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The Effect Of Strategy And Intellectual Capital On Firm Performance: The Moderating Role Of Corporate Governance

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Abstract
This study aims to examine the effect of corporate strategy and intellectual capital on company performance with corporate governance as a moderating variable. The study used secondary data with purposive sampling technique. The study was conducted on 135 manufacturing companies listed on the Indonesia Stock Exchange in 2019-2020. Partial test results showed that the influence of human capital on company performance is subscribed while the other hypotheses are rejected. Moderation testing showed that corporate governance strengthens the effect of capital employed on company performance while other hypotheses are rejected.
Keywords: differentiation, cost leadership, intellectual capital, human capital, structural capital, capital employed, company performance, corporate governance

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I. Introduction

The Covid-19 hit Indonesia in March 2019 and indeed had an impact on the economic sector. Indonesia's economic growth rate declined significantly in the second quarter of 2020 at -5.32% (covid-19.bps.go.id)[1]. The performance of the national manufacturing industry also decreased in March 2020 with the weakening of the Manufacturing PMI (Purchasing Managers' Index) from 51.9 in February 2020 to 45.3 in March 2020 and 27.5 in April 2020 (Kusumah, 2020). The data from the Central Agency of Statistics (BPS) shows that the decline in income occurred in the accommodation, food, and beverage business sector by 92.47%, while other sectors ranged from 70.67% to 87.93% (covid-19.bps.go.id).

Several studies have reviewed the company's performance before and during the Covid-19 pandemic focusing on the sub-sectors of construction services, restaurants, tourism, and hospitality. Kurniawan *et al* (2021) suggest that studies related to the impact of the Covid-19 pandemic not only examine the comparison of company performance before and during the Covid-19 pandemic but also examine the strategies that companies must carry out to survive and avoid bankruptcy. The competence of employees is also very determinant, especially in job adjustments, for example using technology when working from home (WFH) and adjusting work with health protocols while working in the office (WFO).

Within Porter's framework (1980), there are two strategies that companies can use to achieve a competitive advantage, namely differentiation and cost leadership. A differentiation strategy requires companies to make unique distinctions regarding marketing activities, technology, and especially product innovation. In the cost leadership strategy, the company builds market share by creating a low-cost position compared to other companies by improving processes, minimizing costs, and controlling overhead. Intellectual capital is a company's management competency, innovation ability, and problem-solving to achieve increased performance.

Several studies related to the influence of corporate strategy and intellectual capital on company performance have been carried out but show different results. Previous studies related to differentiation strategies used the measurement of R&D costs. Banker *et al* (2014) explained that it is possible that R&D competition also involves cost reduction. The company also never differentiated R&D related to product innovation and cost reduction separately. Therefore, in this study, the differentiation strategy was measured

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[1] https://covid-19.bps.go.id/

using the ability of premium prices. Previous research related to cost leadership looked at the purchase of property and equipment (Bhattarai, 2018). In this study, the cost leadership strategy was measured using the efficiency of asset utilization (Gani and Jermias, 2006). The efficiency of asset utilization shows the efficiency of the company's asset utilization. Several previous studies also only discussed in general terms related to intellectual capital without examining every indicator of intellectual capital (VACA, VAHU, and STVA), therefore this study aims at examining the effect of each indicator of intellectual capital.

Another significant difference is also identified in the results of previous studies due to differences in organizational conditions. Contingency theory explains that there is no universal system that can always be applied to every organizational environment. Inconsistency reconciliation efforts by finding conditional factors between variables with a contingency approach. The use of a contingency approach allows for a moderating variable of corporate governance.

II. Literature And Hypotheses Development

The resources owned by the company are an important part that determines the success of the strategy and the increasing the company's performance. Wernerfelt (1984) developed a resource-based concept that explains differences in performance between companies are related to variations in the resources and capabilities of the company. Resource-based view explains resource ownership is more important than industry structure to maintain competitive advantage. Companies have different characteristics due to differences in experience, assets, capabilities, and organizational culture. Several assets (resources) are key for the company in creating a sustainable competitive advantage.

