

# EFFECT OF MARKET ORIENTATION, GOOD GOVERNANCE, AND PROFESSIONAL LEADERSHIP ON MANAGERIAL PERFORMANCE OF SPECIAL UNIT OF UPSTREAM OIL AND GAS: A CASE STUDY OF SKK MIGAS INDONESIA

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## ABSTRACT

*This study has a goal to investigate the relationship between the effect of market orientation, good governance and professional leadership on managerial performance of Special Unit of Upstream Oil and Gas (SKK Migas) in Indonesia. This study also looked at the various variables that determine the survival of the industry, particularly oil and natural gas company in terms of managerial performance. The company's performance will be analyzed with some variables of market orientation, good governance, and professional leadership to demonstrate empirically the effects of the variables. The samples are collected from the population of staff and employees totaled 110 respondents. The model is estimated by maximum likelihood estimation (MLE). Study results showed simultaneously and partially that market orientation significantly influence the corporate performance which followed by professional leadership and good governance. It is followed by professional leadership which affecting the corporate performance of SKK Migas. This study implies that competitiveness of the state-owned enterprise requires an understanding of market orientation so that the company can survive in a changing business environment.*

**KEYWORD:** Market Orientation, Good Governance, Leadership Professional, SKK Migas, Oil and Gas Company

## I. INTRODUCTION

Fuels from petroleum and natural gas still become the belle of the community. Consumption of fuel oil (BBM) also continued to increase to nearly 1.5 million barrels per day. While domestic crude oil production in 2013 was only about 825 thousand barrels per day. Indonesia still also has to import oil to meet the needs of the domestic market. In addition, in order to maintain and increase oil production, it must be accompanied by discoveries of new oil and gas reserves. These discoveries also need capable and pro-people management which important for the balance of market demand and people future. Activities to discover new reserves have been pushed hard. However, in implementation, there are many parties which need to improve their coordination and partnership. Thus it is necessity of SKK Migas to improve its performance with market orientation.

Special Unit of Upstream Oil and Gas (SKK Migas) is an institution established by the government of the Republic of Indonesia through Presidential Decree (Decree) No. 9 of 2013 on the Implementation of Management Upstream Oil and Gas. SKK Migas has a mission in managing the oil and gas upstream activities of oil and gas under the Cooperation Contract. Its main duty is extraction of natural resources of oil and natural gas state to provide maximum benefits and revenues for the state for the welfare of the people. In detail, SKK Migas as a state-owned enterprise perform the functions as below ([www.skspMigas-esdm.go.id](http://www.skspMigas-esdm.go.id)):

1. provide advice to the Minister of Energy and Mineral Resources of discretion in terms of preparation and offers the Work Area and Cooperation Contract;
2. implement the signing of the Cooperation Contract;
3. review and submit field development plan to be initially produced in a working area to the Minister of Energy and Mineral Resources for approval;
4. approve the development plan as stipulated in the previous point;
5. approve the work plan and budget;
6. carry out monitoring and reporting to the Minister of Energy and Mineral Resources regarding the implementation of the Cooperation Contract; and
7. Appoint sellers of petroleum and / or natural gas part of the country that can provide maximum benefits for the country.

Table 1. Growth in Oil and Gas Production

	PEPC	PEP	PHE
<b>PRODUCTION (BOPD)</b>	21,388	121,520	66.480
<b>% Growth in 3 years (2011-2013)</b>	119,6%	-2,8%	112%
<b>Sales (USD) Million</b>	172.79		
<b>Sales growth</b>	38.71%		

To achieve the above objectives, SKK Migas build corporate strategies and analysis of the company's readiness to recognize market conditions, changes in national and international regulations, and formulating leadership formation to improve company performance. In achieving these goals, SKK Migas has focused on the corporate objectives such as market share and profitability and how the company can determine the markets demand and satisfy it with a more effective and efficient compared with its competitors (Agarwal et al., 2003). In the last few years, the company has been a challenge to increase market orientation and build key element to achieve the corporate performance (Han, et al., 1998). This strategy is driven by international market orientation in modern marketing management (Narver and Slater, 1990). In addition, the company must have higher knowledge on market-orientation and future market to connect with customers. Therefore, this capability drives company to earn higher returns than other non-market-oriented company (Day, 1994). In this regard, Jaworski and Kohli (1993, p. 53) stated that business organization operating in a volatile market was expected to be more market-oriented than other organization operates in a relatively stable market. Therefore, it demands the company for wider orientation market.

