

# Performance Improvement Strategy with Dynamic Capabilities in Service and Knowledge Management Aspects in PDAM Jember Regency

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## Abstract

*The purpose of this study is to analyze the influence of resources on dynamic capabilities consisting of service and knowledge management aspects, as well as their effect on company performance at PDAM Kabupaten Jember. Resources are measured by indicators of production efficiency and distribution efficiency, service aspects are measured by indicators of technical services and consumer growth (customers), knowledge management is measured by indicators of the ratio of employees to consumers (customers), the ratio of education and training (training) employees, the ratio of training and education costs, company performance is measured by indicators of ROE, ROA, R and billing effectiveness. Research with SEM-PLS, research period 2011-2019, which is the period after all PDAMs in Indonesia carry out debt restructuring. The results of the study show that resources have a significant influence on aspects of service, knowledge management and company performance. Dynamic capabilities which consist of aspects of service and knowledge management have a significant influence on the company's performance of PDAM Kabupaten Jember. The results also show that dynamic capabilities are important for PDAM Kabupaten Jember to adapt to changes after debt restructuring.*

## Keywords

service aspect, company performance; knowledge management; PDAM resources



## I. Introduction

Several studies have been conducted to see the relationship between knowledge management and organizational performance, but there are still few that examine the practice assessment of knowledge management and then compare it with financial performance with direct indicators. Several previous studies have focused on certain aspects of knowledge management rather than overall, such as linking organizational performance with knowledge, Lee et al., (2005), Harlow (2008) with the level of knowledge in organizations and their effect on organizational performance. Kalling (2003), examines the relationship between knowledge management and performance that stops at performance proxies, such as income proxies, productivity. Choi & Lee (2003) calculate the company's performance. Organization must have a goal to be achieved by the organizational members (Niati et al., 2021). The success of leadership is partly determined by the ability of leaders to develop their organizational culture. (Arif, 2019). Using overall

success, growth rate, market share, profitability and product innovation are proxies of profit, Lin & Tseng (2005) by calculating company performance with 7 items: productivity, cost performance, competitiveness, sales growth, profitability, market and innovation where four is the profit proxy.

In the late 1980s research results showed that financial measures are not only for understanding performance management due to organizational and market improvements as the goal of corporate competition. Kaplan & Norton (2012), show that the Balanced Scorecard (BSC) as a requirement uses a comprehensive performance perspective and its measurements include internal business processes, customer (consumer) knowledge, learning and growth and financial performance. Furthermore (Kaplan & Norton (2012) that managers when making decisions do not only concentrate on finances. The nature of knowledge can force an organization to change new performance indicators.

The most important asset for organizations is intellectual capital and new ways of managing it must be done. There is a paradigm that shows that a good and effective business strategy will be achieved by synergizing knowledge to create new innovations, being able to reduce costs and increase productivity. The funds that have been spent by organizations through information technology investments will be useful in processing knowledge, creating, storing it. There is support from knowledge management to create value, innovation processes and documentation through organizational or company culture. Based

on Law No.23 of 2014, that the implementation of local governments in order to accelerate the realization of community welfare by providing services, empowerment and community participation, to increase regional competitiveness with the principles of democracy and equity. , justice, and the uniqueness of a region. In the context of efficiency and effectiveness in the administration of regional governments, it is necessary to pay attention to aspects of the relationship between the Central Government and the regions, the potential and diversity of regions, as well as the opportunities and challenges of global competition in unity. state administration system.

Regional Drinking Water Company (PDAM) is a form of Regional Owned Enterprise (BUMD) owned by regions that are still bound by existing regulations. PDAM must start thinking about profit, in addition to other things such as service as the main focus, after the issuance of Government Regulation Number 54 of 2017, there are 16 things that need to be followed up from PP. 54 of 2017. Regulations on PDAMs will be prioritized because PDAMs are the most important of the approximately 1,020 existing BUMDs but in terms of profit, PDAM's contribution is the smallest and is a challenge at this time.

In accordance with the President's wish that in order to meet the needs of drinking water for the community in a sustainable manner, it is the obligation of the state. contained in the National Medium-Term Development Plan (RPJMN) 2015-2019. The government accelerates the achievement of universal access to 100% safe drinking water by 2019 through the organization of the drinking water supply system (SPAM). Then the president formed this institution with presidential regulation no. 90 of 2016 concerning the Agency for the Improvement and Implementation of the Drinking Water Supply System (BPPSPAM).