Companies could run a differentiation strategy as a way to develop creative and innovative products, unique products that are different from competitors, and products with continuous development (Porter, 1980). Innovative products can be offered at a premium price as a signal that the product has high quality and is different from competitors. High product quality makes products have more bargaining power in the market and increases buying interest thereby increasing company performance. Companies that pursue innovation strategies tend to offer products that are different from competitors so that they are able to charge premium prices to their consumers. In accordance with the explanation above, the research hypothesis is proposed as follows:

H_1: Differentiation strategy gives a positive effect on company performance

The efficiency of asset utilization occurs when assets (resources) that have not been used optimally are utilized to produce more products so that product costs per unit are lower. Miles and Snow (1978) explain that companies can implement a cost leadership strategy to produce products at lower costs than competitors. The company's ability to produce at a lower cost than competitors with relatively the same product quality gives the company a competitive advantage. Based on the explanation above, the second hypotheses proposed in this study are:

H_2: Cost leadership strategy gives a positive effect on company performance

When a company has resources that are not easily imitated, it has a competitive advantage over competitors. One resource that is difficult for competitors to imitate is intellectual capital. Pulic (2000) developed the value-added intellectual coefficient method to measure intellectual capital with three indicators: value-added capital employed (VACA), value-added human capital (VAHU), and structural capital value-added (STVA). Human capital represents the competence, attitude, and intellectual property of employees. Structural capital is the result of organizational processes and values that reflect the company's external and internal focus. Capital employed is a tangible asset in the form of physical and financial assets that drive changes in business operations through the creation of new values that also improve company performance. One of the most significant assets the company has is the intellectual capital, an asset that is not easily imitated by competitors. It is important for the company because it helps the company gain a competitive advantage over other companies. Based on the explanation above, the following hypotheses are proposed:

H_{3a}: Human capital gives a positive effect on company performance

H_{3b}: Structural capital gives a positive effect on company performance

H_{3c}: Capital employed gives a positive effect on company performance

Novatiani *et al* (2018) explained that a differentiation strategy with the support of good corporate governance will improve company performance through monitoring the implementation of the strategy so that no stakeholder is harmed. Corporate governance carries out a monitoring function so that the implementation of differentiation strategies contributes to improving company performance. The principle of accountability ensures that the selection of product and service innovation strategies is in accordance with the capabilities of the company. Based on this explanation, the following hypothesis is proposed:

H_4: Corporate governance strengthens the influence of differentiation strategy on company performance

Jermias (2008) explains that companies with a cost leadership strategy are more efficient in using debt financing in order to improve performance. Funding through debt makes oversight by the board more stringent so that it is not used for personal gain. The principle of fairness emphasizes that the rights of stakeholders are guaranteed

and there is transparency in the management of debt financing. Gani and Jermias (2006) explain that independent commissioners tend to rely on results (outcomes) or financial controls in evaluating management performance due to a lack of information from internal parties. An independent board of commissioners will effectively limit the manager's opportunistic behavior by always evaluating the company's finances and outcome. This argument shows that increased supervision by independent commissioners can increase the effectiveness of the cost leadership strategy implementation. Based on this explanation, the following hypothesis is proposed:

H_5 : Corporate governance strengthens the effect of cost leadership strategy on company performance

Safieddine *et al* (2009) explained that intellectual capital is a determining factor whether a company can outperform competitors. Companies that have good governance standards and practices, for example protecting and respecting the rights of employees, are able to maintain the quality of intellectual capital. In addition, employees with quality knowledge will be interested in joining a company that has good governance because they think the company will pay attention to the human capital aspect. Companies also need to have good governance to protect and regulate patents, brands, databases, procedures, and organizational culture. Governance is a system that controls the company so that it is needed to maintain procedures and culture-oriented to value creation for internal and external parties of the company. Corporate governance has the responsibility to create, develop and utilize the company's overall assets, both intangible assets and physical and financial assets of the company. Based on this explanation, the following hypothesis is proposed:

H_{6a}: Corporate governance strengthens the influence of human capital on company performance

H_{6b}: Corporate governance strengthens the influence of structural capital on company performance

H_{6c} : Corporate governance strengthens the effect of capital employed on company performance

III. Methodology

This research was conducted on several manufacturing companies listed on the Indonesia Stock Exchange in 2019-2020. The sampling technique used in this research is purposive sampling by using criteria in sample selection.

Variable Measurement

Dependent Variable. The dependent variable in this study is the company's performance. This study uses financial performance to measure the success of the company. Researchers use ROA to measure financial performance. Return on assets can be measured by the following formula (Roslita and Anggraeni, 2019):

$$\textbf{\textit{Return on Asset}} = \frac{Net\ Income}{Total\ asset}$$

Independent Variable. The independent variables in this study are differentiation, cost leadership, and intellectual capital which consists of three indicators, namely: human capital, structural capital and capital employed. The differentiation strategy was measured using price premium capability. Cost leadership was measured using asset utilization efficiency. Companies are classified based on the implementation of differentiation strategy and cost leadership using cluster analysis (Singh and Agarwal, 2002). Companies that focus on differentiation strategies will be given a score of 1 (one) while other companies are given a value of 0 (zero). Likewise, companies that focus on cost leadership strategies will be given a score of 1 (one) while other companies are given a value of 0 (zero). Intellectual capital was measured by value added capital employed (VACA), value added human capital (VAHU), and structural capital value added (STVA) (Pulic, 2000).