The orientation is important since the strength of proactive market orientation is a company that is constantly trying to find new opportunities and target customers. As a consequence, market orientation strategy is suitable for companies that operate in a dynamic environment and volatile because it is the strongest foundation to create sustainable competitive advantage (Narver, et al., 2000, p. 89). On the other hand, Narver, Slater, and Tjetje (1998, p. 241) emphasized the importance of organic organizational structure (organic form) for the company to survive in a dynamic and turbulent environment. Organic organizations described as a decentralized organization in decision making as well as nurturing relationship and interdepartmental communication and organizational functions to be more flexible and to improve easier creation of formal corporate governance.

The good and healthy managed company will create a positive reference for the investors. This condition is very instrumental in minimizing capital costs to be borne if the company applying for a loan. This is in addition will strengthen the financial performance and make the company's products released to the market becomes more competitive and acceptable. That is why a well-managed company will try best to attract investors to invest. This supported by a Russell Reynolds Associates'' (1997) survey which revealed that the quality of the commissioner is one of the main factors considered by institutional investors before they decide to buy shares. This will be especially when an investor intends to invest for long periods of time. With a healthy cash flow technology services can be better managed, and allows company management to change their corporate governance and professional leadership from bureaucracy type into entrepreneurship type in order to make the company can be more efficient, reliable, and highly competitive.

According Soewardi (1999, p.170), there are main characteristics of people who work in bureaucracy setting, their pattern was not the patterned by achievement, but rather patterned by non-achievement, such as 4-D (closeness, nepotism, moneyism, and shamanism). 4-D pattern more "rewarding" and more quickly produce which impact on the working types of old bureaucracy setting. With a 4-D

pattern, everything "could be arranged" which lead to mismanagement. Even this mismanagement bring positive attitude of employee loyalism to the boss, but it reduce organizational efficient. In addition, it also brings obedient subordinates. however, it also break their capability and even reduce their innovativeness to do initiative, or creative act at work, because it can harm their job position and it will endanger their "reward" that impact on severe penalties for those critical to fight their boss' mainstream. So, in bureaucratic setting, the safest issue for the employee is to keep silent even it reduce their productivity.

It requires right strategy to prevent the issues are not getting worse. In general, the strategy must involve the development of the organizational structure, budget resources allocation on, leadership, responsible behavior, and organizational culture. Therefore, the implementation of our strategic plan needs management commitment and support to implement good corporate governance (GCG). Therefore, SKK Migas has planned to realize the goals to be achieved in order to have a positive impact on company performance improvement.

Meanwhile, Payne A.F. (1988, p. 46) states that the implementation of market orientation is closely related to personal behavior in organizations. In organizational context, leadership and market orientation is important to improve corporate sustainability. Therefore, Slater and Narver (1998, p. 212) states that a business organization that wants to improve its performance in a fast and dynamic business environment must improve their role of manager. It has been considered as one important aspect. Based on the explanation above, the author take a study with a title: " Effect of Market Orientation, Good Governance, and Professional Leadership on Managerial Performance of Special Unit of Upstream Oil and Gas: A Case Study of SKK Migas Indonesia."

This paper is organized into five parts. Part 1 contains introduction to the brief history of Special Unit of Upstream Oil and Gas (SKK Migas) which established under Presidential Decree (Decree) No. 9 of 2013 with its mission and function. This part also gives background and reason why the author take the topic. Part 2 consists of market orientation as the mechanisms in creating customer value and how the company consider the variables are important in every corporate activity and planning process. It also explained the leadership aspects and how the leadership can foster the achievement of organizational goals. It then reviewed the performance resulted from the value-added activities and the development of management activities. For part 3 and part 4, it contains sampling methodology and analysis results, respectively. The conclusion and future work are given in part 5.

