

Market Orientation and Sharia Product Knowledge on Business Performance: Innovation Capability as an Intervening Variable in Sharia Banking Industry

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Abstract

Purpose - This study investigates the influence of market orientation and Sharia product knowledge on business performance in the Sharia banking industry, with innovation capability as an intervening variable.

Method - Quantitative approach, the research employs Structural Equation Modeling Partial Least Squares (SEM PLS) to analyze data collected from a saturated sample of 213 permanent employees of PT Bank Muamalat, Central Java Regional Office.

Result - The findings reveal that both market orientation and Sharia product knowledge significantly and positively impact business performance. Furthermore, innovation capability also demonstrates a positive and significant effect on business performance. The results confirm that innovation capability effectively serves as an intervening variable, strengthening the relationship between market orientation, Sharia product knowledge, and business performance. All five hypotheses tested in the study were supported, indicating the critical role of market orientation and Sharia product knowledge in enhancing innovation capability, which in turn improves business performance in the Sharia banking sector.

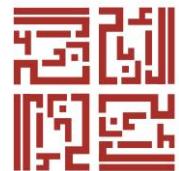
Implication - These findings highlight the importance of aligning market strategies with Sharia principles and leveraging innovation to achieve competitive advantages in the dynamic banking industry.

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Originality - This research contributes to the growing literature on Sharia banking by providing empirical evidence of the interplay between market orientation, Sharia product knowledge, and innovation capability. It underscores the necessity for Sharia banks to prioritize knowledge dissemination and innovative practices to sustain performance in a competitive market. Future research is recommended to explore other potential variables that may mediate or moderate these relationships.

Keywords: Market Orientation, Sharia Product Knowledge, Business Performance, Innovation Capability, Sharia Banking



Introduction

The Sharia banking industry in Indonesia has been experiencing significant growth, driven by increasing public awareness of the importance of conducting economic activities in compliance with Sharia principles (Iryani & S.F, 2021). As one of the countries with the largest Muslim population in the world, Indonesia has great potential to develop Sharia banking as an engine of justice-based economic growth. However, this growth still faces challenges, particularly in improving competitiveness and business performance (Haidar, 2022; Nasution et al., 2020; Syafrizal, 2019). In this context, the implementation of market orientation strategies and the enhancement of Sharia product knowledge become urgent needs.

Market orientation, which focuses on a deep understanding of consumer needs and preferences, is believed to drive business performance (Soeherman & Panjaitan, 2022). In the Sharia banking sector, market orientation must be translated into strategies that not only aim for profit but also reflect Sharia values. This presents its own challenges as Sharia banking customers have unique expectations regarding the products and services they use. On the other hand, Sharia product knowledge is a critical factor in building trust and customer loyalty. Adequate knowledge of Sharia-based products, such as murabahah, ijarah, and mudharabah, enables banking employees to provide more effective services (Nurcahyo, Jannah, et al., 2024). This knowledge is not only relevant to front-line employees but also to all levels of management to ensure that all implemented strategies remain aligned with Sharia principles (Risqina et al., 2020).

However, to enhance business performance, market orientation and Sharia product knowledge need to be supported by innovation capability. This capability reflects an organization's capacity to create, adapt, and implement innovations in products, services, and business processes (Freixanet et al., 2018). In a highly competitive industry like Sharia banking, innovation is a determining factor for sustainability and competitive advantage. Organizational culture plays a pivotal role in fostering innovation capability within the Sharia banking industry (Alma et al., 2024). A culture that

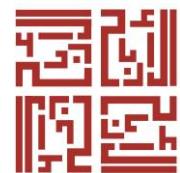


encourages creativity, risk-taking, and continuous learning can significantly enhance an organization's ability to innovate. For Sharia banks, aligning organizational culture with Sharia principles while promoting innovation creates a unique dynamic (Nurcahyo, Isnawati, et al., 2024; Soeherman & Panjaitan, 2022). This balance ensures that innovative practices not only meet market demands but also adhere to ethical and religious values, offering a distinct competitive advantage.

The integration of digital technology has become an indispensable part of enhancing innovation capability in Sharia banking. From mobile banking applications to AI-driven customer service tools, digital transformation allows banks to improve operational efficiency and customer experience (Orlova, 2021). By leveraging technology, Sharia banks can create tailored products that meet customer needs while maintaining compliance with Sharia principles. This approach not only improves customer satisfaction but also drives business performance in an increasingly digitalized market (Novia et al., 2020).

Table 1. Sharia Bank Growth Data

Category	Data/Information	Internal Data Source
Asset Growth	PT Bank Muamalat Kanwil Jawa Tengah's assets grew by 10% in 2023 compared to 2022.	PT Bank Muamalat Kanwil Jawa Tengah Financial Report (2023)
Financing Growth	Sharia financing increased by 12% in 2023, focusing on housing and MSME financing.	PT Bank Muamalat Kanwil Jawa Tengah Financing Report (2023)
Profit Growth	Pre-tax profit increased by 9.3% in 2023.	PT Bank Muamalat Kanwil Jawa Tengah Financial Report (2023)



