THE ROLE OF INNOVATION MANAGEMENT AND BUSINESS STRATEGY TO BOOST THE SUSTAINABLE PERFORMANCE OF ISLAMIC BANK IN INDONESIA

a Deny Hendrawaty, b Margono Setiawan, c Sumiati, d Fatchur Rohman

ABSTRACT

Purposes: In terms of asset share and market share, Islamic banks in Indonesia continue to perform worse than conventional banks. This contrasts with the majority Muslim population in Indonesia. Considering, this research is aimed at investigating the influence of innovation management and business strategy on the performance of Islamic banks in Indonesia.

Theoretical Framework: This study employs a causal research approach. With a quantitative methodology and cross-sectional data collection, explanatory research was conducted. Exogenous variable in this research is innovation management and business strategy. The endogenous variable in this research is Sustainable Islamic Bank Performance.

Design/Methodology/Approach: This study's unit of analysis is the Islamic banking service industry. The survey includes a sample of 197 Islamic banks, including Islamic Commercial Banks, Islamic Business Units, and Islamic People Financing Banks, according to data from the Financial Services Authority (OJK). The unit of observation or respondent is the management/top management of each of these banks. The number of samples taken was 75. The measurement scale employed an ordinal scale based on the Likert technique. For data analysis, the SEM (Structural Equation Modeling) technique was utilized.

Result: Business strategy and innovation management have a significant impact on the sustainable performance of Islamic banks in Indonesia, according to the results of a test of hypotheses. Innovation management has a greater impact on the performance of Islamic banks than business strategy.

Research, Practical and Social Implications: The managerial ramifications of this study's findings are that the management of Islamic banks must reconsider and reformulate their business strategies to be more in line with current conditions, as well as develop innovative management in line with the ever-changing technological trends.

Originality/Value: The novelty of this study is that innovation and strategy in Islamic Banks are important aspects that empirically influence the sustainability performance of Islamic Banks. Aspects of innovation and strategy are important when managing Islamic Banks so that they can grow and obtain positive profits.

a Ph.D. Candidate Management of Science, Faculty of Economic, Brawijaya University, Malang, Indonesia, E-mail: wati.dewanti66@gmail.com, Orcid: https://orcid.org/0009-0005-1621-2344
b Faculty of Economic, Brawijaya University, Malang, Indonesia, E-mail: margono@ub.ac.id, Orcid: https://orcid.org/0009-0001-8315-662X
c Faculty of Economic, Brawijaya University, Malang, Indonesia, E-mail: sumiati@ub.ac.id, Orcid: https://orcid.org/0000-0001-6190-5290
d Faculty of Economic, Brawijaya University, Malang, Indonesia, E-mail: fathur@ub.ac.id, Orcid: https://orcid.org/0000-0003-0761-3240
O PAPEL DA GESTÃO DE INOVAÇÃO E ESTRATÉGIA DE NEGÓCIOS PARA IMPULSIONAR O DESEMPENHO SUSTENTÁVEL DO BANCO ISLÂMICO NA INDONÉSIA

RESUMO

Finalidades: Em termos de quota de ativos e de mercado, os bancos islâmicos na Indonésia continuam a ter um desempenho pior do que os bancos convencionais. Isso contrasta com a maioria da população muçulmana na Indonésia. Tendo em consideração, esta pesquisa tem como objetivo investigar a influência da gestão da inovação e da estratégia de negócios no desempenho dos bancos islâmicos na Indonésia.

Estrutura Teórica: Este estudo emprega uma abordagem de pesquisa causal. Com uma metodologia quantitativa e coleta de dados transversais, foi realizada uma pesquisa explicativa. Variável exógena nesta pesquisa é a gestão da inovação e estratégia de negócios. A variável endógena nesta pesquisa é o Desempenho Sustentável do Banco Islâmico.

Projeto/Metodologia/Abordagem: A unidade de análise deste estudo é o setor de serviços bancários islâmicos. O inquérito inclui uma amostra de 197 bancos islâmicos, incluindo bancos comerciais islâmicos, unidades de negócios islâmicas e bancos de financiamento do povo islâmico, de acordo com dados da Autoridade de Serviços Financeiros (OJK). A unidade de observação ou inquirido é a direção/administração de topo de cada um destes bancos. O número de amostras colhidas foi de 75. A escala de medida empregou uma escala ordinal baseada na técnica Likert. Para análise de dados, utilizou-se a técnica SEM (Structural Equation Modeling).

