Effect Of Human Capital And Competitive Strategies Against The Financial Performance Of Small And Medium Enterprises

Enni Savitri, Almasdi Syahza

Abstract: The purpose of this study is to analyze the effect of human capital on financial performance, the effect of human capital on competitive strategies and the influence of competitive strategies on financial performance. The samples consists of 68 SMEs managers in Province of Riau engaging in the manufacturing sector. The results using Path Analysis show that human capital have an effect on financial performance and on competitive strategies. Competitive strategies has an effect on financial performance. Human capital is important for choosing the right competitive strategy. The selection of the right competitive strategy improves financial performance. The selection of the right competitive strategy is necessary in the creation of strategies and of varied products. Improved financial performance is reflected by the growth of industrial assets and when SMEs focused on certain areas.

Index Terms: human capital, competitive strategies, financial performance.

INTRODUCTION

Small and Medium Enterprises (SMEs) are constantly growing and developing. Even though they are small scale businesses, their roles are very significant in supporting the economy and creating new jobs. The Province of Riau is an area with an abundant potential and has many natural resources, both land and maritime. Making it as the province one of the regions with investment developments from throughout Indonesia. Another advantage is the conducive atmosphere that is always maintained so when investors glance at this area they will invest in business capital. Riau's potential is demonstrated by high investment in the area. This can be seen from the economic growth which is always above the national average. The economic growth is very good and continues to increase. In addition, conducive conditions in Riau are one of the main assets in assisting the development of business. Empowerment of the SME sector is one of the pillars of Riau's economy. Nationally, SMEs accounted for more than 51.2 million business units or 99.98 percent of the total economic contributors and their contribution to the workforce reached 97.04 percent of the total workforce.

Small and Medium Business contributors in the Province of Riau continue to increase over time. The growing awareness of becoming an entrepreneur is one of the main factors of this increase. Every year the growth of SMEs in the Province of Riau ranges from 5-10 percent. In 2016, The number of SMEs in Riau in the field of trade was 77,156, services field was 19,656, production field was 12,760, and industrial field was 11,320. The number of SMEs in Bengkalis Regency was 42,029. SMEs in Bengkalis Regency in the Province of Riau needed financial assistance to develop healthily. In 2018, the Provincial Government sought to allocate capital assistance to Cooperatives. The same assistance was given to empower SME's so that their business productivity grew. Each SME received funds from the Bengkalis Regency Government ranging from IDR 10-IDR 200 million and Rp20 million. (Sari, 2016).

- ***Enni Savitri**, Department of Accounting, Faculty of Economics and Business, Universitas Riau, Indonesia, enni.savitri@lecturer.unri.ac.id*
- ***Almasdi Syahza**, Faculty of Teachers Training and Education, Universitas Riau, Indonesia, almasdi.syahza@gmail.com*

One solution to overcome the problems that affects the SMEs financial performance is to look at human resource-based business management (Resource Based View - RBV). With this management the company is able to create special competencies (Barney, 1991; Grant, 2010). The RBV theory states that resources and capabilities are the basis for forming strategies. The chosen strategy must enable the company to use its core competencies for opportunities in its external environment. The problem is that not all resources and capabilities of the company have the potential to be a basis for a sustainable competitive advantage.

There are various problems that are generally related to SMEs in carrying out their business. One obstacle that often arises is the sustainability of the economic wheel of the local community, especially in the middle to lower economic areas. Other problems are difficulties in guaranteeing access to capital, problems in marketing, lack of guidance and lack of assistance from the government. There relating to the management of SMEs, namely Law No. 20 concerning Business, Small and Medium Enterprises (2008). There are many aspects contained in the constitution, which are of public concern, including the aspects of financing and guarantees, which is often called "access to finance" for SMEs.