New Customer Growth	PT Bank Muamalat Kanwil Jawa Tengah added 15% new customers in 2023.	PT Bank Muamalat Kanwil Jawa Tengah Customer Development Report (2023)
Digital Banking Growth	30% increase in digital transactions (mobile banking and internet banking) in 2023.	PT Bank Muamalat Kanwil Jawa Tengah Digital Banking Report (2023)
New Sharia Products	5 new sharia products launched in 2023, including sharia-compliant investment products.	PT Bank Muamalat Kanwil Jawa Tengah Products and Services Report (2023)
Sharia Banking Market Share	Bank Muamalat's market share in the sharia banking sector reached 3.5% in 2023, with significant growth in Central Java.	PT Bank Muamalat Kanwil Jawa Tengah Market Analysis Report (2023)
Customer Satisfaction	80% of customers rated PT Bank Muamalat Kanwil Jawa Tengah's sharia products and services positively.	PT Bank Muamalat Kanwil Jawa Tengah Customer Satisfaction Survey (2023)
Capital Increase	PT Bank Muamalat Kanwil Jawa Tengah's capital increased by 7% in 2023, supporting the expansion of sharia services and products.	PT Bank Muamalat Kanwil Jawa Tengah Financial Report (2023)
Digital Service Growth	25% of total financing services are now provided digitally through mobile applications.	PT Bank Muamalat Kanwil Jawa Tengah Digital Services Report (2023)

Source : Oprational Division Banking Muamalat Central Java, 2024

The table 1. above provides an overview of the growth data for PT Bank Muamalat Kanwil Jawa Tengah, focusing on key performance indicators that reflect the bank's progress in the Sharia banking sector in 2023. It includes categories such as asset growth, financing growth, and profit growth, showing positive trends in the bank's financial performance. The data reveals that the bank's assets grew by 10% compared to the previous year, highlighting its solid financial standing and successful expansion strategies.



Additionally, the table emphasizes the growth in financing, particularly in Sharia-compliant financing for housing and micro, small, and medium enterprises (MSMEs). The bank saw a 12% increase in Sharia financing, indicating a strong demand for these services. This growth aligns with the bank's focus on expanding its financing portfolio, especially targeting sectors that contribute to the economic development of the region. The table also includes data on new customer acquisition, with PT Bank Muamalat Kanwil Jawa Tengah reporting a 15% increase in new customers in 2023. This growth reflects the bank's effective customer development strategies and its expanding market reach. Furthermore, the increase in customer satisfaction, with 80% of customers rating the bank's products and services positively, demonstrates the bank's success in delivering quality and customer-centric offerings.

Finally, the table highlights significant advancements in the bank's digital banking services, with a 30% increase in digital transactions. The launch of new Sharia products, including investment options, and the bank's 7% increase in capital demonstrate the bank's continuous innovation and commitment to enhancing its services. These positive trends underline PT Bank Muamalat Kanwil Jawa Tengah's strong position within the Sharia banking industry and its sustained efforts to improve customer experience and operational efficiency.

The Sharia banking industry faces intense competition, not only from conventional banks but also from fintech and digital financial platforms (Suseno & Muthohar, 2018). This competition necessitates the development of strategies that emphasize both compliance with Sharia principles and business excellence. By focusing on market orientation and innovation capability, Sharia banks can position themselves as market leaders capable of meeting customer needs while adhering to ethical standards (Pathak, 2017). This dual approach is vital in sustaining their market relevance and achieving long-term profitability. Human resource development is a critical aspect of achieving superior business performance in Sharia banking. Employees equipped with in-depth Sharia product knowledge can better serve customers and align their



work with organizational goals (Marditama et al., 2024). Regular training programs focused on both Sharia compliance and innovative thinking can empower employees to contribute to the bank's strategic objectives. This, in turn, enhances the overall effectiveness of market orientation strategies and strengthens the bank's competitive position.

Sharia governance plays a crucial role in ensuring that innovation efforts in Sharia banking remain compliant with Islamic principles (Ramadhan, 2015). The presence of Sharia advisory boards helps guide the development of new products and services, ensuring they align with ethical standards. Effective Sharia governance not only safeguards the bank's reputation but also builds trust among customers and investors, reinforcing the bank's position in the market.

Literature Review

Market Orientation

Market orientation refers to a business philosophy and strategic approach that focuses on understanding and responding to the needs, preferences, and behaviors of customers in order to create value and maintain a competitive advantage (Midhat Ali et al., 2021; Rashid, 2012). It involves continuously gathering market intelligence and using it to shape product development, marketing strategies, and customer service. Market orientation emphasizes customer satisfaction as the core driver of business performance and seeks to align all departments within the organization towards achieving customer-centric goals (Helme-Guizon & Magnoni, 2019).

At its core, market orientation is about being proactive rather than reactive to market changes. It involves systematically analyzing consumer trends, competitor actions, and environmental factors to anticipate shifts in demand. By being attuned to the market, organizations can better tailor their offerings to meet evolving customer needs, ensuring long-term business success and sustainable competitive advantage (Hussain, 2020).

Furthermore, market orientation requires a deep commitment to customer relationships, with a focus on creating value through product quality,



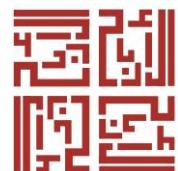
service excellence, and innovation. It encourages firms to involve employees at all levels in understanding and meeting customer demands. This customer-centric culture drives continuous improvements in product offerings, enhances customer loyalty, and ultimately improves organizational performance (Faeni, 2024). In the context of Sharia banking, market orientation becomes even more crucial as customers increasingly seek services that align with Islamic principles. Sharia-compliant financial products must not only meet the financial needs of customers but also adhere to ethical standards and promote social responsibility (Ibrahim et al., 2017). As such, Sharia banks need to adopt a strong market orientation to differentiate themselves, attract new customers, and build trust within a competitive and growing industry.

