“Human resource management in promoting innovation and organizational performance”

AUTHORS	I Gede Riana https://orcid.org/0000-0002-8912-2252 Gede Suparna https://orcid.org/0000-0003-4261-9402 I Gusti Made Suwandana https://orcid.org/0000-0002-6500-3320 Sebastian Kot https://orcid.org/0000-0002-8272-6918 http://www.researcherid.com/rid/P-5165-2018 Ismi Rajiani https://orcid.org/0000-0002-4316-0501 http://www.researcherid.com/rid/O-2306-2018

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I Gede Riana, Associate Professor of Management Science, Faculty of Economics and Business, Department of Management, Udayana University, Bali, Indonesia.

Gede Suparna, Assistant Professor of Management Science, Faculty of Economics and Business, Department of Management, Udayana University, Bali, Indonesia.

I Gusti Made Suwandana, Instructor of Management Science, Faculty of Economics and Business, Department of Management, Udayana University, Bali, Indonesia.

Sebastian Kot, Doctor of Science (Economics), Management Faculty, Czestochowa University of Technology, Czestochowa, Poland; Faculty of Economic Sciences and IT, North-West University, Vaal Triangle, South Africa.

Ismi Rajiani, Doctor of Management, Assistant Professor of Management Science Muhammadiyah Gresik University, Indonesia.

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I Gede Riana (Indonesia), **Gede Suparna** (Indonesia),
I Gusti Made Suwandana (Indonesia), **Sebastian Kot** (Poland), **Ismi Rajiani** (Indonesia)

HUMAN RESOURCE MANAGEMENT IN PROMOTING INNOVATION AND ORGANIZATIONAL PERFORMANCE

Abstract

Human resource management (HRM) is one of the elements enabling an organization to remain competitive in turbulence conditions. The effective practice of HRM makes competent and innovative employees contributing to the achievement of organizational objectives. This study aims to analyze HRM practices in creating innovation and organizational performance. The questionnaire was used to measure the respondents' perceptions of variables used by a Likert scale. A survey of 126 manager samples and middle managers at export-oriented short and medium enterprises (SMEs) in Bali, Indonesia, was conducted to test the model. The analysis has shown that the proposed model was proven to be compliant with the research hypotheses. HRM significantly affects organizational performance and innovation, and it was found out that innovation can improve organizational performance. However, in the process of simultaneous testing, it was found out that innovation cannot improve organizational performance. The lack of attention to investments in human resources became one of the barriers to SMEs in creating innovation.

Keywords managers, competitiveness, innovativeness, small business, Indonesia

JEL Classification M12

INTRODUCTION

Globalization has demanded the organization to be always ready in facing the increasing industrial competition. This condition requires the organization to always foster the innovation by integrating various new knowledge to conduct the organizational learning (Dahie & Mohamed, 2017). The previous study stated that creativity and innovation in products, processes, and services contribute to the long-term growth and success of the organization (Yeh-Yun Lin & Yi-Ching Chen, 2007; Zhou & Shalley, 2008). Innovation and creativity are also essential so that the organization can win an increasingly stringent competition in the changing environment (Chow, 2017). An innovative organization is proven to maintain a competitive advantage (Johannessen & Skaalsvik, 2015; Ghosh, 2015) because it can respond faster to environmental changes (Do, Yeh, & Madsen, 2016). A key to the ability to create innovation to support the organization's performance is the support of the quality of human resources, which should be on the top priority (Rajiani & Norain, 2018).