PDAM performance is assessed based on aspects of service, operations, finance, and human resources. Ways to improve PDAM performance by facilitating performance improvement and assisting the preparation of business plans. Regional Drinking Water Company (PDAM) as a regional company engaged in drinking water services in the form

of Regional Owned Enterprises (BUMD) has the potential to be developed, as a source of Regional Original Income. PDAM has goals in the social sector, among others, in providing services for the community to obtain clean water and the existence of business interests to obtain profits which are used to finance company activities and revenue for the region. The purpose of PDAM is to participate in the implementation of regional development and national economic development in general, to provide drinking water that meets health standards, namely clean and healthy water and meets the requirements of the community in an area (Kusuma, 2006).

This situation must be considered by the PDAM management in order to prepare a strategy so that PDAMs can survive and develop, especially during the industrial revolution 4.0 and entering the era of disruption. So that PDAM management must look again at what is used in order to produce quality and better products and services, especially in service to consumers (customers). This can be used by management to evaluate the performance of PDAMs.

PDAM Jember Regency is located in Region II East Java which has been restructuring to improve its performance so that it becomes one of the Regional Owned Enterprises in Jember Regency that contributes to local revenue. Financial performance data before and after restructuring:

**Table 1.** Financial Performance Before Restructuring (2007-2010) and

<b>Indicator</b>	<b>Before</b>	<b>Average After</b>
ROE	-24.50%	-12.60%
ROA (Operating Ratio )	1.08	0.98
CR (Cash Ratio)	666.44%	1151.54%
BE (Billing Effectiveness)	70.77%	91.63%
SC (Service Coverage)	34.95%	39.30%
G (Customer Growth)	3.50%	5.26%
PE (Production Efficiency)	%	62.70%
NRW	32.84 %	28.81%
ER (Employee Ratio)	7.83	6.75
TR (Training Ratio)	28.83%	46.06%
TCR (Training Cost Ratio)	0.90%	1.11%

Source: PDAM Kabupaten Jember, 2021

Based on conditions before and after debt restructuring, PDAM Kabupaten Jember needs to adapt to owned resources so that it can generate value (added value) for PDAM. Dynamic capabilities are needed for the acceleration of PDAM Jember Regency to rise and compete. Several previous research results such as Han & Li (2015); Kaltenbrunner & Renzl (2014); Nuhu et al., (2019) show the importance of dynamic capabilities to improve company performance with different results and become a research gap that can be filled by researchers. The results of Denford (2013) show that the identification of dynamic capabilities is important for businesses to expand their market reach. Based on the results of the study, it is interesting to study and prove the dynamic capabilities based on the service and knowledge management aspects at PDAM Jember Regency as a research update.

## II. Review of Literature

Dynamic ability is one of the models successfully developed by Teece & Pisano (1994) a theory that examines the potential and ability of a group or organization to create, reform or reshape, and still exist in dynamic competition. Based on Teece & Pisano (1994)

in developing a model, it is necessary to study how competitive advantage is obtained and as much as possible maintained. Dynamic capability (Dynamic Capability) consists of the words dynamic about the capacity to revitalize the capability to achieve the target or target with changes in the business environment; among others, by carrying out the necessary innovations, rapid and dynamic technological changes, as well as being difficult to determine from the nature of the market and future competition. Then the word capabilities denote the main functions of strategic management such as adaptation, correlation, and configuration, resources, and functional capabilities of an enterprise.

How effectively dynamic capabilities affect competitive advantage, several researchers have studied the process of operational mechanisms. For example, dynamic capabilities can provide technical knowledge related to the existing knowledge base in changing business activities and dynamically improving operations (Helfat, 1997). This shows that dynamic capabilities can improve the operating system. Therefore, it can adapt to changes influenced by the environment.

Meanwhile, according to Zott (2003) argues that dynamic capabilities are more than just resource-based displays; this is because they reconstruct resources and advantages that can directly generate rent. Dynamic capabilities are indirectly related to company performance with the aim of changing the company's resource pool, operational routines, and competencies, which in turn affect the economic value performance. The strategic conflict approach uses game theory tools and therefore implicitly views competitive outcomes as a function of the effectiveness of firms unbalancing their competitors through strategic investments, pricing strategies, signals, and information controls. Both the competitive forces and strategic conflict approaches seem to share the view that rental prices flow from the market position of a privileged product.

Service quality is the customer's assessment of certain products and services in accordance with expectations that provide satisfaction for them (Al-Jazzazi & Sultan, 2017). Quality corresponds to satisfaction where the highest quality is the consumer's best preference (Yarimoglu, 2014). In order for a company to be able to achieve sustainable and competitive success and advantage, it needs to be oriented towards competitiveness, development and market growth, so it is necessary to pay attention to quality services and achieve customer satisfaction. (Angelova & Zekiri, 2011).