Innovation Capability

Innovation capability refers to an organization's ability to develop new products, services, and processes that meet market demands and enhance its competitive position (Wikaningrum & Kartikasari, 2023). It involves the capacity to generate creative ideas, implement them effectively, and adapt to changes in the business environment. Innovation capability is critical for companies seeking to maintain long-term growth, as it enables them to stay ahead of competitors and respond to evolving consumer needs (Nurcahyo, Widagdo, et al., 2024).

For a business to successfully innovate, it requires a supportive culture that encourages risk-taking and experimentation. This includes having the right resources, such as skilled personnel, technology, and financial investment, to turn innovative ideas into tangible outcomes (Nurcahyo, 2024). Additionally, a strong innovation capability is built upon collaboration and the exchange of ideas across different departments and stakeholders, ensuring that new solutions align with both internal capabilities and market demands (Risqina et al., 2020).

In the context of Sharia banking, innovation capability is essential for introducing new financial products and services that meet the needs of

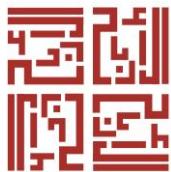


customers while adhering to Islamic principles. This capability allows banks to create Sharia-compliant solutions that cater to both the ethical and financial requirements of their customers (Zaichkowsky, 2016). It also enables them to differentiate themselves in a competitive market by offering unique, value-driven services that attract and retain loyal customers. Moreover, a well-developed innovation capability can improve operational efficiency by streamlining processes, integrating advanced technologies, and enhancing customer experiences. Sharia banks, for instance, can leverage digital platforms to offer convenient, accessible services while maintaining compliance with religious guidelines (Khan, 2020). This innovation-driven approach not only strengthens the bank's market position but also contributes to the overall growth of the Sharia banking industry.

Sharia Product Knowledge

Sharia product knowledge refers to the understanding and awareness of financial products and services that comply with Islamic principles, which prohibit activities such as charging interest (*riba*), gambling (*maysir*), and uncertainty (*gharar*). In the context of Sharia banking, this knowledge includes not only the features and benefits of these products but also the ethical considerations and guidelines that make them compliant with Islamic law (Bouteraa et al., 2020). Sharia product knowledge is essential for both banking professionals and customers, as it ensures that financial transactions and investments align with Islamic values (Aisyah, 2018).

For banking professionals, having comprehensive Sharia product knowledge is crucial for offering accurate advice and recommendations to customers. It enables them to clearly explain the differences between conventional financial products and Sharia-compliant alternatives (Qurrata et al., 2021). This knowledge helps build trust with clients, as they rely on the expertise of the bank to provide solutions that adhere to their religious beliefs while also meeting their financial needs. For customers, understanding Sharia-compliant products is important in making informed financial decisions that align with their ethical and religious values (Süß & Kretzschmar, 2018). With



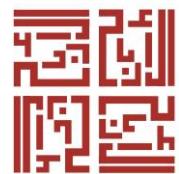
growing interest in ethical banking, many customers are increasingly seeking products that not only provide financial returns but also adhere to Islamic principles of fairness, transparency, and social responsibility. This makes Sharia product knowledge a key factor in the success and growth of Islamic financial institutions, as it helps attract and retain customers who are committed to ethical investing (Nurcahyo, Anis, et al., 2024).

Moreover, Sharia product knowledge extends beyond just individual products. It involves understanding the broader regulatory framework governing Islamic finance, including the various contracts and principles such as mudarabah (profit-sharing) and murabaha (cost-plus financing). By fostering a deep understanding of these principles, banks can better innovate and develop new products that meet the needs of their customers while ensuring compliance with Sharia law (Auda Jaser, 2008). This in turn strengthens the credibility and sustainability of the Islamic banking sector.

Business Performance

Business performance refers to how effectively a company achieves its objectives, utilizing available resources to create value and generate profits (Nart et al., 2024). It is a comprehensive evaluation of various key indicators, including financial performance, market share, customer satisfaction, operational efficiency, and employee performance (Naini et al., 2022). Business performance helps stakeholders, such as investors, managers, and employees, assess the company's success and identify areas for improvement. Key metrics often include profitability ratios, revenue growth, return on investment (ROI), and cost management.

In the context of Sharia banking, business performance is measured not only in terms of financial success but also through the adherence to Islamic principles. This includes ensuring that products and services comply with Sharia law, creating value for customers while avoiding unethical practices such as riba (interest) or maysir (gambling). For Sharia banks, business performance involves achieving a balance between financial growth and maintaining the ethical standards prescribed in Islamic finance, which is



crucial for attracting and retaining customers who prioritize these values. Effective business performance in Sharia banks also requires strong customer relationships, innovation in product offerings, and a commitment to social responsibility (Oktaviana & Miranti, 2023). In addition to financial metrics, Sharia banks measure their success by the extent to which they meet the needs of their customers in a way that reflects Islamic principles. For example, they might track the uptake of new Sharia-compliant products, customer satisfaction levels, or the ability to meet financing demands in a socially responsible manner (Yasa et al., 2017). Furthermore, business performance in this sector is often closely linked to market orientation and innovation capability. A strong market orientation ensures that the bank's products align with customer needs, while innovation capability allows the bank to continuously develop new, relevant, and Sharia-compliant solutions. Together, these factors enhance the bank's ability to compete in the market, improve customer loyalty, and drive long-term sustainable performance (Lasuin, 2016).