The findings of Gil-Marques and Moreno-Luzon (2013) indicated that the practice of human resource management has a significant impact on innovation. It is in line with (Sheehan, Garavan, and Carbery (2013), Lu, Zhu, and Bao (2015) who said that HRM could make a positive contribution in helping the organizations to innovate. The results of research by Ma Prieto and Pilar Perez-Santana (2014) emphasized the vital role of HRM in fostering the innovative behavior because it

can provide certainty that all functions in the organization can run well. Research of Budhwar, Chand, and Katou (2007), Nawab, Nazir, Mohsin, and Syed (2016) provided strong evidence that HRM can have a practical function to support the performance of the organization, while Som (2008) claimed that the implementation of HRM through an appropriate approach is proven to be able to enforce the achievement of the organization. Some other researchers confirmed again that HRM significantly impacts improving the organizational performance (Nawab et al., 2016; Al-Haraisa, 2016). Furthermore, Sabiu, Ringim, Mei, and Joarder (2019) emphasized that HRM in terms of selection and recruitment has a strong influence on organizational performance.

Research on innovation is relatively rare in SMEs, because it is more focused on conventional operating activities. Besides, the concept of innovation is still perceived as an activity that is only adopted by medium-sized companies and large companies. As a result, SMEs often ignores the vital role of innovation to support organizational performance. One way to examine the uniqueness of human resources is through HRM to get suitable employees for the organization. The dynamic capability theory (Teece, 2007) also claimed that organizations could combine internal and external knowledge to deal with environmental changes in capturing the opportunities. HRM is a concept that can make it easier for employees to share knowledge because they feel comfortable at work (Okoe, Boateng, Narteh, & Boakye, 2017). Based on these considerations, this study aimed to analyze HRM practices in fostering innovation and organizational performance.

1. LITERATURE REVIEW

Human resource management (HRM) is a series of activities, functions, and processes, which are different but interrelated and directed to attract, develop, maintain, and even terminate the employment (Florén, Rundquist, & Fischer, 2016). There are five dimensions of HRM (Laursen & Foss, 2003; Jiménez-Jiménez & Sanz-Valle, 2005; Shipton, Fay, West, Patterson, & Birdi, 2005; Tan & Nasurdin, 2011), namely performance appraisal, career management, reward systems, training, and recruitment. HRM can enhance the employees' innovative behavior to support organizational innovation. Innovation is a process of accumulation of knowledge that needs to be planned, organized, and managed adequately (Johannessen & Skaalsvik, 2015). Innovation is considered as the beginning of making changes but is deemed to be more than just making changes so that it can be felt differently (Crumpton, 2012). Innovative organizations are relatively easy to carry out their vision and mission to perform better. In general, the concept of performance is based on the idea, in which organizations are a collection of productive assets, namely human, physical, and capital resources to achieve common goals (Carton & Hofer, 2006). Abu-Jarad, Yusof, and Nikbin (2010) asserted that organizational performance is the ability of organizations to achieve goals and objectives by using the resources that are efficient and effective.

The influence of HRM on organizational performance has been widely studied. Batt's (2002) findings indicated that there was a significant relationship between HRM, especially salaries and career security, and organizational performance. Human resource practices can increase sales growth, teamwork, and employee participation in decision-making. HRM is the process of recruitment, incentives giving and staffing have a synergy effect that affects the employees' attitudes towards work (El-Ghalayini, 2017). Likewise, Guest, Mitchie, Conway, and Sheehan (2003) stated that there is a strong relationship between HRM and productivity and financial performance, while Farouk, Elanain, Obeidat, and Al-Nahyan (2016) said that HRM has a strategic role because it can have a direct impact on organizational performance.

Almost no one dares to ensure that all employees can act innovatively in the organization. Innovative employees need innovative cultural aegis in the organization (Coffman, 2015) so that they can support each other's activities and also sharing (Okoe et al., 2018). Staff placement strategies can support innovation creation to make the employees feel comfortable because they have clear expectations at work. Heeks, Amalia, Kintu, and Shah (2013) stated that HRM could make employees feel comfortable in the workplace and can increase the ability to innovate, so the organiza-

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tions become more innovative. The well-run HRM model has a significant impact on organizational performance. Research findings by Vermeeren, Kuiper, Bram, and Vogelaar (2014), Al-bahhussin and El-garaihy (2013) confirmed that HRM significantly increases customer satisfaction and organizational performance. Furthermore, Chand and Katou (2007) stated that HRM, which is through programs of recruitment, selection, work plan, job design, training and development, as well as payroll systems, has a significant impact on organizational performance, whereas Wright, Gardner, Moynihan, Park, Gerhart, and Delery (2000) stated that the implementation of HRM has a considerable effect on the competitive advantage, which can improve organizational performance (Al-Haraisa, 2016).