Assessment of financial performance in SMEs is very important to complete as this helps to maintain the viability of its business. Small and medium-sized companies can describe the development of their business by looking at their simple financial performance. Studies on SMEs that measure general financial performance were assessed by profitability. Studies that support the concept of direct influence of human capital on financial performance were (Nahkata, 2007), (Pierre, 2011) and (Kilicman, et.al, 2018). The management of the company special competencies can be created (Grant, 2010). (Leitner, 2001) and (Ardiana et al, 2010), show no influence of human capital on financial performance. (Pribadi & Kanai, 2011), and (Sampurno, 2010) support the notion that human capital influenced competitive strategy. The research of (Finney et al., 2005), (Amoako-Gympah, 2008), (Kong and Thompson, 2009) and (Muchtolifah, 2008) show that human capital did not have an influence on competitive strategies. There is an influence between competitive strategies and financial performance, namely Finney et al. (2005). While the research of (Musyarofah, 2004) found there was no affect by competitive strategies on financial performance.

The difference with previous research is the measurement of the performance of SMEs specifically based on intangible asset investments, namely human capital and the selection of competitive strategies with reference to the grand theory of RBV. Variations were also noted in previous research results. These observations highlighted a research gap and so then created motivation for the researcher to confirm and research further the financial performance of SMEs. The focus of this research was to see whether financial performance increased through human capital that was owned directly or mediated by competitive strategies. The purpose of this study is to analyze the effect of human capital on financial performance, the effect of human capital on competitive strategies and the influence of competitive strategies on financial performance. The results show that human capital have an effect on financial performance and on competitive strategies. Competitive strategies has an effect on financial performance. Human capital is important for choosing the right competitive strategy. The selection of the right competitive strategy improves financial performance. The selection of the right competitive strategy is necessary in the creation of strategies and of varied products. Improved financial performance is reflected by the growth of industrial assets and when SMEs focused on certain areas.

Literature Review

Resources Based View Theory

Concern about company resources began with (Penrose, 1959). Penrose investigated how internal management processes influenced the behavior of a company by understanding that the company has a collection and combinations of resources. Penrose developed the theory of *the growth of the firm*. Penrose's concept confirmed that company growth was limited by opportunities that existed as a function of a group of productive resources that were controlled / owned by the company (Barney, 1991). Penrose also explained that the learning process created new *knowledge* and formed the basis of organizational growth through combining existing resources (Eisenhardt & Santos, 2000).

The RBV view is a method for analyzing and identifying the strategic advantages of a company based on a review of the combination of assets, expertise, capabilities, and intangible assets that are specific to an organization. The assumption underlying RBV is that companies differ fundamentally because each company has a "collection" of unique resources in the form of tangible and non-intangible assets and organizational capabilities to utilize these assets. Each company develops competencies from these resources and when it is well-developed, these competencies are a source of corporate competitive advantage (Pearce & Robinson, 2011).

The basic reason for RBV is that the guidance, type, amount and nature of a company's resources must be considered first and foremost in choosing and defining strategies that can lead to a sustainable competitive advantage. Strategic management according to the RBV involves the development and exploitation of the company's unique resources and capabilities and makes an effort to continuously maintain and strengthen these various resources. This theory states that it is very profitable for a company to run a strategy that is currently not implemented by any competing company. When other companies are unable to duplicate certain strategies, the companies that run them have the sustainable competitive advantage. However, to be valuable, a resource should be scarce, difficult to replicate and cannot be easily replaced.

Human Capital

(Choo and Bontis, 2002) define Human Capital (HC) as a supply of knowledge and skill of workers in an organization or company who combine to solve business problems. (Daum, 2005) defines HC as a source of innovation and renewal because new and good ideas are created / produced by humans. From these two definitions, it is implied that humans find new products, find creative ways to reduce costs, provide good services, and are able to build relationships with customers and stakeholders for the long term. Likewise, HC is the people in organizations / companies whose collective skills, knowledge, and capabilities are pooled. Human Capital can be difficult for competitors to emulate (Fletcher *et al*. 2005). HC in this context includes individual human capabilities that work for companies, both workers and managers who have skills, knowledge, competencies, and experience (Daum, 2005).