Hypothesis

The Influence Of Innovation Capability Toward Business Performance.

The influence of innovation capability on business performance is profound, as it directly impacts a company's ability to adapt, grow, and maintain a competitive edge in a rapidly changing market (Putri et al., 2024). Innovation capability refers to the ability of a business to develop new products, services, or processes that improve its offerings and meet evolving customer demands. A strong innovation capability enables organizations to respond to challenges and capitalize on new opportunities, which is crucial for sustaining business performance over time (Fawehinmi et al., 2020).

In the context of business performance, innovation capability can lead to enhanced operational efficiency, increased market share, and higher profitability. When a company develops innovative solutions, it not only differentiates itself from competitors but also attracts more customers by meeting their specific needs more effectively. In turn, this drives revenue

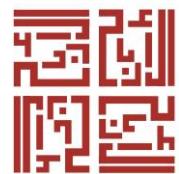


growth and improves customer retention (Tamer Cavusgil et al., 2003). Moreover, innovation capability allows a business to streamline processes, reduce costs, and optimize resource utilization, which contributes to overall organizational efficiency. For Sharia banking institutions, innovation capability plays an equally significant role in improving business performance (AlNuaimi et al., 2021). The ability to develop Sharia-compliant products and services that cater to the financial needs of customers while adhering to Islamic principles enables these institutions to attract a broader customer base. By offering innovative financial solutions such as Islamic investment products, digital banking services, and alternative financing methods, Sharia banks can improve their competitiveness in a market that is increasingly seeking ethical and socially responsible financial options.

H1 : Innovation Capability have a significant effect toward Business Performance

The Influence Of Market Orientation Toward Business Performance.

The influence of market orientation on business performance is crucial, as it directly aligns a company's strategies with customer needs, preferences, and market dynamics (Jawel, 2019). Market orientation refers to an organization's ability to gather, analyze, and respond to market intelligence to create customer value and achieve business goals. By focusing on understanding and meeting the evolving demands of the market, companies can enhance their competitiveness, improve customer satisfaction, and ultimately drive business performance (Soeherman & Panjaitan, 2022). A market-oriented approach leads to improved product development, better customer service, and more effective marketing strategies. Companies that embrace market orientation are better positioned to anticipate customer needs and adjust their offerings accordingly. This results in a stronger market presence, increased customer loyalty, and higher sales performance. Additionally, market orientation helps organizations to quickly adapt to changes in the business environment, such as



shifts in consumer preferences or technological advancements, ensuring that they maintain a competitive edge (Agarwal & Gowda, 2020).

For Sharia banking, market orientation is particularly important as it allows financial institutions to align their offerings with the ethical and religious values of their customers. Understanding the needs of the Muslim population seeking Sharia-compliant products is essential for attracting and retaining customers. By focusing on delivering products that are not only financially viable but also ethically sound, Sharia banks can build trust and foster long-term customer relationships (Haryono, 2018). A strong market orientation helps these banks to introduce innovative products and services that meet the financial and spiritual needs of their customers, thus enhancing business performance.

Moreover, market orientation helps in improving internal processes, as it encourages collaboration across departments to ensure that the customer's voice is heard and acted upon in all aspects of the business (Nurcahyo, Widagdo, et al., 2024). In Sharia banking, this could include the development of new products like ethical investment funds, halal lending options, or digital banking services that align with Islamic values.

H2 : Market Orientation have a significant effect toward Business Performance

The Influence Of Market Orientation Toward Innovation Capability.

The influence of market orientation on innovation capability is significant, as market orientation provides valuable insights that drive an organization's ability to innovate effectively (Akgun, 2015). Market orientation involves actively gathering, analyzing, and responding to customer needs, competitor actions, and broader market trends. This customer-centric approach helps organizations identify gaps in the market, uncover emerging trends, and understand shifts in consumer behavior, all of which are essential for fostering innovation (Alma et al., 2024).



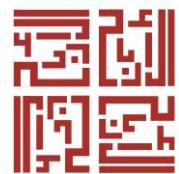
When a company adopts a market-oriented approach, it gains a deeper understanding of the evolving needs and preferences of its target audience. This understanding serves as a foundation for innovation, as organizations can develop new products, services, and processes that are tailored to meet the specific demands of the market (Chayanan, 2019). By staying attuned to market dynamics, companies can identify opportunities for creating innovative solutions that address unmet needs, thus enhancing their innovation capability. Furthermore, a market-oriented culture encourages collaboration across various departments, facilitating the sharing of market insights and ideas that drive creative solutions.

In the context of Sharia banking, market orientation plays a critical role in fostering innovation capability. As customer preferences for Sharia-compliant financial products evolve, banks that actively listen to their customers' needs are better positioned to develop innovative services that align with Islamic principles (Jawaid, 2021). By understanding customer concerns about ethical finance, Sharia banks can design new products such as halal investment opportunities, interest-free financing options, or digital platforms that offer easy access to Sharia-compliant banking. This customer-driven innovation allows banks to differentiate themselves in a competitive market and enhance their ability to attract and retain customers.

H3 : Market Orientation have a significant effect toward Innovation Capability

The Influence Of Sharia Product Knowledge Toward Business Performance.