H1: HRM has a significant effect on organizational performance.

Sheehan et al. (2013) stated that interventions in HRM could make a positive contribution to organizational innovation activities. HRM is also found to significantly increase the employee involvement, leadership, managers' motivation to learn, promotion of learning the culture, and development of social capital to support innovation. Ma Prieto and Pilar Perez-Santana's (2014) research stated that human resource management practices are related to the placement and selection of the appropriate employees, which has implications for innovative employee behavior so that it has a significant impact on innovation (Gil-Marques & Moreno- Luzon, 2013). Employee participation can lead to confidence in the activities carried out, so it can improve innovation behavior. Research conducted by Al Haraisa (2016), Farouk et al. (2016) stated that HRM has a significant effect on innovation. Results of research conducted by Nieves and Quintana (2016) showed that the implementation of recruitment and selection has a direct impact on innovation. Also, Lu et al. (2015), analyzed the dimensions of HRM, and it was found that all aspects of HRM have a significant effect on innovation.

H2: HRM has a significant effect on innovation.

Innovation is a fundamental requirement in managing an organization to compete sustainably (Chen & Huo, 2015). Innovation is considered the key to winning a competition through the creation of new ideas (Samuel, Siagian, & Octavia, 2017). Innovation can also help organizations create new products, improve the processes, and even be able to lower production costs through technological support (Trott, 2008). Ghos (2014) revealed that innovation gains more attention as a source of sustainable competitive advantage. Although it is essential, the role of innovation in improving the organizational performance is still a debate (Iscan, Göknur, & Atilhan, 2014). In general, innovation is a way of creating new values for organizations to improve the competitiveness (Gomusluoglu & Ilsev, 2009). The vital role of organizational innovation is to maintain the effectiveness of an organization in achieving long-term success to overcome turbulence in the external environment (Sabiu, Mei, & Joarder, 2016).

Chen (2017) mentioned that innovation is a crucial factor that can affect employee performance and organizational performance. Some researchers claim that innovation plays an essential role in encouraging better organizational performance due to the increase in the effectiveness of the organization. Nawab et al. (2015) stated that the ability of organizations to innovate has a significant impact on the performance of the organization. The existence of various innovations by the organization can improve competitiveness to make the organization perform better. Moreover, research conducted by Valdez-Juárez, García-Pérez de Lema, and Maldonado-Guzmán (2016), which is related to the effect of innovation on SMEs performance, stated that innovation is an organization's need to improve the competitiveness to be able to achieve superior performance.

Furthermore, Cho and Pucik (2005) explained that innovation could improve the product quality. Therefore, it is also increasing profitability and market value. Moreover, Hua and Wemmerlöv (2006) stated that the higher the level of intensity of product changes due to innovation, the better the marketing performance, which also affects the organizational performance. On the other hand, innovation behavior can work well when there is support from an innovative employee. Getting innovative employees requires the implementation of hu-

man resource management practices (Nieves & Quintana, 2016), so it has an impact on organizational performance (Budhwar et al., 2007).

H3: Innovation has a significant effect on organizational performance.

2. RESEARCH METHODS

The population of this research was all SMEs that carry out export activities in Bali in five regencies. The target population was 168 top managers and middle managers spread over 42 export SMEs. The questionnaire was arranged based on eleven indicators consisting of several statements with five answer choices, namely strongly disagree (SDA-1), disagree (DA-2), neutral (N-3), agree (A-4) and strongly agree (SA-5). HRM uses four indicators referring to the researches of Tan and Nasurdin (2011), Manafi and Subramaniam (2015). Innovation uses three indicators, which were adopted in the study of Lai, Hsu, Lin, Chen, and Lin (2014), Nawab et al. (2015), Byukusenge, Munene, and Orabia (2016). Also, the organizational performance uses four indicators referring to Sanchez and Marin (2005), Chong (2008). The results of the questionnaires distribution obtained 126 that were entirely and validly filled, then the data collected was analyzed by WarpPLS. The profile of the research respondents was arranged in Table 1.

