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JURISMA

CHALLENGES IN PERSPECTIVE ON CORPORATE STRATEGY

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ABSTRACT

There are several issues in corporate strategies such as the impact of corporate to performance, the cause and limit of performance, development management and external environment of corporation. This study aims to discuss those issues based on literature review. It is found out that corporate impact to performance is non-neglectable, event though the degree of impact is still unknown. Experience managerial service are important for company to achieve its performance and to achieve its performance, corporation may choose between two approaches incremental and comprehensive, each approach has its own benefits and drawbacks. As a result, it should be aligned with internal and external condition of the corporation and the cost and benefit aspects. External aspect of the corporation in this particular, macroeconomic uncertainty, will influence the strategy of corporation even when the firm only play in local market. In addition, national economic development will impact on how corporation build its strategy.

***Keywords**: corporate strategy, corporate-impact, corporate performance.*

INTRODUCTION

As the company grows, it will have variety of business that plays in several market or industries. To manage several company the parent company will need corporate strategy to help the holding to increase its value as a whole. Corporate strategy defines set of plan and action to achieve identified purpose (Lynch, 2008). Corporate Strategy is the decision of the company that determines its objective, policies and strategy to achieve the goals (Foss, 1997). Corporate strategy applies to whole enterprise whereas business strategy defines the products and market of business within the firm (Foss, 1997). Corporate Strategy is designed to achieve company's competitive advantages through several activities to choose and to manage several businesses in several markets (Michael A, et al., 2007).

There are several subjects that worth to discuss in corporate strategy. Firstly, whether there is impact of corporate into profitability as previous study is still undecided. Study done by Rumelt (1991) and (Schmalensee, 1985) argued that there is no corporate effect to profitability. However, Bowman (2001) contend there is corporate effect into firm's performance. Secondly, the performance of the corporate and the matters that should be considered in achieveing the performance. Some studies defined performance as profitablity (Schmalensee, 1985), size, and growth. Thirdly, the management development to achieve performance as there are two options provided; incremental and comprehensive approach. Fourthly, the external environemnt of the firm as firm plays in multiple markets and industries that perhaps across the nation.

This paper aims to discuss the issues in corporate strategy as mentioned above based on literature review. The authors will start the paper with the rationale of the impact of corporate strategy followed by the discussion on firm's performance and the limit and trigger to achieve those performance, in this case we will focus only to growth and size. Next, we explain the management development to accomplish performance. Thereafter, we will elaborate how the firm deals with its macroeconomic uncertainty such as change in exchange rate, interest or inflation. In addition, we will also discuss the conglomeration in emerging market.

LITERATURE REVIEW

The Impact of Corporate Strategy

The study done by Bowman & Constance E, (2001) elaborated previous research that argued that corporate strategy has no or little impact to performance (ROA,market share, and Tobin'q). For that reason, Bowman (2001) provides logical explanantion to show that corporate strategy has effect on performance. His arguments based on theorytical aspect, issues in variance decomposition, and statistical issues.

Theoretical aspect. Bowman (2001) stated some studies earlier has shown the impact of corporate strategy to performance. The study done by Rumelt (1991) shows that scope of firm, in this matter is related diversification, has impact to profitability. In addition, vertical intergration is benefial when the transcation cost is huge (Williamson, 1975). Furthermore, corporate core compentencies is important (Prahaland & Hamel, 1990). In regard with organizational structure, Williamson (1975) and Chandler (1977) specified that coporation structure is important to separate line of business. Williamson (1975) also stated the advantages of internal capital market in corporation. Moreover, corporate management that includes managerial capability for whole company and for each individual business has influenced on profitability (Andrew, 1987, Hambrick & Mason, 1974). Correpodently, Bowman (2001) indicated that factors mentioned above (scope of business, core competencies, organizational structure, planning and culture and corporate management) are the five concern of corporate strategy.

Issues in variance decomposition. Bowman (2001) specified that previous study decomposed the variance of company performance into components that associated with industry, business, corporate effect. Thus, it fails to capture to see the advantages for the parent company as a whole. One thing to note that we cannot conclude that which components (industry, corporate and business) has more important roles to firm's performance. However, we can conclude that corporate effect in not negligible to firm's performance as shown in previous study using variance decomposition as summarized in table 1.