The influence of Sharia product knowledge on business performance is critical, especially for financial institutions operating in the Islamic finance sector. Sharia product knowledge refers to a deep understanding of financial products that comply with Islamic principles, such as the prohibition of interest (*riba*), gambling (*maysir*), and uncertainty (*gharar*) (Farida, 2012). For Sharia banks, having comprehensive knowledge of these products is essential for offering solutions that align with both financial and ethical standards. This



knowledge enables banks to serve their customers more effectively, fostering trust and enhancing business performance (Nasution et al., 2020).

When employees of a Sharia bank are well-versed in the features, benefits, and principles of Sharia-compliant products, they are better equipped to guide customers toward the most suitable financial solutions (Nurcahyo, Isnawati, et al., 2024). This increases customer satisfaction and loyalty, as clients are confident that the bank's products align with their religious and ethical values. A high level of product knowledge also enables bank staff to effectively communicate the advantages of Sharia-compliant products compared to conventional banking options, helping to attract new customers who are seeking ethical financial services (Firmansyah et al., 2022). As customer satisfaction and loyalty increase, the bank's overall performance improves, driving profitability and long-term growth.

Sharia product knowledge also contributes to business performance by enabling the bank to develop innovative financial products that meet the needs of a diverse customer base. By understanding the specific requirements of customers in different market segments, Sharia banks can create tailored financial solutions, such as Islamic savings accounts, halal investment products, or interest-free loans, that resonate with customers. This innovation leads to enhanced market positioning, as the bank can differentiate itself by offering unique products that meet both financial and ethical needs.

H4 : Sharia Product Knowledge have a significant effect toward Business Performance

The Influence Of Sharia Product Knowledge Toward Innovation Capability.

The influence of Sharia product knowledge on innovation capability is significant, as a deep understanding of Sharia-compliant financial products provides the foundation for developing innovative solutions that align with Islamic principles. Sharia product knowledge encompasses the specific rules, regulations, and ethical guidelines that define Islamic finance, and it plays a critical role in fostering innovation within Sharia banks (Alma et al., 2024). When employees and decision-makers have strong knowledge of Sharia-

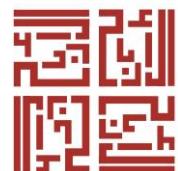


compliant products, they are better equipped to identify opportunities for creating new products and services that meet the needs of customers while adhering to Islamic law (Ahmad Shakir & Iqbal Khan, 2022).

Sharia product knowledge enables banks to innovate within the confines of Islamic finance by providing insights into the ethical and legal requirements that must be respected. This understanding encourages creativity in developing financial products that not only fulfill customer demands but also remain true to the core principles of Islamic finance, such as the prohibition of interest (*riba*), gambling (*maysir*), and uncertainty (*gharar*) (Chen et al., 2022). With a solid grasp of these principles, banks are better positioned to design innovative solutions that serve both the financial and ethical needs of their customer base, setting them apart in a competitive market.

Furthermore, Sharia product knowledge encourages cross-functional collaboration within Sharia banks. Employees from different departments such as product development, marketing, and customer service can work together to create products that integrate Islamic financial principles while meeting market demands. This collaborative approach facilitates the generation of new ideas and the rapid development of innovative financial products, such as Islamic microfinance, halal investment portfolios, or digital banking platforms that comply with Sharia law (Aisyah, 2018). By ensuring that innovation is aligned with both customer needs and Islamic values, banks can maintain their competitive edge in a growing sector of ethical finance. In addition, a strong foundation of Sharia product knowledge helps banks stay ahead of emerging trends in Islamic finance, allowing them to adapt quickly to changing customer preferences and regulatory requirements (Riduan, 2021). This proactive approach to innovation not only enhances the bank's product offerings but also strengthens its market position by ensuring that it remains responsive and adaptable to new opportunities and challenges.

H5 : Sharia Product Knowledge have a significant effect toward Innovation Capability



Methods

The research employs a quantitative approach, utilizing Structural Equation Modeling (SEM) with Partial Least Squares (PLS) to analyze the relationships between market orientation, Sharia product knowledge, innovation capability, and business performance in the context of Sharia banking. SEM-PLS is a robust statistical method that allows for the testing of complex relationships among multiple variables, both direct and indirect, making it an ideal tool for examining the interplay between these constructs (Hair, 2017). The choice of SEM-PLS is based on its ability to handle small to medium-sized sample data and its capacity to assess latent variables, which are critical for understanding the underlying factors that drive business performance in the Sharia banking sector.

The sample for this study consists of 213 permanent employees from PT Bank Muamalat Kanwil Jawa Tengah. The data is collected through structured questionnaires distributed to the selected participants. These employees are chosen because they are directly involved in the bank's operations and have sufficient knowledge of the bank's products, services, and market strategies. The survey instrument is designed to capture data on market orientation, Sharia product knowledge, innovation capability, and perceived business performance, based on established scales from previous research in the field of marketing and Islamic finance.

Table 2. Indicators

Variables	Definition	Indicator	Source
Business performance	The effectiveness of a company in achieving its goals, utilizing available resources to create value and generate profits.	Market share, customer satisfaction, operational efficiency, and employee performance.	(Naini et al, 2022).