Resultado e Conclusão: A estratégia empresarial e a gestão da inovação têm um impacto significativo no desempenho sustentável dos bancos islâmicos na Indonésia, de acordo com os resultados de um teste de hipóteses. A gestão da inovação tem um maior impacto no desempenho dos bancos islâmicos do que a estratégia empresarial.

Originalidade/ValorPesquisa, Implicações Práticas e Sociais: As ramificações gerenciais das conclusões deste estudo são que a administração dos bancos islâmicos deve reconsiderar e reformular suas estratégias de negócios para estar mais de acordo com as condições atuais, bem como desenvolver uma gestão inovadora em linha com as tendências tecnológicas em constante mudança.

Originalidade/valor: A novidade deste estudo é que a inovação e a estratégia nos Bancos Islâmicos são aspectos importantes que influenciam empiricamente o desempenho de sustentabilidade dos Bancos Islâmicos. Aspectos de inovação e estratégia são importantes na gestão de bancos islâmicos para que eles possam crescer e obter lucros positivos.

Palavras-chave: gestão de inovação, estratégia de negócios, banco islâmico, desempenho.
1 INTRODUCTION

Islamic bank is a financial institution that provides credit and services for payment traffic and money circulation in accordance with sharia law Sudarsono (2008). Islamic banks have existed in Indonesia since 1992, when Bank Muamalat became the country's first Islamic commercial bank. In 2003, the Indonesian Ulema Council (MUI) issued a fatwa prohibiting bank interest, several factors contributed to the growth and expansion of the Islamic banking business in Indonesia. which helped to the expansion of the Islamic banking industry in Indonesia. The promulgation of Law Number 21 of 2008 regarding Sharia Banking on July 16, 2008, along with the promulgation of Bank Indonesia Regulation (PBI) Number 11/3/PBI/2009 regarding procedures and rules for establishing branch offices, has resulted in the rapid growth of Islamic bank service offices.

As a result of government actions, Several Islamic commercial banks (BUS) and Islamic business units (UUS) have been founded. In the year 2021, there were 12 Islamic Commercial Banks, 21 Islamic Business Units, and 164 Islamic People Financing Banks (BPRS) (Financial Services Authority, 2022). Total Islamic banking assets accumulated from BUS, UUS, and BPRS in 2021 reached IDR693.80 trillion. With this figure, the asset share of sharia banking to national banking is still in the range of 6.74%. In addition, in terms of market share in national banking, Islamic banking is only able to control 5.47%, and the remainder is still controlled by conventional banks. This information contrasts with Indonesia's massive Muslim population, which remains the majority. Meanwhile, efforts must be made to boost Islamic banking's performance in order to grow its market share Widarjono (2018).

Company performance is the product or consequence of all business-related activity (Best.,2009). From the perspective of the Muslim people, Islamic banking in Indonesia offers lucrative economic and market potential. Nonetheless, Islamic banks in Indonesia are not optimally capitalizing on this commercial potential.

According to Thompson, among the managerial tasks of formulating and implementing corporate strategy is taking an approach to implementing strategy, changing conditions, new ideas, and new opportunities (Thompson et al.,2014). The efforts to deal with changing conditions, changing ideas, and capturing new opportunities are closely related to innovation management. Serikan and Kızıloglu stated that innovation management is very important and has an impact on almost every sector and organization that continues to pursue innovation (Serinkan & Kızıloğlu, 2015).
Tornjanski disclosed that innovation in the banking business is acknowledged as a significant component that influences the banking economy and financial system. Prior research has shown the significance of innovation management to business performance (Tornjanski et al., 2015). Base on (Olalere et al., 2021) demonstrates that financial innovation has a considerable beneficial impact on the market value of Malaysian Islamic banks (Olalere et al., 2021). Moreover, Ahmad discovered that innovation can influence the success of Islamic banks in Pakistan (Ahmad et al., 2021).

Moreover, the formulation and execution of business strategy are components of the strategic management process, where business strategy is one of the company's levels of strategy (Wheelen et al., 2015). Managers examine and select successful tactics for their firms (Pearce et al., 2015). Goromonzi demonstrated that the application of strategy has a substantial and favorable impact on the performance of commercial banks (Goromonzi, 2016). Base on (Ndung'u et al., 2016) observed that banks' competing strategies impact their financial success (Mousavi, 2022). In addition, partnership with other institutions boosts the demand for bank products and helps banks to invest in novel technology not only to improve their performance but also to preserve their brand/image.