Table 1. Previous Study on Corporate Effect

STUDY	CORPORATE EFFECT
Schmalensee (1985)	a. zero (using ANOVA) b.not included (variance components)
Kessides (1987)	a.1 to 8 % b. 11 to 54 %
Wenerfelt and Montgomery	0.2 to 3.7%
Kessides (1990)	5.1 to 9.8%
Rumelt (1991)	Using sequential analyst of variance : a. 14.8 to 17.6% (mkt share ≥ 1%) b. 10.9 to 11.6% (mkt share > 0%) Using variance components : a. 0 % b. 1.6%
Roquebert et al (1996)	17,9%
McGahan and Porter (1997)	Using sequential analyst of variance: 9,1 to 11,9% Using variance components : 43%

STUDY	CORPORATE EFFECT
McGahan and Porter (1998)	*8.8 to 23.7%*
McGahan	*a. 0 to 1 %* *b. 8.3%*
Chang and Singh (1997)	*market share ≥ 1%* *a. 0% b. 1,6% (3 digit SIC)* *sales ($2 million to $2 billion) :* *a. 4,3% b. 8,5%*
Bercerra (1997)	*a. 12 % (ANOVA)* *b. 4,71% (Variance Components)* *c. 3,05 to 10,95% (repeated random factor)*

Statistical issues. Bowman (2011) mentioned that there are several statistical issues on previous studies such as data sample and statistical technique. In data sample, previous studies included single business firms that make it difficult to differentiate business and corporate effect. In addition, single business firms are lowering the effect of corporate level. This is in line with the study done by McGahan & Porter (1999), after took out the single business in the sample, the impact of corporate strategy rose by ten percent. Another issue that Bowman (2011) noted that the definition of industry and business. Logically, when the study defines industry broadly, it will higher the number of businesses that consider as a single business, thus, the impact of corporate strategy be low. In contrast, if the definition of the industry is narrow, then impact will be higher. Moreover, most of the studies classify the industry based on four digit Standard Industrial Classification (SIC), the 1-digit classification is general and the 4-digit is the most classification that consist the most specific information about the industry and contain single business firm as well. Thus, it misjudges the impact of corporate strategy as it also included single business firm.

Most of study used analysis of variance and variance components. However, Bowman (2011) argued that those technique have their limitation. Analysis of variance using dummy variables, and the justification in selection of dummy variables used are questionable. In addition, each industry has different characteristic, but in analysis of variance, it might categorize the variables in general term such as size or sales. Furthermore, the variance components assumed the sample represent the true population and the different sample might lead to different result. Moreover, previous studies absence the interaction or covariance effect between corporation and years or industry.

Based on the explanation above, Bowman (2011) affirmed that corporate has impact to performance. As shown in table 1, despite their issues, most of study confirmed that the impact of corporate is non-negligible and sometime has substantial effect. In addition, the leadership studies such as done by Lisberson and O'connor (1972) imply that corporate strategy and corporate management have impact to corporate performance.

The Corporate Performance

As shown in Bowman (2011) there are different definition of performance, some studies define performance as profit, accounting measurement (ROA, ROI, Q-ratio) or market share. Other clasical view defines performance as the size or the growth. In this section, the authors will elaborate more on the size and the growth including their causes and limitation based on study done Penrose (1955).

There are external and internal factors that contribute or limit the growth. External factors such as economic condition or access to financial resources. On the other hand, there are several internal *factors that encourage and limit the growth. The problem of planning. Firm needs managerial and entrepreneurial service to plan and expand. Planning is necessary before the company doing the expansion. However, the expansion will lead to other expansions as once the expansion in undertaken, company will find other opportunities. This might happen for two reasons. First, when company doing expansion, it will acquire the resources that needed during the first expansion and still not at their maximal capacity. Second, there will be resources that will not be used after the expansion done. These free resources are attracting the company to expand. The continuing availability of unused productive service. Company has their resources that not fully utilized as the cost of maximize that resources are high, thus, the company let it be unused. Company will organize the lowest-cost combination to maximize the production. Limits on the supply of Managerial Service. Experience managerial services are required for company to expand and it usually requires groups of people that capable to support company in expanding. On the other hand, the supply of experience managerial service is limited. In addition, experience managerial service provide confidence for the company to expand. Experience managerial service provides confidences to company to expand, when company use less experience service, it might lead to higher cost as the lack of knowledge to doing activities in expansion. The release and Growth of Managerial Services. During the expansion, the managerial service gains new experiences and skills and it would not be optimized used after the expansion done as the company does not know the incremental skills or experience that the managerial service has. Thus, policy to manage it is necessary so that it can be used at optimum level. The utilization of productive services and limits on demand. Company needs versatile resources especially the management that ambitious, flexible and imaginative. Sometime the problem that limit the company to grow is the lack of the entrepreneurial services, not because of external condition.*

In term of size, there some factors that limit to size of companies. As the company getting bigger, the complexity and the scope is higher. Thus, it requires huge coordination that might lead to higher cost of production. Furthermore, it might also develop decentralization. However, company may face some challenges in develop decentralization. First, the unwilling superior to distribute its power. Second, decentralization needs high quality people that able to deal with business activities including deal with unseen problem. On the other hand, there are limitation of capable service. Third, there is no evidence that decentralization will lower down the cost.