Table 1. Profile of the respondents

No.	Profile of respondents	Total	Percentage
	Gender		
1	Male	57	45.24
2	Female	69	54.76
	Age		
1	< 26 years old	18	14.28
2	27-36 years old	66	52.38
3	37-46 years old	32	25.40
4	> 47 years old	10	7.94
	Education		
1	Senior high school	71	56.35
2	Diploma	26	20.63
3	Bachelor	12	9.53
4	Master	17	13.49
	Years of service		
1	6-10 years	75	59.52
2	11-15 years	26	20.63
3	16-20 years	13	10,32
4	21-25 years	12	9.53

3. RESULTS

The measurement model was evaluated by checking the validity (convergent and discriminant) of construct indicators and composite reliability for indicator blocks.

Table 2. Latent variable coefficients

Coefficients	HRM	Innovation	Organizational performance
R-square	–	0.396	0.219
Composite reliability	0.854	0.645	0.923
Cronbachs' alpha	0.768	0.658	0.882
Average variance extracted	0.599	0.589	0.755
Variance inflation factors (VIFs)	1.347	1.345	1.197
Q-square	–	0.380	0.225

R-square shows the proportion of predictor variables, which explains the response variable. Variable business performance of *R*-square was 0.219, informing that the contribution of HRM variable and innovation on the organizational performance was 21.9%, and the remaining was 78.1% that is influenced by other variables outside of research model and error. The value of composite reliability and Cronbach's alpha was used to determine the reliability of the instrument, which shows that the instrument has been reliable with a composite reliability coefficient (> 0.70) and Cronbach's alpha value (> 0.60). The convergent validity was evaluated using the average variance extracted value (AVE > 0.50), indicated that the AVE value was above 0.50, which means it has fulfilled the convergent validity criteria. Similarly, the value of variance inflation factors (VIFs) shows the value of < 3.3, which means that the model is free from the problem of collinearity of vertical, lateral, and common method. The model with predictive validity must have a Q-square (Q2) value, which is higher than zero. The results of the analysis show that the model has had good predictive validity because the value of Q2 was 0.380 and 0.225.

Output correlations among latent variables are correlations among latent variables to evaluate discriminant validity. The results of the analysis show that the root of AVE was higher than the correlation of the latent variables with *p*-value of < 0.001, so the model was proved to have met the discriminant validity criteria. Also, the cross-loading indi-

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cator value was above 0.5 (Table 4), which means that the model has fulfilled the convergent validity criteria.

Table 3. Correlations among latent variables

No.	Variables	HRM practice	Innovation	Organizational performance
1	HRM practices	(0.774)	0.467	0.348
2	Innovation	0.467	(0.768)	0.346
3	Organizational performance	0.348	0.346	(0.869)
***P*-values for correlations**				
1	HR practices	1,000	< 0.001	< 0.001
2	Innovation	< 0.001	1,000	< 0.001
3	Organizational performance	< 0.001	< 0.001	1,000

Table 4. The outer model's measurement analysis

Construct	Item code	Cross loading	Type (SE)	*p*-value
HRM practices	Compensation	0.857	Reflect 0.073	< 0.001
	Training	0.893	Reflect 0.072	< 0.001
	Performance assessment	0.596	Reflect 0.077	< 0.001
	Participation	0.712	Reflect 0.075	< 0.001
Innovation	Product innovation	0.524	Reflect 0.082	< 0.001
	Process innovation	0.864	Reflect 0.072	< 0.001
	Market innovation	0.957	Reflect 0.071	< 0.001
Organizational performance	Sales growth	0.978	Reflect 0.070	< 0.001
	Competitive position	0.974	Reflect 0.070	< 0.001
	Profit growth	0.647	Reflect 0.076	< 0.001
	Employee growth	0.835	Reflect 0.073	< 0.001

Furthermore, direct influence hypothesis test results and indirect influence among variables by using WarpPLS are shown in Figure 1 and Table 5.