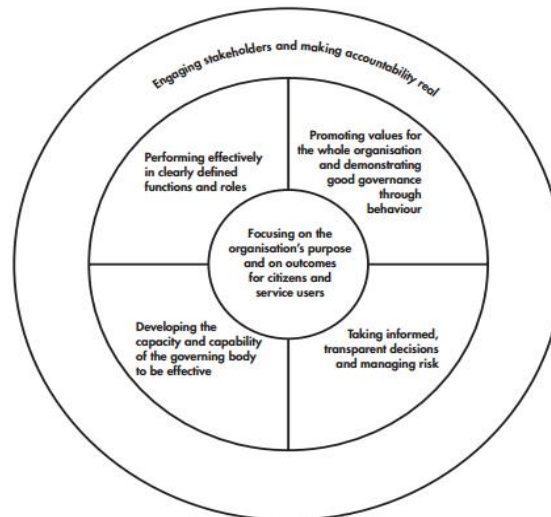
## **II. LITERATURE REVIEW**

### **Market Orientation**

From perspective proposed by other experts (e.g. Cadogan and Diamantopoulos), market orientation can be defined as organizational behavior that includes the collection, dissemination, and response to market intelligence that reflected customer orientation, competitor orientation, and coordination mechanisms in creating customer value (Cadogan and Diamantopoulos, 1999). Market orientation is also defined widely by Lado (1998) by combining distribution and environmental orientation. In this context, market orientation is defined as the extent that companies use information about the market interest to coordinate and implement strategic actions (Lado, 1998). Since the study take state-owned enterprise which want to develop market orientation, the researchers will use market orientation model developed by Narver and Slater (1990), e.g., customer orientation, competitor orientation, and interfunctional coordination combined with components of responsiveness developed by Jaworski and Kohli (1993), Gray et al. (1998), and Dobni and Luffman (2000).

### **Good Governance**

Corporate is a term used to describe a business organization that has legal entity status. As legal entity, it is subject of law that bears the legal rights and obligations as stipulated by laws and regulations regarding Corporate law. In Indonesia, it known as Act No. 40 of 2007 on Limited Liability Company which stated that corporate have a slightly different definition than the term of Company. The term of company has a broader sense includes not only a business entity with legal status (i.e., Limited Liability Companies and Cooperatives), but also a business entity which not a legal entity (e.g., CV, Firm, and other forms of partnership and other businesses).



**Figure 1.** Principles of good governance (Source: Garrat, 2000).

Corporate activity is run and controlled by 3 elements as in Act 3/40 2008 called 3 Organ of Company, e.g., the General Meeting of Shareholders, the Board of Commissioners and Board of Directors. All the three activities of Company Organs (in running and controlling corporate) are known by the term of “governance”. Although initially there are a maze of Indonesian synonym for the term, but since 2007, the National Committee on Governance (NCG) officially use the term "Governance" as a synonym for the term “governance” officially. With measurable strategic planning, board of directors can monitor the company performance. According Garrat (2000), the company which has corporate planning will survive and continue to produce high-performance organization. The clearly measurable strategy and planning will make the board can measure and monitor the company performance on an ongoing basis. According to Garrat (2000), a company that can survive and compete in the free market era of 21st century must build a higher performance ability which is represented by the following characteristics.

The shape of the company must be more transparent, streamline and nimble in adjusting into effective leadership, as well as innovativeness. In addition, it must have operational orientation focused on impulse customers (market orientation) with an emphasis on integrated quality and use the time as efficiently as possible in every activity and process.

### **Definition of Leadership**

Leadership has been defined in relation to individual characteristics, behavior, influence on others, patterns of interaction, role relationships, its place in an administrative position, as well as other people's perception regarding the validity of influence (Yuki, 2001). Greenberg (1997) defined leadership as a process of an individual to influence others in the group to achieve the group or organization objectives. According Ivancevich and Matteson (1999), leadership is a process of influencing others to facilitate the achievement of organizational goals. The same definition proposed by Gana (2004) which defined leadership as a process of influencing people and mobilize various other resources to cooperate in achieving the objectives (Gana, 2004).

