THE MARKET OF COMPANIES STRATEGIC

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Abstrak: Research has shown that companies successfully pursuing either a cost leadership or a differentiation strategy are better able to gain competitive advantages over other companies and accordingly achieve superior performance. Thus, if actually do realize superior performance based on their strategic orientation, capital markets should recognize this and place a positive value on such strategy-focused companies. The aim of this paper is to empirically investigate how capital markets perceive and reward the strategies pursued by companies. Methodology this paper uses Tobin's Q as a measure of market perception. By regressing Tobin's Q against relevant control variables and proxies for differentiation and cost leadership strategies, the paper evaluates the relationship between market perception and company strategy. Furthermore, the paper also conducts abnormal returns analyses (both portfolio and regression analysis) to determine whether the market accurately prices the different strategies, given the complexity in both the nature and the implementation of such strategies. Findings - The analysis shows that markets place a positive value on companies. Successfully pursuing either a cost leadership or a differentiation strategy; moreover markets place a higher value on companies pursuing a differentiation strategy compared to a cost leadership strategy. The abnormal returns analyses show that the market is not able to fully price the superior performance generated by pursuing differentiation strategy resulting in abnormal returns from portfolios formed based on higher levels of differentiation. Research limitations/implications - By providing detailed information to the market about the strategies they follow, companies will enable markets to value their strategies accurately, thus reducing their cost of capital. Fundamental investors looking to earn abnormal returns can use company strategy in their portfolio selection. A variety of characteristics are conceived to influence a company's strategic positioning and market perception of such characteristics. This evaluation is limited to a macro level assessment of the implications of the overall strategy pursued by a company. Future research, in the form of detailed field studies, could be directed at evaluating the market perceptions and other implications of multi-dimensional, lower level, operational strategies on a company-by-company basis. Originality/value - To the best of the authors' knowledge, this is the first paper to show how financial markets value company strategy. The paper also provides evidence to the complexity of a differentiation strategy, and how such complexity can lead to market mis-pricing.

Key words: Market, Companies, and Strategic

INTRODUCTION

Research of the generic strategies, differentiation or cost leadership, enables a company to achieve better performance (Porter, 1985); Hambrick, 1983; Miller and Friesen, 1986, found the lack of strategic focus to be a major reason for the downfall of several Japanese companies. Allen (2007) also Japanese Companies such as Honda, Sony, and Nintendo "rise to global dominance by their well-developed and defined corporate strategies". He goes on to document how other Japanese companies (e.g. Mitsubishi) are using a commitment to Porter's generic strategies as a mechanism for corporate renewal. However, to sustain such superior performance into the future, companies should build effective barriers to prevent imitation of best practices that enable such superior performance. Porter (1996, 2001) argues that cost leadership strategy is easily replicable since best practices that enhance cost efficiency can spread rapidly with modern technological innovations. Conversely, a differentiation strategy is harder to imitate since it is built on products or services that are perceived to be different from the competitors; hence leading to more sustainable performance. To the extent that the superior performance through strategic positioning of Companies could be sustained into the future, contemporaneous measures such as earnings or ROA do not capture this persistence. Even so, the stock markets should theoretically recognize and reward the profitability implications of the superior performance resulting from the strategy pursued by companies.

However, as noted by Narver and Slater (2000) prior literature on this subject has focused mainly on the contemporaneous effects of strategy

on performance. In this article, we examine the market perception of different strategies pursued by companies, and to the best of our knowledge, is the first article to do so. We use empirical data for a large sample of publicly traded companies to investigate how capital markets perceive and reward strategies pursued by companies. We evaluate the market perception using both Tobin's Q and the abnormal returns from companies pursing the strategies. In addition, we also investigate the differential impact of different types of strategy (i.e. diversification and cost leadership) on the market value of companies. We use the operationalization (empirical construction) of strategy measures as defined by Balsam ,(2011), who use publicly available accounting information to capture the empirically realized level of either differentiation or cost leadership strategy achieved by a company.