Hypotheses testing was done by observing the path coefficient direct effect of influence among latent variables and calculation of variance accounted for (VAF) for mediation testing. Table 5 provides information that HRM has a significant positive effect on innovation with a path coefficient of 0.629 and *p*-value of < 0.001, which means highly significant. These results show that the hypothesis that HRM has a significant effect on innovation is acceptable. The influence of HRM on organizational performance shows a path coefficient of 0.362 with *p*-value of < 0.001, which means it is highly significant, and accepts the hypothesis that the HRM has a significant effect on organizational performance. Besides, the impact of innovation on the organizational performance obtained that the path coefficient was 0.149 with *p*-value of 0.043, which means significant. This result also accepts the hypothesis that innovation has a significant effect on organizational performance. Furthermore, testing the indirect effect of HRM with organizational performance through innovation shows the value of variance accounted for (VAF) was 20.57%, which means the role of innovation mediation on the effect of HRM on organizational performance was unmediation (Hair, Hult, Ringle, & Sarstedt, 2013).

Testing the size effect (f2) can provide information about the variations explained by exogenous latent variables on endogenous latent variables (Cohen, 1998). Criteria of (f2) area as follows: if the value is 0.02-0.15 (small effect), 0.15-0.35 (medium effect), and if > 0.35 (strong effect). The results of

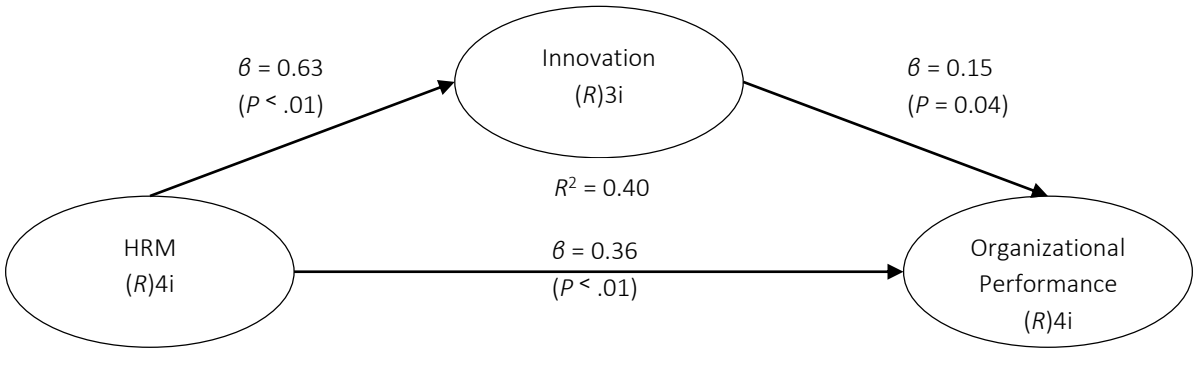

Figure 1. Analysis using WarpPLS

Table 5. Path coefficient direct effect and variance

Relationship among variables	Path coefficients	*p*-values	Effect size	SE	Remarks
HRM → Innovation	0.629	< 0.001	0.396	0.076	Highly significant
HRM → Organizational performance	0.362	< 0.001	0.164	0.082	Highly significant
Innovation → Organizational performance	0.149	0.043	0.055	0.086	Significant
Mediation effect using variance accounted for (VAF)					
HRM → Innovation → Organizational performance	Indirect effect	0.629 x 0.149 = 0.093721			VAF = 0.093721: 0.455721 = 20.57% (unmediation)
	Total effect	0.093721 + 0.362 = 0.455721			

the analysis (Table 3) show that the average effect size (f2) was 0.205, so it can be concluded that the formation of variation pattern in the relationship among latent variables in the research model is in the medium category. Thus, the expansion of the research model still enables to get more comprehensive results of the analysis.