Innovation capability	The ability of an organization to develop new products, services, and processes that meet market demands and enhance its competitive position.	The capacity to generate creative ideas, implement them effectively, and adapt to changes in the business environment.	(Nurcahyo, Widagdo, et al, 2024)
Market orientation	A strategy that focuses on understanding and responding to customer needs, preferences, and behavior to create value and maintain competitive advantage.	understanding customers, monitoring competitors, coordinating internally, and responding to market changes.	(Helme-Guizon & Magnoni, 2019; Hussain, 2020; Midhat Ali et al, 2021; Rashid, 2012)
Sharia product knowledge	Understanding and awareness of financial products and services that comply with Islamic principles, which prohibit activities such as interest (<i>riba</i>), gambling (<i>maysir</i>), and fraud (<i>gharar</i>). In the context of	Product features, underlying Sharia principles, and the ability to guide customers	(Auda Jaser, 2008; Süß & Kretzschmar, 2018)



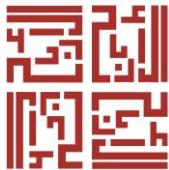
Islamic banking, this knowledge encompasses not only the features and benefits of these products but also ethical considerations and guidelines in accordance with Islamic law.

Data analysis is performed using Smart PLS software, which is specifically designed for SEM-PLS. The analysis includes testing the measurement model for validity and reliability, followed by evaluating the structural model to assess the relationships between the variables (Syaiful, 2018). Hypotheses are tested to determine whether market orientation, Sharia product knowledge, and innovation capability significantly influence business performance. Additionally, the study investigates whether innovation capability acts as an intervening variable between market orientation, Sharia product knowledge, and business performance. The results are expected to provide valuable insights into the factors that contribute to the success and growth of Sharia banking institutions.

Results and Discussion

Outer Model

The outer model assessment focuses on evaluating the reliability and validity of the measurement constructs to ensure the accuracy of the data analysis. This process involves testing the indicators for their factor loadings, composite reliability (CR), and average variance extracted (AVE). Factor loadings above 0.7 indicate that the individual indicators strongly represent their latent constructs, while a CR value above 0.7 confirms internal

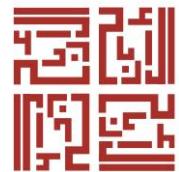


consistency. Additionally, an AVE value above 0.5 demonstrates that the constructs capture sufficient variance from their indicators. The Fornell-Larcker criterion and cross-loadings are also analyzed to confirm discriminant validity, ensuring that each construct is distinct from others in the model. By establishing the reliability and validity of the outer model, the study ensures that the structural relationships tested in the inner model are based on robust measurement constructs.

Table 3. Measurement Evaluation Models

Latent Variables	Convergent Validity		Internal Composite Reliability			Discriminant Validity
	Indicators	Loading	AVE	CR	CA	
		> 0.70	>0.50	>0.70	>0.70	< 1
Market Orientation	X1.1	0.721				
	X1.2	0.749	0.767	0.817	0.810	YES
	X1.3	0.832				
	X1.4	0.714				
Sharia Product Knowledge	X2.1	0.717				
	X2.2	0.737				YES
	X2.3	0.893	0.724	0.895	0.741	
Innovation Capability	Y1.1	0.876				
	Y1.2	0.776	0.812	0.832	0.856	YES
	Y1.3	0.883				
Business Performance	Y2.1	0.746				
	Y2.2	0.823	0.888	0.954	0.920	YES
	Y2.3	0.762				
	Y2.4	0.757				

This research uses Partial Least Square (PLS) to analyze and evaluate the validity and reliability of the model construct using Smart PLS. SmartPLS was carried out to test the Outer Model and Inner Model of the research. The outer model test is carried out to see the validity and reliability of indicators and



variables in the research. This can be seen based on 3 categories, namely (1) Convergent Validity which consists of an outer loading value with a value of >0.7 and an AVE value >0.5 . (2) Internal consistency is seen based on Cronbach's alpha value >0.7 and Composite Reliability with criteria >0.7 . (3) Discriminant validity is seen based on the Fornell-Lacker value where the root value of AVEsquare (diagonal) is greater than all other variable values and HTMT (heterotrait-monotrait correlation ratio) is less than 1. Based on the provisions, indicators and variables in this research can be said to be valid and reliable.

Inner Model

The inner model assessment focuses on evaluating the structural relationships between the latent variables to determine the predictive power and significance of the hypothesized paths. This assessment provides critical insights into the strength and significance of the direct and indirect relationships among the constructs. The findings reveal the extent to which market orientation and Sharia product knowledge directly and indirectly influence business performance through innovation capability. These insights are essential for understanding how Sharia banking institutions can leverage their strategic orientation and knowledge to enhance innovation and drive superior performance outcomes.