The effects of innovation management and business strategy on the performance of businesses were evaluated in separate studies. This study intends to investigate the effect of innovation management and business strategy on the performance of Islamic banks in Indonesia as to address this deficiency.

2 THEORITICAL BACKGROUND
2.1 THE IMPACT OF INNOVATION MANAGEMENT ON THE PERFORMANCE OF ISLAMIC BANK

A holistic approach to management innovation provides a solid foundation for a more in-depth understanding of banking dynamics and is a powerful instrument for addressing difficulties in an unstable business environment (Tornjanski, 2015). Innovation management includes managerial activities in which organizations innovate under controlled cycles of unpredictable and complex structures to adapt to their developments in internal and external settings (Ndunga et al., 2016).

Successful innovation in the banking business is built on an integrated set of factors, including quality, customer satisfaction, simplicity, sociability, difference, separability, speed of invention, technology utilization, product compatibility, and
innovative culture (Tornjanski et al., 2015). Various types of innovation include product innovation, process innovation, position innovation, and paradigm innovation (Tidd & Bessant, 2013). Serikan and Kızıloğlu measure innovation management in the banking sector with three indicators namely innovation systems, competitors and technology, and new services (Serinkan & Kiziloglu, 2015). Organizations that control IT and threaten customers' access and use will be more sustainable, as they will be able to take corrective actions more quickly and accurately to avoid consent to the information obtained (Saputra et al., 2023). But business model innovation has a negative relationship with non-financial performance (Mustapha et al., 2023).

Previous research has shown the role of innovation management on company performance. Ndunga showed that innovation affects the financial performance of commercial bank branches (Ndung’u et al., 2016). Ahmad discovered that innovation can influence the success of Islamic banks in Pakistan (Ahmad et al., 2021). Based on Olalere, financial innovation has a substantial positive effect on the market value of Islamic banks in Malaysia (Olalere et al., 2021). The initial hypothesis is then constructed as follows:

H1: Innovation management has a significant impact on Islamic bank performance.

2.2 THE IMPACT OF BUSINESS STRATEGY ON THE PERFORMANCE OF ISLAMIC BANKS

Managers examine and pick the successful business strategies for their organization. The business will be successful if it has multiple comparative advantages over its competitors (Pearce & Robinson, 2015). The integrated and coordinated set of commitments and activities that organizations use to gain a competitive advantage in a particular product market by leveraging their core competencies is the terminology of business strategy (Hitt et al., 2015). According to (Wheelen et al., 2015), the concept of business strategy entails a concentrated effort to enhance the competitive standing of a business unit or firm's product or service within a certain industry or market segment in which such business unit or company operates. According to the study's findings, business strategy is essential because it has numerous effects on business units or corporations. The concept of competitive strategy is the pursuit of excellence in order to effectively compete against all competitors. Collaborative strategy and cooperative strategy are both types of business strategies that involve engaging in partnerships or alliances with one or
more companies to get a competitive advantage over rivals. Entrepreneurial orientation and knowledge management have a significant effect on the competitive advantage and business performance of SMEs and competitive advantage (Widodo, 2023).

Research indicates that corporate strategy influences firm performance. A. and E. Lipitakis integrate e-business strategic planning, strategic planning, and performance management (Lipitakis, 2017). Goromonzi demonstrated that strategy adoption has a large and beneficial impact on commercial bank performance (Hair, 1998). Moreover, Ndung'u highlighted the impact of banks' competitive strategies on their financial performance (Ndung’u et al., 2016). In addition, collaboration with other institutions boosts the demand for bank products and helps banks to invest in novel technologies that are designed not only to improve their performance but also to preserve a strong brand/image. Accordingly, the second hypothesis is structured as follows:

H2: Business strategy of Islamic banks has a significant impact on their performance.

3 METHOD

Briefly This study employs the causality research method, which explores the causal relationship between the variables of the research paradigm-described model. Explanatory study is conducted utilizing a quantitative technique and cross-sectional data collection, i.e., data/information collected at a single point in time, namely in 2023.

The unit analysis of this study is the Islamic banking services industry. As per the Financial Services Authority (OJK), the target audience encompasses 197 entities comprising Islamic commercial banks, Islamic business units, and Islamic people's financing banks (BPRS). Each of these institutions' unit of observation or respondent is the management/top management. In this study, a cross-sectional design and stratified sampling were utilized to collect data.75 samples were collected for this study.