4. DISCUSSION

Human resource practice (HRM) has become an increasingly important topic in the study of human resource management. The results of this study found out that HRM can improve the organizational performance. HRM is a way for management to influence and shape the skills, attitudes, and behavior of individuals in their work (Yu, 2013). Sheehan et al. (2013) stated that HRM is the result of HRD intervention in increasing the employees' capacity to contribute to innovation activities. HRM is also seen as a series of interrelated activities to attract, develop, and maintain the organization's human resources (Florén et al., 2016; Von Bonsdorff, Zhou, Wang, Vanhala, von Bonsdorff, & Rantanen, 2018). The implementation of effective HRM is through the implementation of recruitment, training delivery, performance assessment, and compensation system, which can foster the innovation organization (Budhwar et al., 2007; Chang et al., 2011). Also, the ability to develop the innovation can be predicted through the efforts by the organization to share the experiences and ideas (Mumford, Bedell-Avers, & Hunter, 2008; Nevalainen & Maijala, 2012; Wang & Noe, 2010; Riana, Rihayana, & Ratih, 2019). Innovation requires the transformation and exploitation of the existing knowledge in organizations (Lawson & Samson, 2001) through knowledge sharing. Okoe et al. (2018) emphasized that knowledge sharing is one of the outcomes of HRM.

One of the management processes that can be done to exploit and perform the transformation of knowledge is by HRM. The HRM concept has been widely adopted in organizational practices (Glaister, Karacay, Demirbag, & Tatoglu, 2018; Okoe et al., 2018) and is proven to be able to provide organizational opportunities to get the right employees, so it facilitates the implementation of innovation (Lu et al., 2015; Nieves & Quintana, 2018; Okoe et al., 2018). Besides, various activities of HRM enable the employees to feel more justice because they are allowed to get training, sustainable performance assessment, and fair compensation. Explicitly, Okoe et al. (2018) stated that HRM can increase job satisfaction, and can facilitate employees to do knowledge sharing, and can enable the employees to feel a friendlier workplace. Thus, those conditions can create the innovation behavior. This opinion is confirmed by Papa, Dezi, Gregori, Mueller, and Miglietta (2018) that HRM can strengthen the application of innovation because employees who are satisfied and feel friendly with the organization have a stronger desire to acquire the knowledge from the environment of the competitors.

The study also found that HRM was able to make organizations more competitive so that they could perform better. Madison, Daspit, Turner, and Kellermanns (2018) stated that HRM contributes significantly to improving the competitiveness of organizations. The implementation of HRM can improve the employees' capabilities and innovation behavior, so that it has implications for organizational performance (Cho, Woods, Jang, & Erdem, 2006; Lambooij, Sanders, & Koster, 2006; Silvia, Ermanno, & Francisco, 2016; Do et al., 2016), and it can even have an impact on sustainable performance (Zaid, Jaaron, & Bon, 2018; Rajiani, Haslinda, & Hardjono, 2016). On the other hand, several studies stated that innovation is one of the keys to organizational success in the competition

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(Chow, 2017; Sheehan et al., 2013; Johannessen & Skaalsvik, 2015; Gosh, 2015).

The findings of this study indicated that innovation has a weak effect on organizational performance. Innovation is often identified not only as a novelty of production (Yeh-Yun Lin & Yi-Ching Chen, 2007; Zhou & Shalley, 2007) but also as a novelty of administrative management (Clark, 2010), so it provides additional value to organizational output. Innovation is a mechanism in organization to produce new products, processes, and systems to adapt to changing environments (Lawson & Samson, 2001). Innovation creation requires the investment support in the field of human resources (Valdez-Juárez et al., 2016), which, on the other hand, it is also one of the weaknesses of SMEs, so it does not support the innovative climate. The development of innovation requires the ability of management to provide stimulus to the employees to develop the valuable experience into the organization's assets in creating the knowledge (Mathuramaytha, 2012).