Company will have incremental growth if the company able to utilize its unused resources and provides advantages to society. However, once incremental expansion is done, the justification might fade as the company finds others opportunities and acts on it concurrently. As result, perhaps it will be more efficient if the parts of the company run independently. The next section, the author will describe how company manage its development to achieve desirable performance.

Coprporate Strategy Development

This section will elaborate the approach that corporate may take to manage its development to achieve its performance. This section mostly based on the study done by Rees and Porter (2006). The study suggests to that there two options for the company to grow, by incremental or by comprehensive approach. Both approach have their own benefit and limitation. Incremental approach is the development that build gradually whereas comprehensive approach is the development that implemented widely. (Rees & Porter, 2006)

Comprehensive strategy is needed when there is significant organization failure or extreme external changes that has happened or predicted. In addition, looking future in the narrow view will be dangerous (McLuhan, 1997) in (Rees & Porter, 2006). However, comprehensive strategy has a number of weaknesses. It is difficult to develop due to the difficulty of determining organizational capacity, the complexity of the organization's external environment and difficult to be defined by to narrow a range of people. This strategy is also not easy to implement because it does not fit with the existing structure, the new structure is forced rigidly, there are conflicts of interest, the application tends to be mechanistic, and so forth.

Rees & Porter (2006) have seen that incremental strategy has several advantages. It can strengthen existing conditions without eliminating the good practices and expertise that already apply. This strategy is also focused on making realistic changes. It is the problem-solving approach or implementation-oriented. However, there is a possibility when the incremental expansion done, the reason for expansion is disappear and become insignificant as new opportunities is come up (Penrose, 1955)

External Environment of Corporation

In this section, the author will only elaborate the two external factors that affecting the corporate strategy; macroeconomic and national economic development as describe in the next two sub section. Macroeconomics elaboration is mostly based on the study done by Oxelheim & Wihlborg (1991) and national economic development is centered from the study made by Achi, et al (1998) and focused on conglomeration in emerging market. In each seaction, each study proposed corporate strategy that might useful to cope with those external enviroment.

RESULT METHOD

Macroeconomic Factor of Corporation

The exchange of goods and services across national borders is increasing from time to time. Capital can also move quickly from one country to another. The movement of funds between countries will affect the movement of exchange rates, inflation, interest rates and other macroeconomic factors. These macroeconomic factors will trigger uncertainty at the corporate level. Therefore, corporations need to have a strategy to manage macroeconomic uncertainty comprehensively (Oxelheim & Wihlborg, 1991). There are various macroeconomic factors that can cause uncertainty in the company, starting from monetary, fiscal, industry and trade regulation. The relationship between these factors is shown in Figure 1. Each factor can occur simultaneously and dynamically over time. Corporations need a comprehensive view of the macroeconomic risks.