The core data for this study is collected utilizing the Likert technique, resulting in the generation of ordinal data. The ordinal measuring scale is a type of scale that arranges data in a specific order or sequence (Ferdinand, 2014). The technique of Structural Equation Modeling (SEM) was employed for the purpose of data analysis.
4 RESULT AND DISCUSSION

4.1 MODEL EVALUATION (GOODNESS AND FIT)

The study model will be examined using SmartPLS 3.0 and the Partial Least Squares (PLS) technique will be employed for analysis. Partial Least Squares (PLS) represents a viable alternative to Structural Equation Modeling (SEM) for addressing intricate variable interactions in research inquiries. However, it is important to note that PLS is most suitable for cases when the sample size is limited, often ranging from 30 to 100 observations.

4.1.1 Inner model analysis

The study model will be examined using SmartPLS 3.0 and the Partial Least Squares (PLS) approach. Partial Least Squares (PLS) is a viable alternative to Structural Equation Modeling (SEM) for addressing issues pertaining to the interplay of highly intricate variables, even when the sample size is limited (ranging from 30 to 100 samples).

<table>
<thead>
<tr>
<th></th>
<th>R Square</th>
<th>$f^2$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Strategy</td>
<td>0.350</td>
<td></td>
</tr>
<tr>
<td>Innovation Management</td>
<td>0.103</td>
<td></td>
</tr>
<tr>
<td>Performance of Islamic Bank</td>
<td>0.760</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: output Smart PLS
In addition to ascertaining the presence of a statistically significant correlation between variables, it is imperative for a researcher to assess the magnitude of the relationship by employing the Effect Size or f-square metric. The user's text is not clear and does not provide enough information to be rewritten academically. The year 2013. A f square value of 0.02 is considered tiny, while a value of 0.15 is categorized as medium, and a value of 0.35 is classified as large. Values that are less than 0.02 can be dismissed or deemed as ineffective (Sarstedt et al., 2017).

For the model to meet the criterion of model fit, it is necessary for the standardized mean square residual (SMSR) to be below 0.05. The year 2015. The two entities being referred to are Cangur and Ercan. The term "RMS" refers to the root mean square, which is a mathematical measure. The topic of interest is the comparison between the theta value and the root mean square value. The condition for theta is that it should be less than 0.102. Similarly, the SRMR (Standardized Root Mean Square Value) should be 0.10 or below, and the NFI (Normed Fit Index) value should be greater than 0.9. The results of the model fit evaluation are presented in Table 2.

```
<table>
<thead>
<tr>
<th></th>
<th>Saturated Model</th>
<th>Estimated Model</th>
</tr>
</thead>
<tbody>
<tr>
<td>SRMR</td>
<td>0.042</td>
<td>0.042</td>
</tr>
<tr>
<td>d_ULS</td>
<td>0.438</td>
<td>0.438</td>
</tr>
<tr>
<td>d_G</td>
<td>1.416</td>
<td>1.416</td>
</tr>
<tr>
<td>Chi-Square</td>
<td>481.346</td>
<td>481.346</td>
</tr>
<tr>
<td>NFI</td>
<td>0.837</td>
<td>0.837</td>
</tr>
<tr>
<td>rms Theta</td>
<td>0.093</td>
<td></td>
</tr>
</tbody>
</table>
```

Source: Output Smart PLS

Based on the fit model table, it can be observed that the Root Mean Square Theta (RMS Theta) value is 0.093, which exceeds the value of 0.102. Additionally, the Normed Fit Index (NFI) value is recorded as 0.837, which falls below the threshold of 0.9. The SRMR value, also known as the Standardized Root Mean Square value, is found to be 0.042, which falls within the range of 0.10. Consequently, it satisfies the fit model criteria as determined by the two model evaluations.
4.1.2 Outer model analysis

The Outer Model elucidates the association between each construct and its accompanying indicators, wherein the values of these indicators are utilized for the purpose of evaluating the construct's validity and reliability. The analysis can be elucidated using the concepts of discriminant validity, loading factor, construct validity, and composite reliability. The loading value of each element provides an explanation for Construct Validity. Composite Reliability and Cronbach's Alpha are employed as measures to evaluate the reliability, or level of reliability, of the dimensions employed in measuring the variables under consideration. This section explores the association between indicator variables and their underlying latent variables, sometimes referred to as the measurement equation.
Table 3. Measurement Model Testing