When it is simultaneously modeled, it turns out that this study provides innovation findings that do not mediate the effect of HRM on organizational performance. This result informs that HRM contributes to improving organizational performance (Silvia et al., 2016; Do et al., 2016) and creating innovation (Nieves & Quintana, 2018; Okoe et al., 2018). However, innovation in SMEs does not have an impact on improving organizational performance. This result is contradictory with some studies (Yeh-Yun Lin & Yi-Ching Chen, 2007; El-Kassar & Singh, 2019; Chen, 2017) that innovation plays an important role not only in overcoming the pressure of competitors but also gaining a competitive advantage and better performance.

5. LIMITATIONS OF THE STUDY

Although it is not yet considered to be an essential role in improving the organizational performance of SMEs, innovation remains to be the key to corporate success in facing the competition in an ever-changing environment. Innovation is still seen as a driving of the organization to succeed in winning the competition. Kremer, Villamor, and Aguinis (2018) explained that innovation could be strengthened through creativity, voice, and knowledge sharing. Also, the development of innovation requires the support of innovative leaders to create an innovative culture (Coffman, 2015). This research is a quantitative study so that in the future, it is expected to be expanded to be able to clarify the effect of innovation on organizational performance by using a mixed method approach (quantitative and qualitative). Furthermore, testing the impact of innovation on organizational performance in SMEs needs to be carried out continuously, considering that innovation is deemed to be strategic in facing the competition in the 21st century. Innovation becomes a severe problem for SMEs because of the weak investment in the field of human resources that inhibits the implementation of innovation.

CONCLUSION

Although there is a growing understanding of the effect of particular HRM configurations on outcomes at the level of the organization, as well as on employees, but in Indonesia, there are still not many guiding frameworks that bring out what perspectives might mean where innovation is the focal point of interest particularly in the SMEs that become one of crucial elements in fostering the country's economic growth. The framework of HRM in this study can be used as a model of developing the innovation within SMEs in Indonesia, which is unique in management and different from the western counterpart.

The goal of this study in exploring the connections among HRM, innovation, and business performance has been accomplished. With a few researches done in this area, the current outcomes are not definitive; rare research has been completed in Indonesia so far making comparison with previous studies inaccessible. In any case, the finding from this research can be a beginning stage that HRM implementation in terms of recruitment, training, performance assessment, participation, and reward system can make the organization to have better performance allowing firms to be innovative. This suggests that organ-

izational capabilities related to innovation do not necessarily create competitive advantage. The crucial might be the organization's endeavor to utilize effectively these capabilities in molding the effective HRM system that contributes to better performance.

AUTHOR CONTRIBUTIONS

Conceptualization: I Gede Riana.
Data curation: Gede Suparna, I Gusti Made Suwandana.
Formal analysis: I Gede Riana, Gede Suparna, I Gusti Made Suwandana.
Funding acquisition: I Gede Riana, Gede Suparna, I Gusti Made Suwandana.
Investigation: I Gede Riana, Gede Suparna, I Gusti Made Suwandana.
Methodology: Sebastian Kot, Ismi Rajiani.
Project administration: I Gede Riana, I Gusti Made Suwandana.
Resources: I Gede Riana, Gede Suparna, Sebastian Kot.
Software: I Gede Riana, Ismi Rajiani.
Supervision: I Gede Riana, I Gusti Made Suwandana.
Validation: I Gede Riana, Gede Suparna, Sebastian Kot, Ismi Rajiani.
Visualization: I Gede Riana, Sebastian Kot, Ismi Rajiani.
Writing – original draft: I Gede Riana, Ismi Rajiani.
Writing – review & editing: Sebastian Kot.

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