Leadership is also be understood as an ability to influence a variety of strategies and goals, influence the commitment and adherence to the task of achieving the goal, and driving groups in order to identify, maintain, and develop organizational culture (Sadler, 2003). In this perspective, capability must be used to build a joint process to grow the leaders and followers, actuating cooperation. The goal is an important element of leadership. As a process, leadership can be categorized as below:

- (1) bringing effect, examples, and persuasion to others
- (2) building interaction between various factors, both as a leader and a follower,
- (3) improve situational initiation in which all parties interacts, and
- (4) Fostering a wide range of outcomes, such as the achievement of goals, group cohesion encouragement, or a change in organizational culture (Gana, 2004).

### **Performance results**

From the definition, performance corresponds to the actual job finished or actual achievement. The word “performance” is synonym to execution of the work or achievement in a job. Performance variables consist of several elements, quality of work, employee honesty, initiative, attendance, work ethic, reliability, knowledge of the work, responsibility, and the use of time (Umar 1998: 261). Furthermore Osborn (1997: 387-91) developed a performance measurement system based on indicators as below:

- (A) process and results,
- (B) efficiency and effectiveness, and
- (C) Results of program and broader policy.

According Tatikonda and Tatikonda (1998: 49), the purpose of performance measurement is to assist in setting standards, targets, means, or rails for progress, motivate and communicate the organization's strategy, and influence behavior change. From his perspective, performance measurement is designed to improve organization to eliminate non-value-added activities and optimize the value-added activities, in line with the development of management activities (Hansen and Mowen, 1995: 855). The performance measurement is necessary in order to avoid the following.

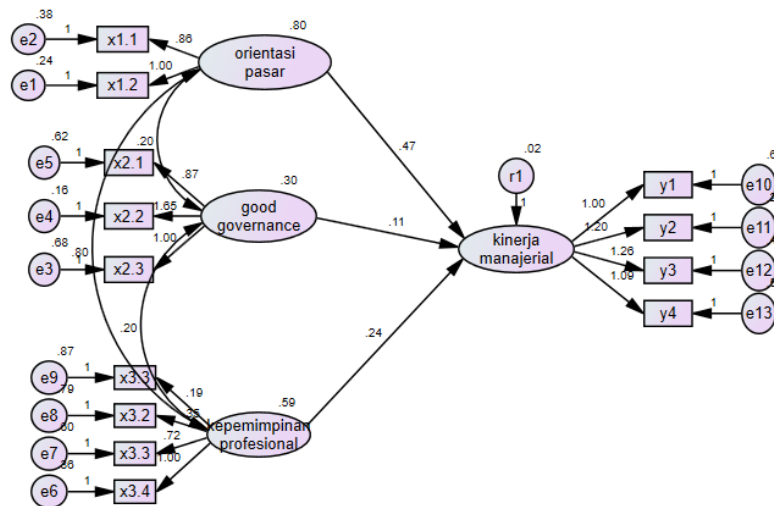
- (A) Top management does not give priority to employees or giving the wrong priorities.
- (B) Middle managers and front-liners are not empowered to make quick decisions when problems arise.
- (C) Working environment form or organizational structure does not encourage innovation and creativity.
- (D) Top management needs improvement from current situation.
- (E) The top management loses control on disparities.

### **III. SAMPLES AND METHODS**

In this study, the population is the staff and employees of SKK Migas, which consists of the head, deputy head, the deputies, and experts. The sample is part of the population. The sample in this study is part of officials, support staff management and staff of experts, most of the leadership and support staff leaders, as well as expert staff seconded to SKK Migas. Since this research will investigate the influence of the independent variables on the dependent variable, the data collection is done by random sampling. From these efforts it collected the samples of SKK Migas employees set at 110 respondents.

### **IV. ANALYSIS AND RESULTS**

This study has observed some of the variables Effect of Market Orientation, Good Governance, and Professional Leadership on Managerial Performance of Special Unit of Upstream Oil and Gas that the company is SKK Migas Indonesia. It then analyzed the test results stating that the market orientation, good governance and professional leadership to managerial performance SKK Migas which summarized in figure 2.



**Figure 2.** Effect of Market Orientation, Good Governance and Leadership Professional to SKK Managerial Performance of Oil and Gas.