Humans are an important element to be developed because the knowledge they have is a critical for increasing the competitive advantage. This is based on the theory of RBV, that companies can explain company performance by the variations in different resources and capabilities. HC already has VRIN criteria which are the basis for achieving company competitive advantage (Hitt et al, 2001; Choo & Bontis, 2002; Pablos & Lytras, 2008; Kong & Thompson, 2009).

Competitive Strategy

The analysis results of the company's internal and external environments are information needed to form a strategic intent and develop a strategic mission (Hitt *et al*., 2001). Strategic intent is the utilization of internal resources, capabilities and the core potential of the company to do what was originally considered a goal and cannot be achieved in a competitive environment. The strategic intent reflects what the company can do as a result of its core competencies and unique ways that can be used to build a competitive advantage and gain profit above the sustainable average. A business-level strategy is based on the specific core competencies of a company and indicates how an organization intends to compete in a particular product market and gain a competitive advantage over its competitors. To implement the strategy as a tool to achieve organizational goals, a management function is needed. Implementation of strategies is part of Strategy Management. Strategy management is a series of managerial decisions and actions that determine the company's performance in the long run. Management strategies include environmental observation, strategy formulation, strategy planning and long-term planning. Strategy is implemented, evaluated and controlled (Wheelen & Hunger, 2001: 4).

Strategic resources owned and controlled by the company are used as a basis for formulation and implementation of strategies to realize optimal business performance (Grant, 2010). In addition, (Barney, 1991) emphasized that the continuity or excellence of a company depended on the resources it has, what strategies are chosen to empower these resources so that they are able to respond to opportunities and challenges from their external environment. (Finney and Campbell, 2007) argues that heterogeneous resources lead to a variety of strategies implemented and differences in benefits obtained by the company. That is, the meaningfulness of the strategy in producing a competitive advantage can be realized if the determination and implementation of the strategy is based on company resources. The strength of the resources will result in producing a positive company performance.

Methodology

The population of this study is from all the SMEs in the Bengkalis Regency in the Province of Riau. 120 SMEs have the potential to strengthen the economy of the community. The sample is drawn engaging in the manufacturing sector and produce products that could be sold in the Bengkalis district or were exported. There were 80 managers or owners. The respondent was the owner of the company or company manager. The research data came from primary data through questionnaires. Two variables are studied, exogenous variable (free) and endogenous variables (bound). Exogenous variable is one, the namely human capital (X) and it is part of intangible assets. The exogenous variables consist two, namely competing strategies (Y_1), and financial performance of SMEs (Y_2). Data analysis in this study used descriptive statistics and path analysis.

Results

Testing of Direct Effects

The results of testing the hypothesis directly between the variables of human capital, competing strategies and financial performance are shown in Table 2. The table shows the value of the path coefficient, p-value and the significance of each variable.

Table 1. Results of Direct Influence Analysis

Variable Relationships	Coefficient	t statistic	p value	Info
Human capital (X) -> Financial performance (Y_2)	0.366	2.087	0.048	Significant
Human capital (X) -> Competitive strategy (Y_1)	0.816	6.923	0.000	Significant
Competitive strategy (Y_1) -> Financial performance (Y_2)	0.550	3.135	0.005	Significant

In Table 1, human capital influences financial performance (0.048). Human capital has an effect on competitive strategies (0.000) and competitive strategies affected financial performance (0.005). It can be concluded that human capital is very influential on competitive strategies.

Testing of Indirect Effects

Indirect testing aims to determine the position of the results of the intervention examination of mediation variables, whether proven to be perfect mediation variables or partial mediation. The results of the examination on indirect influences are used to justify whether the model based on the RBV theory is acceptable or not. Tests were carried out as follows:

Step 1: Calculate the path coefficient by entering the competitive strategy variables into the model. See test results in Table 2.