<table>
<thead>
<tr>
<th>Variable</th>
<th>Code</th>
<th>Loading Factor</th>
<th>Prob</th>
<th>Composite Reliability (CR)</th>
<th>Average Variance Extracted (AVE)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Innovation Management</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI1</td>
<td></td>
<td>0.930</td>
<td>0.000</td>
<td>0.984</td>
<td>0.884</td>
</tr>
<tr>
<td>MI2</td>
<td></td>
<td>0.943</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI3</td>
<td></td>
<td>0.951</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI4</td>
<td></td>
<td>0.956</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI5</td>
<td></td>
<td>0.927</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI6</td>
<td></td>
<td>0.932</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI7</td>
<td></td>
<td>0.945</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MI8</td>
<td></td>
<td>0.937</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Performance of Islamic Bank</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB1</td>
<td></td>
<td>0.942</td>
<td>0.000</td>
<td>0.979</td>
<td>0.853</td>
</tr>
<tr>
<td>PIB2</td>
<td></td>
<td>0.937</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB3</td>
<td></td>
<td>0.954</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB4</td>
<td></td>
<td>0.942</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB5</td>
<td></td>
<td>0.943</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB6</td>
<td></td>
<td>0.938</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB7</td>
<td></td>
<td>0.910</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PIB8</td>
<td></td>
<td>0.812</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Business Strategy</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SB1</td>
<td></td>
<td>0.926</td>
<td>0.000</td>
<td>0.970</td>
<td></td>
</tr>
<tr>
<td>SB2</td>
<td></td>
<td>0.946</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SB3</td>
<td></td>
<td>0.951</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SB4</td>
<td></td>
<td>0.914</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SB5</td>
<td></td>
<td>0.844</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SB6</td>
<td></td>
<td>0.931</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Output Smart PLS

The outer model is assessed by examining convergent validity, discriminant validity, and construct or latent variable reliability, as represented by the composite reliability score. Convergent validity is determined by examining the loading factor, which serves as a validity indicator indicating the reliability of the question. A loading factor refers to the representation of the relationship between the score of a particular item and the scores of the construct indicators employed to assess the construct. A loading factor value exceeding 0.70 is considered valid. According to Hair et al. (1998) argues that when conducting an initial study of the matrix loading factor, a loading factor of approximately 0.3 is considered to have attained the minimum threshold. However, a loading value of 0.4 is more favorable, and a loading factor of 0.5 or more is often deemed significant.

If the square root of the AVE for each construct is greater than the correlation between the model's two components, the model has higher discriminant validity. A valid AVE value must be greater than 0.50. The construct is trustworthy if the composite reliability is greater than or equal to 0.70.
The results of measuring the first-order construct for variables with a factor loading (> 0.50) and a probability (p) of 0.05 are shown in the table above, the studies conducted by Hair et al. (2010) and Ghozali (2008) provide evidence supporting the sufficient validity of the indicator in explaining latent constructs. An arithmetic > t table at = 0.05 shows that the six variables have valid dimensions and indicators.

A Construct Reliability (CR) grade of 0.70 or higher indicates a high level of internal consistency among the dimensions and indicators. Nunnaly assigns the date of 1994 to it. The concept of discriminant validity, specifically the average variance extracted (AVE), can be mathematically represented by taking the square root of the extracted average variance. The observation that the absolute value of AVE exceeds 0.5 implies that the proposed value is bigger than 0.5. Consequently, the indicators and dimensions tend to encompass all latent factors.

4.2 STATISTICAL TEST

The testing results indicate that innovation management and business strategy have a significant impact on the performance of Islamic banks in Indonesia. This suggests that both hypotheses are correct. The business strategy variable influences Islamic bank performance more than innovation management.

The findings of testing this hypothesis support the conclusions of (Ndunga, 2016), (Ahmad & Olalere, 2021) that innovation management has an impact on corporate success. This research confirms the findings of (Lipitakis, 2017), (Goromonzi, 2016), and (Ndung'u, 2016) regarding the impact of business strategy on firm performance.