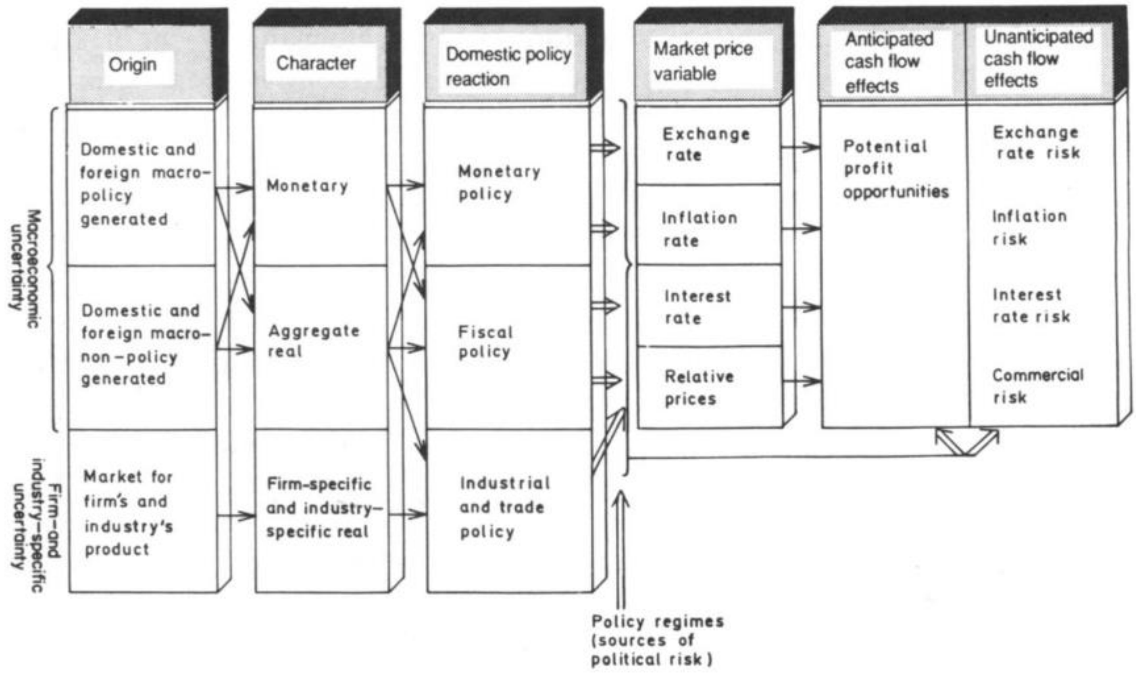

Figure 1. The relationship between macroeconomic uncertainty and the effect on corporate cash flow (Oxelheim & Wihlborg, 1991).

The corporate strategy in anticipating macroeconomic risks is closely linked to 4 factors: target variable, firm behavior to risk, time-perspective and management's view of price adjustment (Oxelheim & Wihlborg, 1991). There are many choice of target variables, such as profits, economic value, market value and cash flows. Different variables can produce different strategies. There are various types of corporate behavior against risk, such as risk neutral (unconcern about fluctuation) or risk-averse (tend to reduce the fluctuations of target variable). Another influential factor is the time perspective, such as long/short term horizon and discount rate. The last factor is management's view of price adjustment.

Oxelheim & Wihlborg (1991) determined the choice of corporate strategy based on these four factors, as shown in Figure 2. Column 1 is the company's risk-attitude and column 2 is financial market adjustment. After determining the financial cash flow strategy (column 3), we can know the good market adjustment (column 4), nominal contracted (column 5) and non-contractual flows (column 6 and column 7). At the implementation level, management must determine what strategies are feasible and the extent to which goals can be compromised with feasible strategies.

					Strategies for Operational Decisions		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Risk-attitude	Financial market adjustment	Financial cash flow strategy	Goods market adjustment	Nominally contracted flows	Non-contractual flows: Commercial	Non-contractual flows: Financial
1	Risk-neutral	IFP	Laissez faire	PPP	Laissez faire	Laissez faire	Laissez faire
2				Real exchange rate changes	Laissez faire	Int'l trade opportunities	Laissez faire
3				Relative price + real exchange rate changes	Laissez faire	Int'l and inter-sectoral trade opportunities	Laissez faire
4		Non-IFP	Expected value maxi-mization	PPP	Select highest expected value currency	Laissez faire	Select highest expected value currency
5				Real exchange rate changes		Int'l trade opportunities	
6				Relative price + real exchange rate changes		Int'l and inter-sectoral trade opportunities	
7	Risk-averse	IFP	Variance mini-mization	PPP	Minimize inflation risk	Laissez faire	Minimize inflation and interest rate risk
8				Real exchange rate changes	Minimize variance for *all* cash flows	Int'l trade opportunities	See column (5)
9				Relative price + real exchange rate changes	Minimize variance for *all* cash flow	Int' l and inter-sectoral trade opportunities	See column (5)
10		Non-IFP	Expected value/ variance trade off	PPP	Trade off expected value/inflation risk	Laissez faire	Trade off expected value/ inflation and interest rate risk
11				Real exchange rate changes	Trade off int'l trade and financial opportunities/ variance of total cash flows		
12				Relative price + real exchange rate changes	Trade off int'l, intersectoral and financial opportunities/ variance of total cash flows		

Figure 2. Choice of corporate strategy for macroeconomic risk (Oxelheim & Wihlborg, 1991).