Table 2. Results of Mediation Test Analysis with Competing Strategy Variables

Variable Relationships	Coefficient	p-value	Info
Human capital (X) -> Financial performance (Y_2)	0.366	0.048	Significant
Human capital (X) -> Competitive strategy (Y_1)	0.816	0.000	Significant
Competitive strategy (Y_1) -> Financial performance (Y_2)	0.550	0.005	Significant

Step 2: Calculate the path coefficient without entering the competitive strategy variable in the model and test results, see Table 3.

Table 3. Results of Analysis of Mediation Tests Without Competitive Strategy Variables

Variable Relationships	Coefficient	p-value	Info
Human capital (X) -> Financial performance (Y_2)	0.814	0.000	Partial Mediation

Table 3 illustrates the relationship between the variables of human capital, competitive strategies and financial performance. It can be seen that the values of human capital on financial performance, human capital on competitive strategy and competitive strategy on financial performance significant, based on audit standards to determine mediation position. The mediation model shows indirect effect of human capital influence on financial performance though competitive strategies has a partial mediation. These results indicate that the higher the human capital investment is mediated by the selection of competitive strategies, the higher the financial performance of SMEs. This means the results in this study showed that human capital can directly improve financial performance, financial performance can be achieved if mediated by the implementation of competitive strategies. The integration model of human capital, competitive strategies and financial performance in total experienced a higher change in producing financial performance.

Discussion

Effects of Human Capital on Financial Performance. Every decision related to the organization will be determined by the human capacity of the organization and has an impact on achieving organizational performance. Humans in organizations / companies with skills, knowledge and capabilities present human capital and are very difficult to imitate by competitors (Fletcher *et al*. 2005). This is based on the company's Resources Based View (RBV) theory which explains the differences in company performance are due to variations in resource differences and capabilities. The skills possessed by managers of SMEs of various types of food companies needed a majority of production skills. Production skills were more important than financial management skills, administrative skills, communication skills, and cooperative skills in these organizations. This is in accordance with the results of interviews of several SMEs of various foods companies in the Bengkalis Regency of the Province of Riau. The results of this study were consistent with research from (Hitt, *et al.*, 2001) and Coleman (2007). This study does not support the Ardiana et al. (2010), show that the element of *human capital* did not improve performance, in this case that managers or managers of SMEs relied more on business intuition (Leitao & Franco, 2008).

Effect of Human Capital on Competitive Strategies. The results of the analysis showed that the influence of human capital on the selection of competitive strategies of SMEs showed that the higher the human capital investment the more appropriate the selection of competitive strategies for SMEs. Human capital did not directly improve financial performance but could indirectly improve financial performance if mediated by competitive strategies. Human capital is able to improve the strategy of competing in various food SMEs from knowledge through to formal education, as well as knowledge and training. Knowledge came from job experience and family experience, skills through production skills, communication skills, working with organizations and making financial reports. Various food SMEs have been implemented properly by the ability to manage the business, make decisions, to lead, to be innovative and to adapt to environmental changes. This research support (Sampurno, 2010) who stated that the alignment between human resources and business strategies had an influence on company performance. Other studies did not support that human capital had an influence (low influence) on performance if not mediated by Porter's competitive strategy (Hitt et *al et.*, 2001).

Effect of Competing Strategies on Financial Performance. The results of the analysis showed competitive strategies influenced the financial performance of SMEs. This demonstrates that the more precise the selection of competitive strategies, the higher the achievement of financial performance of various food SMEs. Winning the competition and gaining profitability is the goal that every company wants to achieve. Companies will get different profitability depending on what strategies they use to win the competition. In this case the company needs to implement a business strategy in determining position and maintaining that position in the industry. Improvements resulted in increased sales in general, neutral in obtaining profits and growth in various food SMEs in Bengkalis District in the Province of Riau. The integration model of this study is relevant to the RBV concept, which explains that the company's unique resources and capabilities are the basis for forming a strategy. The chosen strategy must enable the company to use its intimate competence to build opportunities in its external environment. RBV assumes that every organization / company has a unique set of resources and capabilities that are the basis of the strategy and are the main source of company returns. This study support (Ortega, 2010) who states that the cost of leadership strategies was positively related to company performance. Different findings from (Nikat, 2015) stated that leadership cost strategies did not affect the performance of SMEs, the application of good business strategies was the way to achieve a competitive advantage.

