organizations, strengthening industrial networks and supply chains. Similarly, Hanifah, Hasliza, Hazlina, and Ali (2019) reported that more than 99 percent of businesses in Malaysia fall under the SME category, further underscoring their dominance in the national business landscape. In addition, Zalina, Firdaus, and Azman (2016) emphasized that SMEs serve as major contributors to Malaysia's economic development. Their presence not only supports employment and innovation but also enables larger organizations to effectively meet the growing demand and supply of goods and services, thereby reinforcing the interconnectedness of SMEs and large enterprises in sustaining Malaysia's economic progress.

Export Performance

Export performance plays a pivotal role in the strategic operations of businesses, serving as a key indicator of organizational effectiveness and competitiveness. Improving export outcomes is often a central objective for firms seeking to enhance managerial efficiency and expand market reach. Through the assessment of export performance, companies can gauge their operational maturity and international readiness. As noted by Ribau, Moreira, and

Raposo (2017), export activities are widely recognized as essential contributors to national economic growth and societal well-being.

Recent data underscores the growing importance of Malaysian SMEs in global trade. In 2024, Malaysian Micro, Small, and Medium Enterprises (MSMEs) recorded a 31.3% increase in exports, contributing RM196.8 billion to the national export total—up from RM146.8 billion in 2023. This surge elevated their share of national exports from 12% to 14.3% within a year, with much of the momentum driven by tourism-linked services and digital platforms that enabled broader market access.

Managerial Capability

Managerial capabilities are increasingly recognized as a cornerstone of organizational adaptability and strategic execution. Bamel and Bamel (2018) conceptualized managerial capability as the skilful reconfiguration of existing resources to serve new strategic purposes, highlighting the importance of resource fluidity in dynamic environments.

Eisenhardt and Martin (2010) emphasized that managerial capabilities are inherently path-dependent, evolving through a firm's historical decisions and strategic choices. This view aligns with more recent findings by Supramono, Damayanti, and Adhitya (2025), who argue that dynamic managerial capabilities play a pivotal role in accelerating performance recovery and ensuring long-term sustainability.

Managers are not only responsible for setting strategic direction but also for orchestrating the alignment of organizational resources, culture, and capabilities to support technological change. Cortellazzo et al. (2019) and Wrede et al. (2020) underscored this foundational role, noting that effective leadership is essential for navigating the complexities of digital innovation.

Sacavém et al. (2025) argue that in the face of accelerated technological disruption, managers must possess adaptive leadership skills and a deep understanding of change processes to successfully integrate digital tools and foster innovation.

Technological Capability

Technological capability is increasingly recognized as a strategic asset for small and medium enterprises (SMEs), enabling them to innovate, compete, and adapt in rapidly evolving markets. Technological innovation and the widespread use of digital platforms have played a transformative role in accelerating the expansion of the global digital economy. As Aggarwal (2023) observed, digital technologies have become central to economic growth, enabling businesses to scale rapidly and engage with global markets more efficiently.

Ramachandran, and Yusof (2023) emphasized that Malaysian SMEs often struggle with technology adoption due to financial constraints and limited technical expertise. However, firms that successfully leverage technology tend to exhibit higher innovation output and resilience in volatile markets. Lua and Shaharudin (2024) further argue that digital transformation enhances SMEs' innovation and dynamic capabilities, helping them overcome resource constraints and respond effectively to market shifts. For Malaysian SMEs, investing

in digital infrastructure, workforce upskilling, and adaptive leadership is essential to fully leverage technological potential and drive export performance.

Innovation

Innovation is widely recognized as a strategic activity aimed at enhancing the value, functionality, and effectiveness of products, processes, and organizational procedures. Hanifah (2021) emphasizes that innovation involves deliberate efforts to refine and improve existing offerings, thereby increasing their relevance and performance in competitive markets. This perspective aligns with the broader understanding of innovation as a driver of continuous improvement and operational excellence. Easa and Orra (2021) assert that innovation is not merely an optional strategy but a foundational prerequisite for organizational growth and adaptability. It enables firms to respond to changing market demands, embrace digital transformation, and sustain long-term development. Yusr et al. (2022) demonstrated that innovation mediates the relationship between organizational capabilities and product performance in Malaysian SMEs. Similarly, Singh and Hanafi (2020) highlighted that innovation capacity is a key predictor of financial and operational success.

Proposed Theoretical Framework

Proposed Theoretical Framework The proposed framework consists of three constructs. There are variables (IV), namely technological capability and managerial capability while export performance works as the dependent variable (DV) in the study. At the same time, innovation works as the mediator of the study. Based on the past research, P1, P2, and P3 are developed to understand the relationship between capabilities and export performance among SMEs in Malaysia.

Proposition 1: Managerial capability shows a positive relationship with export performance among SMEs in Malaysia.

Proposition 2: Technological capability exhibits a positive relationship towards export performance among SMEs in Malaysia.

Proposition 3: Innovation demonstrates a significant mediating relationship with export performance among SMEs in Malaysia.