According to the conclusions of this study, business strategy has the greatest impact on the success of Islamic banks. Observations indicate that Islamic banks are currently unable to fully apply cost leadership in order to produce products with more competitive prices than competing banks. In addition, Islamic banks continue to have a relatively higher cost of funds structure. Typically, Islamic banking parties do not consider coalition strategies or strategic alliances to enhance their business strategy's superiority. According to (Wheelen, 2015), this demonstrates that the implementation of business strategy, which focuses on improving the competitive position of a business unit or company's product or service in a specific industry or market segment in which the business unit or company competes, is not yet optimal.
Similarly, innovation management has a significant impact on Islamic bank success. On the other hand, based on practical evidence, the OJK identified three significant difficulties in the Islamic banking industry: human resource development, product innovation, and information technology use. Today, Islamic banking tends not to fully implement the creation of products that have Islamic characteristics, because the products produced are not so different from conventional banks and relatively do not provide added value that is different from conventional banks. In addition, the business model of Islamic banks still relies on the existence of physical branches, not yet supported by branchless banking or adequate digitalization. In addition, the added value of the product is not optimal because it is still limited to the basic product. These conditions are anticipated to hinder the performance of Islamic banks. Innovation in the banking business is considered as a significant component that transforms the banking economy and financial system as a whole (Tornjanski et al., 2015). The outer model is evaluated by examining convergent validity, discriminant validity, and construct or latent variable reliability, as represented by the composite reliability value. Convergent validity is determined by looking at the loading factor, which reveals the item's reliability (validity indicator). A loading factor is a statistic that depicts the link between the score of an item and the scores of the construct indicators used to measure the construct. A loading factor value greater than 0.70 is considered legitimate. However, according to Hair, a value of around 0.3 is believed to have reached the minimum level for an initial study of the matrix loading factor, 0.4 is thought to be preferable, and loading factors larger than 0.5 are often significant (Hair, 1998).

The model has more discriminant validity if the square root of the AVE for each concept is greater than the correlation between the model's two components. An appropriate AVE value is one that is more than 0.50. The construct is judged dependable if the total reliability is greater than or equal to 0.70.

The table above shows the results of measuring the first-order construct for variables with a factor loading (λ) > 0.50 with a prob <0.05 meaning that the indicator has good enough validity to explain latent constructs Hair (1998). The results show that the six variables have valid dimensions and indicators with arithmetic > t table at α = 0.05.

The grade of Construct Reliability (CR) indicates that all dimensions and indicators exhibit a relatively high level of consistency, with values equal to or better than
0.70. Nunnaly assigns the dating of the event to the year 1994. The concept of discriminant validity, also known as average variance extracted (AVE), can be elucidated by taking the square root of the extracted average variance. The observation that the Average Error (AVE) exceeds 0.5 implies that the proposed value is more than 0.5. In a general sense, it can be postulated that the indicators and dimensions are representative of all latent variables.

### Table 4. Hypothesis Testing

<table>
<thead>
<tr>
<th>No</th>
<th>Hypothesis</th>
<th>Coefficient</th>
<th>Standard Error</th>
<th>t stat</th>
<th>Prob.</th>
<th>R²</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Innovation Management → Performance of Islamic Bank</td>
<td>0.317*</td>
<td>0.153</td>
<td>2.073</td>
<td>0.039</td>
<td>0.26</td>
</tr>
<tr>
<td>2</td>
<td>Business Strategy → Performance of Islamic Bank</td>
<td>0.583*</td>
<td>0.156</td>
<td>3.731</td>
<td>0.000</td>
<td>0.50</td>
</tr>
</tbody>
</table>

*Significant at α = 0.05 (t table = 1.98)

Source: Output Smart PLS

### 5 CONCLUSIONS

It is proven that innovation management and business strategy have an influence on the performance of Islamic banks in Indonesia. Islamic Bank companies that practice innovation consistently can make a positive contribution to improving the performance of Islamic Banks in Indonesia. Digital innovation currently needs to be carried out by bank managers where customers need speed of service without having to come to the bank counter. All transactions using digital media have been proven to also be able to save on bank operational costs which have an impact on the bank's revenue performance.

In the long term, bank managers who can develop strategic plans are also considered to be able to influence the performance of the bank. Providing loans based on sharia principles can reduce the risk of bad credit so that the performance of Islamic Banks remains stable and improves. This shows that Islamic Banks will be far more viable compared to Conventional Banks if they practice Islamic law. Managerial implications of this study's findings include that Islamic bank management must reevaluate and reformulate their business strategies to be more in line with current conditions, as well as construct innovative management in step with ever-changing technological trends.
REFERENCES