$$\textbf{Differentiation} = \frac{Gross\ Margin}{Total\ Sales\ Revenues}$$

$$\textbf{Cost Leadership} = \frac{Total\ Sales\ Revenues}{Total\ assets}$$

$$\textbf{Human Capital} = \frac{VA}{HC}$$

$$\textbf{Structural Capital} = \frac{SC}{VA}$$

$$\textbf{Capital Employed} = \frac{VA}{CE}$$

VA : OUT-IN

Description:

OUT : output (selling)
IN : input (total expenses non employee expenses)
HC : human capital (employee expenses)
SC : structural capital (VA-HC)
CE : capital employed (total equity)

Moderating Variables. The moderating variable in this study is corporate governance. A well organized companie's governance is a system designed to guide companies professionally based on the principles of corporate governance. National Committee on Governance (KNKG) explains that there are five principles of corporate governance which are fairness, transparency, accountability, responsibility and independence. In this study, corporate governance was measured by the corporate governance index (Surifah, 2011) which adjusts the principles of corporate governance of the National Committee on Governance (KNKG) so that all five principles of corporate governance are used in the study.

IV. Result

The number of manufacturing companies listed on the Indonesia Stock Exchange from 2019-2020 is 166 companies. Of the 166 manufacturing companies, 135 manufacturing companies meet the predetermined criteria. The initial research data used were 270 data, but there were 45 outlier data.

Hypothesis Testing

Table *T* Test

Model	B	t	Sig.
(Constant)	-,051	-3,229	,001
Differentiation	-,112	-,964	,336
Cost Leadership	,022	,133	,895
Human Capital	,202	2,656	,008
Structural Capital	-,211	-1,659	,099
Capital Employed	-,965	-3,403	,001
Differentiation_GCG	,123	,870	,385
Cost Leadership_GCG	-,033	-,165	,869
Human Capital_GCG	-,180	-1,911	,057
Structural Capital_GCG	,294	1,824	,070
Capital Employed_GCG	1,273	3,670	,000

The T-Test Results table shows the t-test between differentiation and company performance resulting in a t-significance value of 0.336 > 0.05. Based on these results, it can be concluded that differentiation has no effect on company performance. The regression coefficient -0.112 indicates a negative relationship between differentiation and company's performance, so the first hypothesis is rejected. The results of the t test between cost leadership and company performance resulted in a t significance value of 0.895 > 0.05. Based on these results, it can be referred that cost leadership has no effect on company performance. The regression coefficient of 0.022 indicates a positive relationship between cost leadership and company performance, so the second hypothesis is also rejected.

The results of the t-test between human capital and company performance resulted in a t significance value of 0.008 < 0.05. Based on these results, it can be concluded that human capital has an effect on company performance. The regression coefficient of 0.202 shows a positive relationship between human capital and company performance, so hypothesis 3(a) is accepted. The results of the t-test between structural capital and company performance resulted in a t significance value of 0.099 > 0.05. Based on these results, it can be concluded that structural capital has no effect on company performance. The regression coefficient -0.211 shows a negative relationship between structural capital and company's performance, so hypothesis 3(b) is rejected. The results of the t-test between capital employed and company's performance resulted in a significance value of t 0.001 < 0.05. Based on these results, it can be concluded that capital employed has an effect on company performance. The regression coefficient -0.965 indicates a negative relationship between capital employed and company's performance, so hypothesis 3(c) is rejected.

The results of the t-test between the Differentiation*GCG interaction variable and company performance resulted in a t significance value of 0.385 > 0.05 with a regression coefficient of 0.123. Based on these results, it can be referred that corporate governance does not moderate the effect of differentiation on company's performance, so the fourth hypothesis is rejected. The results of the t-test between the interaction variables Cost Leadership*GCG and company performance resulted in a t significance value of 0.869 > 0.05 with a regression coefficient of -0.033. It can be said that corporate governance does not moderate the effect of cost leadership on company performance, so the fifth hypothesis is rejected.