The analysis developed by Oxelheim & Wihlborg (1991) is highly simplified. They are just discussing by using the real cash flows approach. In reality corporations can use different target variables such as profits, economic value and market value. Hedging strategies that can be done by corporations also vary greatly. Research conducted by Oxelheim & Wihlborg (1991) has been more than 25 years old. Currently there has been a growing number of contemporary approaches. The risk management study is growing rapidly in recent years, especially after the global economic crisis of 2008. The banking sector has developed new risk mitigation methods, as set out in Basel III (BIS, 2010) and Basel IV. There are many new approaches to the study of *macroeconomic risks, such as multi-market simulation, stress-tests, extreme value statistics, and so on.*

National Economic Development

National economic development will impact on how corporation build its strategy. For instance, in advance economies countries there is little intervention from the government. On the contrary, in emerging market government plays important roles to support the business. In this section the author will focus on the conglomeration in emerging market including its strategy to grow as the external condition might change.

Conglomerates or business groups with many diversified subsidiaries are growing rapidly in the emerging markets. Achi, et. Al (1998) tried to examine why conglomerates can grow rapidly in developing countries. This study covers the context underlying the development of conglomerates, the institutional framework, the strategies needed to anticipate institutional change and recommendations for shareholders.

Economic institutions in developing countries are not well established yet. But on the other hand, the government is required to carry out ambitious development goals. The government then provides special opportunities to some local companies to encourage economic activities. They have privileged access to capital and information. These privileged enable them to have the capability to influence power and access to resources (Achi, et al., 1998). The unique position also provides opportunities for them to be able to attract the most capable foreign partners.

The business structure developed from such privileges is not sustainable. Conglomerates had serious problems facing the series of economic crises that occurred in the decade 90s. There has been demand from the public and from the international community to encourage political reform and economic deregulation. This condition has forced the conglomerates to change their corporate strategy. In order to survive in the new environment, Achi, et. Al (1998) propose to use 3 strategies: (1) focus on domestic portfolio, (2) focus on portfolio that has potential to regional or international market, and (3) build portfolio in lesser-developed economies. In this paper the authors try to test these 3 strategies, by comparing the strategies performed by the 10 richest conglomerates in Indonesia.

Table 2. The strategies undertaken by the 10 richest conglomerates in Indonesia, data from www.biografiku.com

No	Conglomerate	Focus on domestic portfolio?	Focus on portfolio that has potential to regional/international market?	Build portfolio in lesser-developed economies?
1	Djarum	Yes	No	No
2	Sinar Mas	Yes	No	No
3	Gudang Garam	Yes	No	No
4	Indofood	Yes	Yes	Yes
5	Indorama	Yes	Yes	Yes
6	Kalbe	Yes	No	No
7	Trans	Yes	No	No

No	Conglomerate	Focus on domestic portfolio?	Focus on portfolio that has potential to regional/international market?	Build portfolio in lesser-developed economies?
8	Mayapada	Yes	No	No
9	Lippo	Yes	Yes	Yes
10	Mayora	Yes	No	No

Table 2 has shown that the majority of successful conglomerates in Indonesia do not conduct significant business expansion into international markets or regional markets or lesser-developed markets. This fact raises skepticism over the second strategy (focus on portfolio that has potential to regional or international market) and third strategy (build portfolio in lesser-developed economies) from Achi, et. Al (1998). The authors hypothesize that this fact occurs due to market size factors. Conglomerates in countries with very large market sizes such as China, India and Indonesia, do not have to expand overseas, because there is enough space for business development in the domestic market.

CONCLUSSION AND RECOMMENDATION

Bowman (2011) has argued that the impact of corporate to performance is non-neglectable and he has shown to readers that there are issues in previous that limit the effect of corporate level. However, we can not define the cost and benefit of corporate into performance. Perhaps there is an impact from corporate, but it goes with higher cost. Thus, it will not longer beneficial for the businesses.

To achieve its performance whether in growth, size or accounting measurement company needs resources specifically experienced management service. Certainly, it in line with the cost and the benefit. Company may take incremental strategy or comprehensive strategy to develop and its approach has its own advantages and disadvantages, company should look at their external and internal condition to chose one of approach.

Macroeconomic variables such as interest, exchange rate and tax affecting the strategy of the corporation even though the corporation solely play in domestic market as the borders between nation are thinner. Oxelheim & Wihlborg, (1991) suggest some strategy that firm may take to cope with macroecomic uncertainty as shown in figure 1. National economic condition also affecting how coorporation doing business. Achi et al 1(998) proposed some strategies for conglomeration in emerging market in order to keep grow. However, after doing test on those strategy on conglomeration in Indonesia as shown in table 2. It raises skepticism over the second strategy (focus on portfolio that has potential to regional or international market) and third strategy (build portfolio in lesser-developed economies). The authors hypothesize that this fact occurs due to market size factors.

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