Companies need to evaluate by comparing performance with consumer expectations (customers) as well as with the performance of other companies in the same industry. (Rauch et al., 2015). Maintaining good service quality and developing better integrated systems, it is important to understand customer attitudes (Pakurár et al., 2019).

Knowledge management is a concept and has a broad definition (Ibrahim et al., 2009), from the concept of knowledge management that sharing will result in better performance even though in practice it is not easy for management. The application of knowledge management in each company will be different and not the same, because knowledge itself is a continuous but not systematic flow (Carneiro, 2000). So it is necessary to apply systematic knowledge management that is practically easy to share and apply as a tool to measure performance (Yang et al., 2009).

The practice of knowledge management as an organizational activity consists of four key dimensions and is related to performance: 1. the ability to seek and share existing knowledge; 2. the ability to experiment and create new knowledge; 3. a culture that encourages the creation and sharing of knowledge; and 4. consideration of the strategic value of knowledge and learning Zack et al., (2009).

The definition of knowledge management is a series of processes and techniques for retrieving and using knowledge sourced from databases, research, ideas found in the SiJing organization (2002).

Based on the resource-based theory, the company's performance can be said to be optimal if the company has a competitive advantage and can generate value for the company. While competitive advantage is what the company has that is difficult for competitors to imitate. Competitive advantage can be obtained by managing and utilizing its resources in a good way. Then resource-based theory states that the company is a collection of capabilities to manage the resources it has (Pitelis, 2009).

In order for a company to be able to achieve competitive advantage, Barney & Clark (2008), mentions that it must have:

1. Resources that have a positive value for the organization.
2. Resources are unique compared to the resources owned by competitors.
3. Resources cannot be replaced by other competitors.
4. Resources are difficult for competitors to imitate.

Based on the opinion of Stiles & Kulvisaechana (2004) that a company will have a competitive advantage if it has organizational resources that are scarce, valuable, difficult to imitate and not easily replaced. Companies can achieve with a competitive strategy, namely differentiation or cost leadership.

Organizational performance includes market performance, financial performance, and owner returns (Rehman et al., 2019). The goal of any profit-oriented organization is to achieve financial performance which is seen as a measure to assess management effectiveness (Fadah et al., 2020; Juniar et al., 2018; Saad M & Zhengge, 2015). Performance appraisals can be arranged based on effectiveness, productivity, quality, customer satisfaction, efficiency, innovation and financial resilience (Ondoro, 2015).

Assessing the performance of a company is important in terms of various factors and resources as the goals and objectives of the business being run. Every organization must evaluate and monitor performance and align performance with overall business objectives (Fadah et al., 2020; Juniar et al., 2018; Saad M & Zhengge, 2015). The need to assess organizational performance is an important factor for investors and investors as a guide in making investment and funding decisions. Tools to measure financial performance can use financial ratios (Nwannyanwu, 2017).

Providing good service will increase the company's competitiveness. Competitiveness is also the ability to match or even beat the world's best companies in terms of cost and quality of goods or services (Omerzel & Gulev, 2011). Company resources are important in supporting strategy and improving business performance, including in terms of service, this is shown by Chumaidiyah (2014); Dogan et al., (2014); Ocak & Findik (2019); Omerzel & Gulev (2011); Pasaribu et al., (2016). Based on several research results, hypothesis 1 is formulated that resources have a significant effect on service aspects.

Assets and capabilities are part of resources. Resources owned by superior companies will produce more efficient financial performance than other companies (Tang & Liou, 2010). The results of Charbel et al. (2013); Joshi et al. (2014); Kamukama et al. (2011); furthermore, from Kaplan & Norton (2012) shows that there is an influence of resources on company performance. Based on several research results, hypothesis 2 is formulated that resources have a significant effect on company performance.

Knowledge is a potential source of competitive advantage (Omerzel & Gulev, 2011). Knowledge management processes are important for achieving changes in business strategy (Massingham, 2004). The integration of knowledge management in the

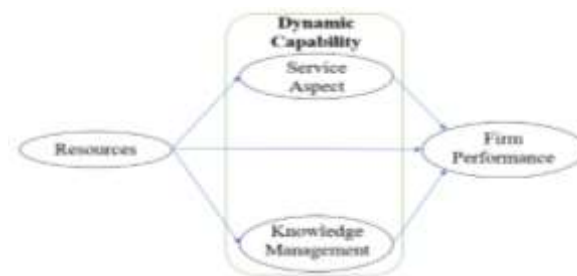
organizational strategy policy-making process provides the ability for organizations to evaluate current strategies and improve future organizational strategies (Birasnav, 2014; Cohen & Olsen, 2015; Donate & Sánchez de Pablo, 2015; Nunes et al. 2006 ; Shujahat et al. 2017; Sundiman, 2018). Based on several research results, hypothesis 3 is formulated that resources have a significant effect on knowledge management.