The results of the t-test between the interaction variables of Human Capital*GCG and company performance resulted in a t significance value of 0.057 > 0.05 with a regression coefficient of -0.180. Through these results, it can be said that corporate governance does not moderate the influence of human capital on company performance, so hypothesis 6(a) is rejected. The results of the t-test between the Structural Capital*GCG interaction variable and company performance resulted in a t significance value of 0.070 > 0.05 with a regression coefficient of 0.294. It can be concluded that corporate governance does not moderate the influence of structural capital on company performance, so hypothesis 6(b) is rejected. The results of the t-test

between the interaction variables of Capital Employed*GCG and company performance resulted in a t significance value of 0.000 < 0.05. Based on these results, it can be concluded that corporate governance moderates the effect of capital employed on company performance. The regression coefficient of 1.273 indicates that corporate governance strengthens the effect of capital employed on company's performance, so hypothesis 6(c) is accepted.

V. Discussion

Advances in technology and information make product and service innovations implemented by companies easily imitated by other companies. Competitors apply systematic methods to obtain new information and techniques that spread rapidly throughout the industry, resulted in many companies failing and unable to take advantage of adopting innovative tools and techniques to increase sustainable profitability. Strategy determination carried out by the company had not carefully considered the company's capabilities. The differentiation strategy with the creation of new products must be supported by resources' capability to adapt. The company has not properly considered the company's ability to implement a differentiation strategy so that the implementation of the strategy does not contribute to performance.

Companies that are unable to adapt to environmental changes and rely on efficient use of assets to generate cost efficiency cannot serve a wide market. Companies with a strategy of distinguishing consumers with low brand awareness and bargaining intensity are influenced by affordable prices. The market share may be narrower when consumers switch to higher quality products, making it difficult for companies to improve performance. Cost leadership strategy based on operating efficiency is easier to imitate by competitors so that competitive advantages and performance improvements will not be created. Meanwhile, cost leadership is focused on cost reduction and price conscious customers serve only a narrow market. This makes improving company performance difficult to achieve. When governance continuously focuses on monitoring cost leadership strategies, the market served may be narrower because consumers are influenced by factors other than price, such as product quality.

Value added resulting from each cost incurred by the company show that the company has managed human resources optimally so as to produce labor products which in turn will improve the company's financial performance. Companies that improve employee capabilities, for example carrying out training will experience an increase in performance because high quality human capital is able to make companies operate more effectively and efficiently. Isanzu (2015) explains that the amount of structural capital needed by the company has not been able to meet the company's routine processes in producing optimal performance, without being accompanied by good structural capital management such as system management, procedures, databases, thus hampering employee productivity in generating value added (VA). These poor systems and procedures make the company not have guidelines in carrying out business processes so that it cannot achieve maximum performance. Investment in tangible assets in the form of physical and financial assets without good asset management skills will make the company's performance decline. When the company adds tangible assets but is not matched with company resources to create value added from the addition of physical assets, the company's performance will decrease.

The company has not sought maximum employee empowerment because the company's focus is on preventive measures to deal with the Covid-19 pandemic. During the Covid-19 pandemic, the workforce is experiencing a high risk of layoffs, reduced wages, late payments, and forced leave. Companies are not yet aware of the structure, system and culture of the company as intangible assets that must be managed properly. The company has not paid more attention to the use of structural capital as a source that contributes to asset utilization and performance improvement. The organizational structure, processes, culture, and routines of the company are seen as something that the company must have, not as an intangible asset that the company can manage to improve performance.

Whilst corporate governance does not moderate the effect of human capital and structural capital on company's performance, corporate governance strengthens the effect of capital on company's performance. This proves that the company has succeeded in managing physical and financial assets to improve performance. The focus of physical and financial capital management contributes greatly in improving the company's work. Al-Musali and Ismail (2014) explain that tangible assets remain the most significant basic resource related to financial performance compared to intangible assets so that the management of tangible assets is also an important concern.

VI. Conclusion

This study examines the effect of corporate strategy and intellectual capital on company performance with corporate governance as a moderating variable. The corporate governance variable is treated as a pure moderator variable. The study was conducted on manufacturing companies listed on the Indonesia Stock Exchange in 2019-2020 with 135 sample companies and 225 research data tested.

Hypothesis testing shows that human capital has a positive effect on company performance. Whilst corporate governance does not moderate the effect of human capital and structural capital on company's performance, corporate governance strengthens the effect of capital on company's performance. This research has its limitations especially on its time-frame. This study only examines the impact of strategy implementation on company performance in year t. The impact of implementing the strategy on the company's performance may occur in the coming year. Future research is expected to examine the impact of implementing corporate strategy on performance at t+1 and t+2. The implementation of the strategy in year t may have an effect on performance at t+1 or t+2.

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