Based on the result of hypothesis testing, the effect of SKK Performance Oil and Gas (Y<sub>1</sub>) Market Orientation (X<sub>1</sub>), Good Governance (X<sub>2</sub>) and Professional Leadership (X<sub>3</sub>) on Managerial Performance of SKK Migas. This is summarized in Table 2.

The test results prove that the market orientation (X<sub>1</sub>), good governance (X<sub>2</sub>), Professional Leadership (X<sub>3</sub>) improve the Performance of SKK Migas (Y<sub>1</sub>).

**Table 2.** Variable Relations

			Estimate	S.E.	C.R.	P	Label
Managerial_performance	<--	Market_orientation	.470	.109	4.310	***	par_10
Managerial_performance	<--	good_governance	.105	.091	1.154	.049	par_11
Managerial_performance	<--	professional_leadership	.237	.121	1.951	.021	par_12

Source: processed data, 2015

**Testing Assumptions**

In addition, it is also considered that the measurement model is estimated by maximum likelihood estimation (MLE) which the multivariate normality of the data used as the absolute requirement. Violation of this assumption will cause a large standard error and the goodness of fit index reduced so the interpretation of the loading factor biased. Multivariate normality was tested by Mardia's Statistics and the threshold used maximum value of the critical ratio Mardia's Statistic = 3 (Bagozzi & Baumgartner, 1994). At the univariate level, the data normality can be evaluated from skewness (= indicates the extent to which the data is distributed symmetrically) and kurtosis (= show the peak of data distribution) where the critical ratio for skewness and kurtosis are no more than ± 2.58 (Bagozzi & Baumgartner, 1994). from the criteria-based testing of normality of data, it is concluded that the data for exogenous construct are normally distributed for both univariate and multivariate levels as shown in the following table.

**Table 3** Testing Normality Data

Variable	min	max	skew	c.r.	kurtosis	c.r.
y4	2.000	5.000	-.383	-1.641	-1.022	-2.189
y3	2.000	5.000	-.609	-2.608	-.879	-1.883
y2	2.000	5.000	-.339	-1.452	-.890	-1.905
y1	2.000	5.000	-.429	-1.838	-1.041	-2.228
x3.3	2.000	5.000	-.344	-1.473	-.757	-1.620
x3.2	2.000	5.000	-.237	-1.014	-.862	-1.846
x3.3_A	2.000	5.000	-.352	-1.507	-.813	-1.741
x3.4	2.000	5.000	-.483	-2.070	-.723	-1.547
x2.1	2.000	5.000	-.267	-1.142	-.739	-1.583
x2.2	2.000	5.000	-.580	-2.483	-.664	-1.421
x2.3	2.000	5.000	-.382	-1.637	-.874	-1.871
x1.1	2.000	5.000	-.354	-1.516	-.883	-1.890
x1.2	2.000	5.000	-.480	-2.053	-.882	-1.887
Multivariate					3.609	.958

Source: Estimation results with AMOS21 (2015)

It appears from the above table that the univariate skewness value is no greater than  $\pm 2.58$  and univariate kurtosis is no more than 10 as suggested by Kline (2004). This condition is supported by critical ratio (CR) for skewness and kurtosis of each variable under  $\pm 2.58$  so that it is concluded that the data are normally distributed at the univariate level (Byrne, 2001). While in line with multivariate kurtosis it appears that CR is also under  $\pm 2.58$ . Therefore, it concluded that the data are normally distributed in the multivariate level (Byrne, 2001).

#### Outliers Testing

Outliers are observations or data that has unique characteristics that look very different from the others observations due to its extreme value, either for a single variable or combination of variables (Kline, 2004). The outliers can be evaluated in two ways, namely analysis on the univariate and multivariate outliers (Kline, 2004).

#### Multivariate Outliers

Detection of outlier is also performed on multivariate level because of the absence of the outlier on univariate level does not guarantee it also will happen on the absence of multivariate outliers. The multivariate statistical outlier is detected using Mahalanobis Distance test. It tested the multivariate distance among the scores of each observation with an average sample (centroid). Table 4 below show 7 observations from the Mahalanobis distance farthest from the centroid.