More and more research results show that service aspect innovation will make companies achieve competitive advantage (RS Kaplan & Norton, 2000). Delivering service products according to customer needs will make it easier for companies to follow changes according to customer desires and improve company image so that they can contribute to the company's operational continuity (Chen & Tsou, 2007; Szymanski & Henard, 2001). Based on several research results, hypothesis 4 is formulated that the service aspect has a significant effect on company performance.

Knowledge management in an organizational activity can be seen from the ability to acquire knowledge and share knowledge, to be able to experiment and create new things, a culture to be able to encourage the creation and sharing of knowledge, to consider strategic value in learning and knowledge. Based on the results of research conducted by Ghorbanizadeh et al. (2019); Henao-Garcia et al. (2020); Lestari et al. (2020); Widodo et al. (2020) shows that there is an influence of knowledge management on company performance. Based on several research results, hypothesis 5 is formulated that there is a significant influence of knowledge management on company performance.

### III. Research Method

This research is a quantitative study that examines the causal relationship between research variables. The research period is 2011-2017, which is the period in which PDAM Jember Regency after restructuring debt. So that the research model can be seen in Figure 1 below:



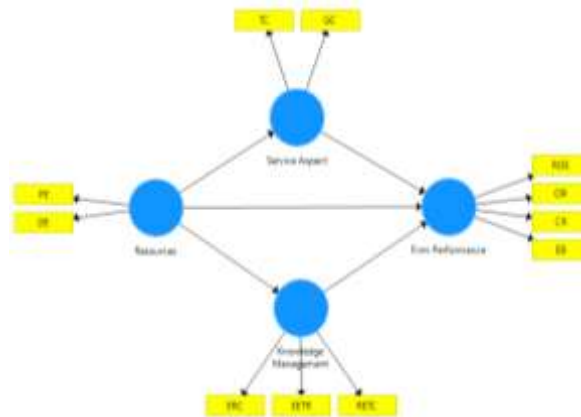
**Figure 1.** Research Model The research

Variable consists of one exogenous variable, namely resources as measured by indicators of production efficiency and distribution efficiency. This study uses three endogenous variables, namely the service aspect is measured by technical services and customer growth indicators, knowledge management is measured by the ratio of employees to customers, the ratio of employee education and training, the ratio of education and training costs, company performance is measured by Return On Equity, Operations Ratio, Cash Ratio and Billing Effectiveness. Hypothesis testing in this study uses SEM-PLS analysis.



## IV. Result and Discussion

The research model after being entered into the SEM-PLS software is as follows:



*Figure 2. SEM-PLS*

Model Based on the structural model that has been built, validity and reliability tests were carried out. The following are the results of the validity and reliability test of the structural model:

**Table 2.** The results of the Structural Model Validity Test

Variables	0.868	<i>Outer Loading</i>	<i>P Values</i>	AVE	Info
Resources	PE	0.762	0.000	0.871	Valid
	DE	0.000	0.000		Valid
Aspects	TC	0.784	0.000	0.779	Valid
	GC	0.837	0.000		Valid
Knowledge Management	ERC	0.742	0.000	0.848	Valid
	EETR	0.794	0.000		Valid
	RETC	0.837	0.000		Valid
Company Performance	ROE	0.853	0.000	0.883	Valid
	OR	0.843	0.000		Valid
	CR	0.858	0.000		Valid
	EB	0.829	0.000		Valid

*Source: Processed Data, 2021*

The first testing stage is testing the outer model. The outer loading value of all indicators shows a value greater than 0.5 with a P value < 0.05, then the average variance extract (AVE) value > 0.5 so that based on this all indicators and variables are declared valid. All composite reliability values show a value > 0.5 so that all variables are declared reliable.

The next testing stage is testing the inner model. Based on the results of data analysis, it is known that the coefficient of determination of the resource variable is 0.306, the variable of determination of the service aspect is 0.394, the coefficient of determination of the knowledge management variable is 0.467. Based on the coefficient of determination of each variable, it can be calculated that the coefficient of determination of the structural model is 0.776 which indicates that the model is substantial. The results show that the contribution of the model can explain the relationship between the four research variables by 77.6% while the rest are factors outside the research model.