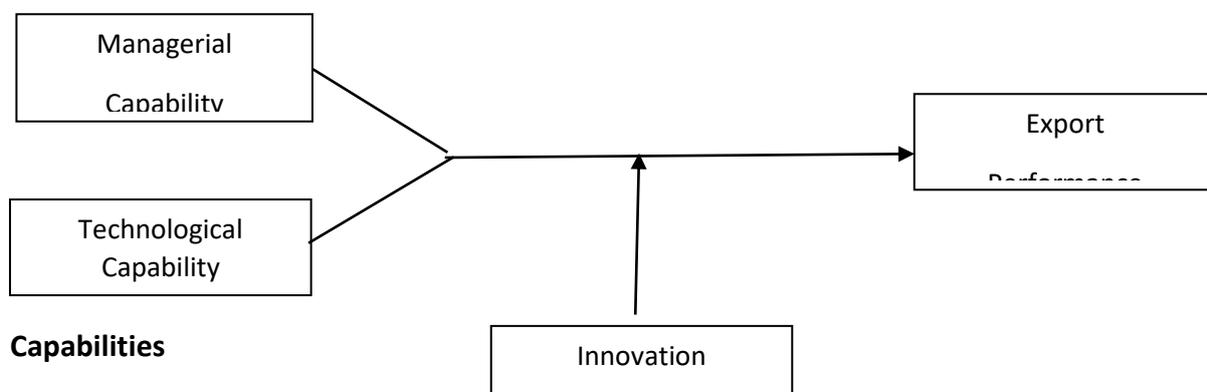


Figure 1 Conceptual Framework of Capabilities and Business Performance among SMEs in Malaysia

Methods

An extensive review of academic databases was undertaken to gather relevant literature that supports this research. The review primarily focused on factors influencing SMEs' export performance and their sources of competitive advantage. Several scholarly databases, including *ScienceDirect*, *utmj.org*, *nih.gov*, *nchi.edu.tw*, and *Palgrave Journals*, were systematically examined. Keywords such as *export performance*, *small and medium enterprises*, *managerial capability*, and *technological capability* were employed to retrieve the most pertinent studies.

In addition to these databases, academic resources were also accessed through *Google Scholar* and institutional databases such as *Web of Science* and *Scopus*. These platforms provided a comprehensive body of peer-reviewed literature relevant to the research objectives. Furthermore, scientific research repositories including *ScienceDirect*, *SAGE Publications*, and *tamu.edu* were consulted to identify and refine the variables incorporated in the conceptual model.

To ensure the accuracy and reliability of data, a diverse set of secondary sources was also analysed. These included government publications, industry reports, market research studies, media coverage, and credible internet sources, particularly those relating to Malaysian SMEs' export performance. Emphasis was placed on selecting high-quality, peer-reviewed scientific literature to guarantee the robustness of the conceptual framework and the validity of the study's findings.

Discussion and Conclusion

This study set out to examine how different managerial capabilities and technological capabilities when mediated by a innovation, influence the export performance of small and medium-sized enterprises (SMEs) in Malaysia. The findings underscore the crucial role of food processing SMEs in strengthening Malaysia's competitive position in international markets. By identifying key factors that drive performance, this research provides a benchmark that SMEs can use to enhance both quality and competence, enabling them to remain competitive in the global arena.

More specifically, the study demonstrates that focusing on critical capabilities—such as managerial capability and technological capability—can significantly improve export outcomes. For SMEs that aspire to expand beyond domestic boundaries, these findings act as a practical guideline, illustrating how strategic capability-building can translate into stronger performance. Moreover, the study highlights the mediating effect of innovation, offering a clearer understanding of how international perspectives shape the link between internal capabilities and export success.

Beyond practical implications, this research contributes to the academic literature by enriching discussions on the role of capabilities in export performance, particularly within the Malaysian SME context. When these capabilities are properly leveraged, SMEs are not only likely to achieve higher performance but also to sustain long-term growth in increasingly competitive markets.

Finally, this study serves as a useful reference point for future researchers. It provides valuable insights that can guide subsequent investigations into the interplay between managerial capabilities, technological capabilities, innovation, and international performance. In doing so, it establishes a solid foundation for continued inquiry and opens new pathways for both theoretical advancement and practical application in the field of SME internationalization.

The findings of this research are expected to provide meaningful insights for SMEs in Malaysia and could potentially serve as a valuable reference for business consulting practices tailored to their needs. Through the study, a conceptual model will be developed to identify the key organizational and managerial capabilities that are most critical for SMEs to achieve success and enhance their export performance. This framework not only highlights the capabilities necessary for competitiveness but also offers practical guidance for SMEs seeking to effectively enter and sustain a presence in international markets.

Moreover, the outcomes of this study shed light on the broader role of global capabilities in shaping business performance, emphasizing that the development of such capabilities is essential for SMEs aspiring to internationalize. By deepening the understanding of how innovation interacts with organizational strengths, the study contributes to both managerial practice and academic discourse. Ultimately, the insights generated can empower Malaysian SMEs to strengthen their strategies, overcome internationalization barriers, and position themselves more competitively on the global stage.

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