Conclusion and Recomendation

Conclution

The selection of the right competitive strategy is necessary in the creation of strategies, as well as the creation of varied products. SMEs must focus on certain segments in order to be able to improve financial performance. This was then reflected in the growth of the industrial assets. The skills possessed by managers of SMEs of various types of food companies needed a majority of production skills. Production skills were more important than financial management skills, administrative skills, communication skills, and cooperative skills in these organizations. This indicates that labor has a role in competing strategies as mediation provides higher changes between increasing human capital towards the financial performance of various food SMEs. Human capital is able to improve the strategy of competing in various food SMEs from knowledge through to formal education, as well as knowledge and training. Knowledge came from job experience and family experience, skills through production skills, communication skills, working with organizations and making financial reports. Competitive strategies that are able to improve financial performance in various food SMEs were illustrated in general by various food SMEs choosing different strategies.

Recomendation

Perform better. Further research should explore more deeply, and in more detail, the intellectual capital owned by SMEs such as human capital, structural capital, relational capital, and spiritual capital. Knowledge of these areas can be used as a reference in implementing business strategies to support better performance achievement. Managers of SMEs in the Province of Riau could improve the performance of their SMEs by actively participating in education and training in order to improve their employee skills and experience. This then could ensure Human Resources can support future employees who come so that employee performance can continue to increase.

References

[1] Amoako-Gyampah, K., and Acquaah, M,"Manufacturing Strategy, Competitive Strategy and Firm performance: An Empirical Study in a Developing Economy Environment." International Journal of Production Economics, Vol.111, No.1, pp. 575-592, 2008

[2] Ardiana, I.A., Brahmayanti., and Subaedi, "Human Resouces Competency, The Effect on The Performance of SMEs at Surabaya", Management Journal and Entrepreneurship, Vol.12 No.1, pp 42-55,2010.

[3] Barney, J, "Firm Resources and Sustained Competitive Advantage", Management Science, Vol. 17, No.1, pp 99-120,1991.

[4] Choo, C.W., & Bontis, N, "The Strategic Management of Intellectual Capital and Organization Knowledge". New York: Oxford University Press, 2002.

[5] Coleman, J.S, "The Role of Human and Financial Capital in the Profitability and Growth of Woman-Owned Small Firms". Journal of Small Business Management, Vol 45, No.3. pp 303. 2007

[6] Daum, J.H. (2005). Intangible assets-based enterprise management – a practical approach. This paper has been presented at the 2005 PMA IC Syposium, Stern School of Busines, New York University, NYC/USA. [Online] Available at http://juergendaum.com/news/0115_2006.htm

[7] Eisenhardt, K.M., and F.M. Santos. "Resources-Based View: A New Theory of Strategy". Stanford University. 2000.

[8] Finney, R.Z., Cambell, N.D., and Powell, C.M. (2005). Strategies and Resources Pathways to Success?. *Journal Of Business Research,* Vol 58, pp 1721-1729.

[9] Finney, R.Z., and Lueg, J. E. Campbell, Market Pioneers, Late Movers, "The Resources-Based View (RBV): A Conceptual Model", Journal of Business Research, pp 925-932, 2007.

[10] Fletcher, P. R.J. Thomas, & S.A, Cantrell, "Human Capital Management, Managing and Maximizing People to Achieve High Performance", SAP White Paper, Accenture, 2005.

[11] Grant, R.M, Contemporary Strategy Analysis, 7th Edition, John Wiley and Sons, Ltd, 2010.