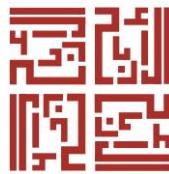


Figure 1. Research Model

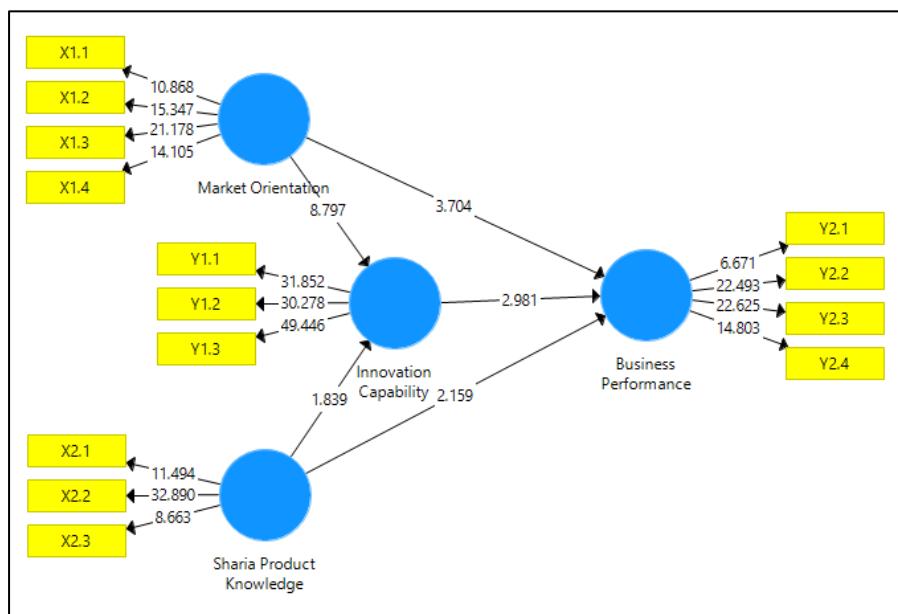
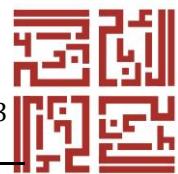


Table 4. Hypothesis Testing

	Original Sample	Sample Mean	Standard Deviation	T-Statistics	P-Value
Innovation Capability>Business Performance	0.309	0.296	0.104	2.981	0.002
Market Orientation>Business Performance	0.456	0.465	0.123	3.704	0.000
Market Orientation>Innovation Capability	0.627	0.626	0.071	8.797	0.000
Sharia Product Knowledge> Business Performance	0.171	0.174	0.079	2.159	0.016



Sharia Product Knowledge> Innovation Capability	0.162	0.170	0.088	1.839	0.033
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Table 5. Mediation Testing

	Original Sample	Sample Mean	Standard Deviation	T-Statistics	P-Value
Market Orientation>Innovation Capability> Business Performance	0.194	0.185	0.068	2.848	0.002
Sharia Product Knowledge>Innovation Capability> Business Performance	0.050	0.051	0.034	1.467	0.071

Based on the hypothesis testing results derived from data collected from 213 permanent employees of PT Bank Muamalat Kanwil Jawa Tengah, the analysis provides substantial insights into the dynamics between market orientation, Sharia product knowledge, innovation capability, and business performance. The findings illustrate the critical interrelationships among these variables and highlight their implications for enhancing organizational performance in the Sharia banking sector.

The first hypothesis establishes that innovation capability positively and significantly influences business performance. With a t-statistic of 2.981 and a p-value of 0.002, this result underscores the pivotal role of innovation in maintaining competitive advantages and achieving superior outcomes. In the dynamic and increasingly competitive Sharia banking industry, innovation capability enables organizations to adapt to market changes, enhance service offerings, and meet customer needs more effectively (Herindar et al., 2021; Monica, 2020; Syafrizal, 2019). This finding reinforces the necessity for Sharia



banks to invest in fostering a culture of innovation and developing systems that support creative problem-solving and technological advancements.

The second hypothesis confirms that market orientation significantly impacts business performance, evidenced by a t-statistic of 3.704 and a p-value of 0.000. This result highlights the importance of adopting a customer-centric approach in strategic decision-making. Market orientation facilitates an understanding of customer needs, competitive positioning, and environmental trends, which are essential for driving business success (Chayanan, 2019; Freixanet et al., 2018; Youn Kue, 2019). For PT Bank Muamalat, this finding suggests that aligning internal processes and strategies with market demands can yield tangible performance benefits, positioning the organization to thrive in a competitive landscape.

Moreover, the third hypothesis reveals a strong and significant relationship between market orientation and innovation capability, with a t-statistic of 8.797 and a p-value of 0.000. This result emphasizes that market orientation is not only crucial for direct performance improvement but also serves as a foundation for fostering innovation. By prioritizing market insights and customer feedback, Sharia banks can stimulate creative solutions and innovative product development, further solidifying their competitive position. For PT Bank Muamalat, this finding underscores the need to integrate market-driven insights into their innovation strategies to achieve sustainable growth (Alma et al., 2024; Julia & Kassim, 2020; Niazi et al., 2023).

The fourth hypothesis demonstrates that Sharia product knowledge positively influences business performance, as indicated by a t-statistic of 2.159 and a p-value of 0.016. This outcome highlights the importance of employee expertise in Sharia-compliant products and services, which forms a core aspect of the bank's value proposition. Employees with a comprehensive understanding of Sharia principles and products are better equipped to communicate value, build trust with customers, and drive performance outcomes (de Abreu Costa & Moreira-Almeida, 2022; Ingvaldsen & Engesbak, 2020; Julia & Kassim, 2020). This finding suggests that PT Bank Muamalat

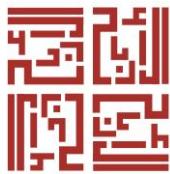


should continue to prioritize training and knowledge enhancement programs to strengthen employee competencies in this area.