In addition, to detect the multivariate outliers it is done by looking at the value of Mahalanobis Distance. The value of Mahalanobis Distance is compared with chi-square value at a significance level of 0.001. If the value of Mahalanobis distance is greater than value of chi-square, there is a problem of multivariate outliers (Ferdinand, 2000: 135; Ghazali, 2004: 106). Under these provisions, in this study the value of chi-square with a significance level of 0.001 and a degree of freedom 59 e.g.  $\chi^2(59, 0.001)$  gaining the value of 77.93.

**Table 4** Detection Multivariate Outliers

Observation number	Mahalanobis d-squared	p1	p2
105	28.608	.007	.560
101	25.671	.019	.615
22	25.374	.021	.396
110	22.329	.050	.811
106	21.887	.057	.759
82	21.208	.069	.777
8	20.722	.079	.770

Source: SEM result, 2015

As shown in Table 3, the results of Mahalanobis Distance calculation is at most 28 608, and the value is smaller than the chi-square value of 77.93. Therefore, it can be concluded there were no problems

of multivariate outlier. In the absence of univariate and multivariate outlier, it means the data is feasible to be used.

#### Suitability Test and Test Statistics

This model Testing used multiple fit index to measure the suitability of the research model in this study. From the analysis of AMOS 21 it obtained the following results:

**Table 5.** Evaluation Criteria Goodness of Fit Index

Criteria	Model Results	Critical Value	Conclusion
Chi-Square	28.608	77.93	Good
Probability	0,000	$\geq 0,05$	Marginal Probability
RMSEA	0,102	$\leq 0,08$	Less
GFI	0,862	$\geq 0,90$	Marginal Probability
AGFI	0,788	$\geq 0,90$	Less
CMIN/DF	2,128	$\leq 5,00$	Good
TLI	0,874	$\geq 0,95$	Marginal Probability
NFI	0,839	$\geq 0,90$	Marginal Probability
CFI (Comparative fit index)	0,905	$\geq 0,95$ (Bentler)	Marginal Probability

Source: Processed Primary Data, 2015

Table 5 informs the result of suitability test for the model has produced a good level of acceptance. Therefore, it can be concluded that the dimensions that form the variable, both exogenous and endogenous is appropriate. This showed that the model can be accepted statistically.

## V. CONCLUSION

Based on the analysis of the variables being tested and discussion on the effect of the variables, e.g., market orientation, organizational structure, leadership of the participatory budget, and managerial performance, and by using the analysis result of the data from a survey of 110 respondents from SKK Migas, it obtained the following conclusions.

1. Market orientation, good governance, and professional leadership respectively, have a significant relationship with a high degree of correlation. It implies that the application of market orientation needs good governance and professional leadership to complete each other in order to get relevant decisions. Similarly, the effectiveness of good governance implementation is influenced by market-oriented policies and professional leadership in SKK Migas. Professional leadership success will be optimal if the aspect of market orientation and the implementation of good governance are also implemented. The relatively high correlation between market orientation, good governance, and professional leadership in SKK Migas resulted due to the rapid and broad decision-making, human resources support, adequate facilities, and the implementation of good governance.
2. Simultaneously and partially, market orientation, good governance, and professional leadership have significant effect on the performance of SKK Migas. This implies that market orientation, good governance, and professional leadership as internal factors of the institutions have an important role in improving the corporate performance of SKK Migas. The relatively high simultaneous effects are caused by (1) the three variables dominantly affecting the performance of SKK Migas; (2) the suitability of the application of market orientation, good governance, and professional leadership. Partially, market orientation has the smallest influence on the performance of SKK Migas. It can be understood because of the need and demand for gas from year to year continues to increase rapidly so the company does not need to look for new market, but consumers are looking for the market. Furthermore, good governance provides the second biggest influence, while the professional leadership gains the greatest influence.

3. Good governance has a lower correlation with professional leadership in SKK Migas. It implies that the implementation of good governance in the context of decision making is less relevant because in Indonesia it has not fully implement good governance due to other reason, such as the involvement of many prominent leaders of SKK Migas has relation with political interest from the parties winner of the election which unsuitable with the good governance objectives.

For future research, it is important to analyze the variables by expanding to other state-owned enterprises and/or to other industries. In addition, it is also important to know the comparison of the privatization process of SKK Migas with the cases from other countries.

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