[12] Hitt, MA., Bierman, L. Shimizu, K. & Kochhar, R, "Direct and Moderating Effect of Human Capital on Strategy and Performance in Prodessional Service Firm: A Resource-Based Perspective". Academy of Management Journal, Vol 44. No.1. pp 13-28, 2001.

[13] Kilicman, A., Poh, L. T. Ibrahim, S. N. I, "On Intelectual Capital and Financial Performance of Banks In Malaysia", Cogent

Economics And Finance, Vol 6, Issue 1, pp 1-15, 2018.

[14] Kong, E., and Thompson, S.B. "An Intellectual Capital Perspective Of Human Resource Strategies And Practices", Knowledge Management Research and Practice, Vol 7, pp 356-364, 2009.

[15] Leitao, J. & Franco, M, "Individual entrepreneurship capacity and performance of SME. University of Beira Interior. [Online] Available at http://mpra.ub.unimuenchen.de/8179/MPRA Paper No. 8179, 2008.

[16] Leitner, K, "Intangible Resources and Firm Performance: Empirical Evidence from Austrian SMEs". Paper prepared for the 16th Nordic Academic of Management Meeting Uppsala 16th-18th August, 2001.

[17] Muchtolifah, "Influence of Human Resource, Market Orientation, Entrepreneurial Orientation Against Competitives Strategy and Hospital Performance", Disertation, Brawijaya University, 2008.

[18] Musyarofah. S, "The Influence of Budget Used and management Style to The Relationship Strategic Change and Company Performance", Indonesia Accounting and Auditing journal, Vol. 8, No.1, pp 43-63, 2004.

[19] Nahkata, C, "The Effects of Human Capital and Entrepreneurial Competencies on the Carrer on The Career Success of SMEs Entrepreneurs in Thailand", The Bussiness Review, Cambridge, Vol. 9, No. 1, pp 62, 2007.

[20] Nikat Kaya, "Corporate Entrepreneurship, Generic Competitive Strategies, and Firm Performance in Small and Medium-Sized Enterprises", Procedia - Social and Behavioral Sciences, Vol.207, pp 662 – 668, 2015.

[21] Ortega E.P, Azorín J.F. and Cortés E.C, "Competitive Strategy, Structure And Firm Performance: A Comparison Of The Resource-Based View And The Contingency Approach". Management Decision, Vol.48, No.8, pp.1282-1303, 2010.

[22] Pablos.P.O and Lytras M.D. "Competencies and human resource management: Impications for organizational Competitive Advantage", Journal of Knowledge Management, Vol.12, No.6, pp 48-55, 2008.

[23] Pearce II, J.A., and Robinson, J.B. (2011). Management Strategy, Formula, Implementation and control. 10th Edition, Book 1. Salemba Empat: Jakarta.

[24] Penrose, E.T, The Theory of the Growth of the Firm. Oxford: Basil Blackwell, 1959.

[25] Pierre, J.S. "Intangible Assets and Performance Analysis on Manufacturing SMEs". Journal of Intellectual Capital, Vol.12, No.2, pp 202-223, 2011.

[26] Pribadi, H., & Kanai, K. "Examining a Exploring Indonesia Small and Medium Enterprise Performance : An Empirical Study". Asia Journal of Business Management, Vol.3, No. 2, pp 98-107, 2011.

[27] Sampurno. Strategic Management, Creating a Sustainable Competitive Advantage, UGM Press: Jogyakarta, 2010.

[28] Sari, G. F. 2016. The Amount of SMEs at Pekanbaru, Riau., Indonesia, [On-Line] Available at: https://www.antarariau.com/berita/80571/jumlah-umkm-di-pekanbaru-mencapai-67728

[29] Wheelen, L.T., & Hunger, J.D, Strategic Management,5th Edition, Andi: Yogyakarta, 2001.

[30] Law No.20, About Small Medium Enterprises at Riau Province, 2008