The fifth hypothesis shows that Sharia product knowledge positively impacts innovation capability, with a t-statistic of 1.839 and a p-value of 0.033. This result suggests that knowledge of Sharia-compliant principles and products fosters innovative thinking and problem-solving within the organization. Employees equipped with deep product knowledge can identify new opportunities for product and service enhancements, aligning innovation efforts with Islamic banking principles. For PT Bank Muamalat, this underscores the importance of embedding Sharia knowledge into their innovation initiatives (Bestari, 2021; Nurcahyo, 2024; Orlova, 2021).

The mediation testing results provide additional insights into the indirect relationships within the model. The sixth hypothesis confirms that innovation capability mediates the relationship between market orientation and business performance, with a t-statistic of 2.848 and a p-value of 0.002. This finding indicates that market orientation indirectly contributes to improved business performance by enhancing innovation capability. For PT Bank Muamalat, this highlights the strategic importance of fostering innovation as a bridge between market-driven strategies and performance outcomes.

However, the seventh hypothesis, which examines the mediation effect of innovation capability in the relationship between Sharia product knowledge and business performance, is not supported, as evidenced by a t-statistic of 1.467 and a p-value of 0.071. While Sharia product knowledge has a direct effect on both business performance and innovation capability, its indirect effect via innovation capability is not statistically significant. This suggests that the direct application of Sharia knowledge may play a more prominent role in driving performance outcomes, while its contribution to innovation may require further investigation. In conclusion, the results collectively emphasize the strategic significance of market orientation, Sharia product knowledge, and innovation capability in enhancing business performance within the Sharia banking industry. For PT Bank Muamalat, these findings provide actionable insights for improving their strategic focus and operational practices. By

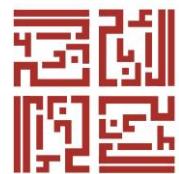


leveraging market insights, enhancing employee knowledge, and fostering innovation, the bank can strengthen its competitive position and achieve sustainable growth in the rapidly evolving financial services landscape.

Conclusion

In conclusion, this study highlights the critical role of market orientation, Sharia product knowledge, and innovation capability in driving business performance within the Sharia banking industry. The findings demonstrate that both market orientation and Sharia product knowledge have a direct and positive impact on business performance, emphasizing the importance of customer-centric strategies and employee expertise in delivering value to stakeholders. Moreover, innovation capability emerges as a crucial factor that not only enhances business performance but also mediates the relationship between market orientation and performance, underlining its role as a bridge between strategic focus and operational success.

The results further reveal that market orientation significantly influences innovation capability, indicating that a deep understanding of customer needs and market dynamics fosters a culture of innovation. Similarly, Sharia product knowledge positively impacts innovation capability, suggesting that expertise in Islamic banking principles enables employees to identify and develop innovative solutions that align with the values and expectations of the Sharia-compliant market. However, the mediating role of innovation capability between Sharia product knowledge and business performance was not statistically significant, pointing to the need for further exploration of this relationship in future research. Overall, the study underscores the need for Sharia banking institutions, particularly PT Bank Muamalat Kanwil Jawa Tengah, to integrate market-driven strategies, enhance employee competencies in Sharia-compliant products, and prioritize innovation as a core strategic objective. By doing so, these institutions can achieve sustainable competitive advantages, adapt to market changes, and continue to deliver superior performance in a highly competitive and dynamic industry. These

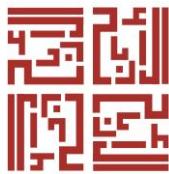


insights provide a foundation for managerial decision-making and strategic planning to foster long-term growth and success.

The findings of this study offer several important implications for the Sharia banking industry, particularly for PT Bank Muamalat Kanwil Jawa Tengah. First, the significant influence of market orientation on business performance and innovation capability suggests that banks must prioritize a customer-focused approach. By continuously monitoring market trends and understanding customer needs, banks can develop strategies that align with both market demands and Sharia principles. This alignment not only improves performance but also fosters innovation, which is essential for maintaining competitiveness in the rapidly evolving financial sector.

Second, the role of Sharia product knowledge in enhancing both business performance and innovation capability highlights the need for continuous investment in employee training and development. Providing staff with in-depth knowledge of Sharia-compliant products ensures that they can deliver superior services and innovate within the framework of Islamic values. This focus on human capital development strengthens the bank's ability to differentiate itself in a crowded market while adhering to ethical and religious standards that resonate with its target audience.

Lastly, the mediation role of innovation capability between market orientation and business performance underscores the importance of embedding innovation as a core organizational competency. While the mediation effect between Sharia product knowledge and business performance was not significant, this finding suggests that innovation capability, while critical, should be complemented by other factors to fully leverage the potential of Sharia product knowledge. Banks must, therefore, adopt a holistic strategy that integrates market orientation, Sharia product expertise, and innovation to achieve sustainable growth and adapt to future challenges in the Sharia banking sector. These implications provide a strategic roadmap for practitioners and policymakers to enhance the industry's resilience and relevance.



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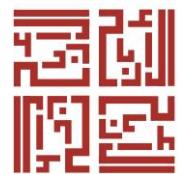
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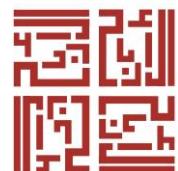
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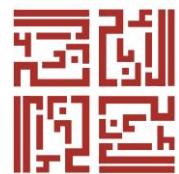
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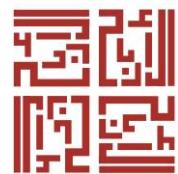
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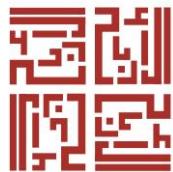
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