**Table 3.** Hypothesis Test Results

<b>Hypothesis</b>	<b>Value Coefficient</b>	<b>P Values</b>	<b>Description</b>
1	0.443	0.000	Significant
2	0.236	0.008	Significant
3	0.210	0.004	Significant
4	0.732	0.000	Significant
5	0.825	0.000	Significant

*Source: Processed Data, 2021*

The results of the first hypothesis test analysis show that resources have a significant effect on resources with a unidirectional relationship, meaning that if the service aspect increases, the resources will also increase. If PDAM Kabupaten Jember can manage its resources well, it will improve the quality of company services from an internal and external perspective. Production efficiency and distribution efficiency that has been carried out by PDAM Kabupaten Jember will improve the technical aspects of service and consumer growth because internally and externally they feel that their resources have been managed properly. The results of the study are in accordance with the results of Chumaidiyah's research (2014); Dogan et al. (2014); Omerzel & Gulev (2011); Pasaribu et al., (2016).

The results of the analysis of the second hypothesis test show that resources have a significant effect on company performance with a unidirectional relationship, meaning that if the service aspect increases, the company's performance will also increase. The management of resources owned by PDAM Kabupaten Jember through production efficiency and distribution efficiency improves the performance of PDAM Kabupaten Jember because financially the performance as measured by ROE, operating ratio and cash ratio is getting better, besides billing management is also getting better due to managing available resources more increasing. The results of the study are in accordance with the research results of Charbel et al., (2013); Joshi et al., (2014); Kamukama et al., (2011); R. Kaplan & Norton (2012).

The results of the analysis of the third hypothesis test show that resources have a significant effect on knowledge management with a unidirectional relationship, meaning that if the service aspect increases, knowledge management will also increase. Production efficiency and distribution efficiency make PDAM Jember district an allocation of resources that can be used to improve knowledge management for company human resources so that the ratio of employees to customers, the ratio of education and training of employees, and the ratio of education costs are better. The results of this study support the results of Birasnav's research (2014); Cohen & Olsen (2015); Donate & Sánchez de Pablo (2015); Nunes et al., (2006); Shujahat et al., (2017); Sundiman (2018).



The results of the analysis of the fourth hypothesis test indicate that the service aspect has a significant effect on the company's performance with a unidirectional relationship, meaning that if the resources increase, the company's performance will also increase. Service is the front line for service companies, especially for PDAM Jember Regency which is in charge of providing water that is suitable for use for the community. The service aspect indicator which consists of internal indicators, namely technical services and from the external side, namely consumer growth has a positive relationship towards company performance. This means that if the service aspect increases for the better, the performance represented by the financial aspect with ROE, operating ratio and cash ratio will get better, followed by better billing effectiveness. The results of the study are in accordance with the research results of Chen & Tsou (2007); Kaplan & Norton Hospital (2000); Szymanski & Henard (2001).

The results of the analysis of the fifth hypothesis test indicate that *knowledge management* has a significant effect on company performance with a unidirectional relationship, meaning that if *knowledge management* increases, company performance will increase. Knowledge management is a key factor in the success of company management. PDAM Kabupaten Jember allocates knowledge improvement for the company's human resources through various ways, namely improving education and training by providing adequate budget allocations. Increased knowledge management has a direct relationship with improving company performance. If knowledge management increases, the management of the company from all aspects will be better, because all the human resources in the company have and understand their duties and are supported by good knowledge so that the company's performance will increase or be better. This is in line with the results of research from Ghorbanizadeh et al., (2019); Henao-Garcia et al. (2020); Lestari et al. (2020); Widodo et al. (2020).

The role of dynamic capabilities where the company must always be able to adapt to various conditions and market conditions that are always changing is a key factor in the success strategy of improving company performance. Dynamic capabilities in service and knowledge management aspects at PDAM Kabupaten Jember make this company exist and be sustainable and even have competitive added value. The dynamic capability of the service aspect is carried out by revitalizing services from the internal and external sides, while the dynamic capability of knowledge management is carried out through innovation responses following technological advances and market changes so that PDAM Jember Regency is able to adapt to changes. affected by the environment through the reconstruction of its resources. Dynamic capabilities are more than just a resource-based view because the company actually reconstructs its resources into profitable profits (Zott, 2003).

## V. Conclusion

The results of the study indicate that resources have a significant effect on aspects of service, knowledge management and company performance. Dynamic capabilities which consist of aspects of service and knowledge management have a significant effect on the company's performance of PDAM Kabupaten Jember. These results show the importance of dynamic capabilities for companies to adapt to changes for the better. To be able to have dynamic capabilities, companies need to have three capabilities, namely adaptive capabilities, absorptive capabilities, and innovative capabilities (Tseng & Lee, 2014). Product innovation requires company investment in research and development activities (Gupta et al., 2016; Qurtubi et al., 2019).

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