Using these measures, we find that the capital markets reward companies pursuing either of these strategies; however it values companies pursuing differentiation higher than the cost leadership strategy. This reflects the longer term sustainability of the differentiation strategy over the cost leadership strategy. We also show that an investment strategy of buying high differentiation companies generate greater abnormal returns compared to a similar strategy of buying high cost leadership companies. Thus, we highlight that markets systematically underprice the differentiation strategy.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

A company needs to possess competitive advantages over its competitors in order to outperform them. Porter (1980) presents a framework describing two strategies that a company can use to achieve competitive advantage; cost leadership and differentiation. He also discusses the structure, processes and the practices that are likely to be identifiable with companies that have a specific strategic orientation. Based on Porter's framework, a company that chooses and pursues a strategy based on either differentiation or cost leadership will be in a position to effectively deal with the competitive forces that determine success within an industry. Porter's framework has become very popular in practice and academia for evaluating both macro and micro issues relating to strategic orientation in an economy Dess and Davis, 1984; Porter, 2001; Miller and Dess, 1993; Allen, 2007.

Companies adopting a cost leadership strategy aim to increase market share based on creating a low-cost position relative to their peers. Cost leadership may be achieved through large volume manufacturing utilizing economies of scale, process improvements, cost minimization, total quality management, just-in-time manufacturing, benchmarking, overhead control, etc. Conversely, a differentiation strategy may be achieved by investing in developing products or services that offer exceptional characteristics that the customers desire, enabling the company to command premium prices.

Research findings from a number of empirical studies have also found support for the linkage between generic strategies and organizational performance, thus validating the claim that adopting the generic strategies result in superior performance. While testing Porter's taxonomy Hambrick (1983) and Dess and Davis (1984) find existence of these strategies among high performing companies. In a study of the characteristics of strategies among successful companies in a mature industrial-products industry, Hambrick (1983) found that asset configuration and utilization were important factors in the profitability of companies and that the characteristics of strategies of various successful companies were similar to Porter's generic strategy framework. Dess and Davis (1984), in a field study, comprising responses from executives and panel experts from the academic community, examined Porter's generic strategies as a determinant of organizational performance and found their results to conform to the premise that adopting generic strategies leads to higher performance. In the same vein, White (1986), in an empirical study of 69 business units from 12 different multi-business companies, showed the linkage between the generic business strategies and business unit performance. Similarly, other empirical studies namely Miller and Friesen (1986), Robinson and Pearce (1988) and Tripathy (2006) have found support for Porter's theory. Thus, prior literature shows that companies following either of these strategies, differentiation and cost leadership, are able to achieve superior contemporaneous performance. Moreover, a company that moves further along in achieving cost leadership or differentiation is able to achieve better performance compared to companies stuck at the lower ends of either of the strategies.

In an efficient market, company value is the present value of expected future net cash flows, discounted at the appropriate risk-adjusted rate of return. Various financial models translate expected future net cash flows in terms of expected future earnings where the expectation is based on a company's current earnings Kothari, 2001. If earnings are more persistent and current earnings

are sustained into the future, then a higher weight is placed on current earnings in valuing a company. We expect a company that advances further along either the differentiation or cost leadership dimensions to produce better performance. Moreover, research shows that capital markets are capable of valuing intangibles such as R&D and advertising expenses Chauvin and Hirschey, 1993; Asthana and Zhang, 2006, IT expenses Aboody and Lev, 1998, and even the regulatory environment Henderson and Hughes, 2010. Therefore, we expect capital markets to be cognizant of the value implications of company strategy and we posit that companies which are successful in pursuing either the cost leadership or the differentiation strategy will enjoy higher capital market valuations. Formally stated:

H1. Capital markets will place a positive value on both the differentiation and the cost leadership strategy.

The sources of achieving a cost leadership strategy (i.e. operational efficiency) can be copied D'Aveni, 1994 or made ineffective due to advent of newer and better sources of efficiency Hamel, 2000. Therefore, such strategies will only confer transitory competitive advantage, and persistent profitability over the long-term is not achievable Eisenhardt and Brown, 1998; Eisenhardt and Martin, 2000. The rapid diffusion of best practices allows competitors to quickly imitate superior management techniques and practices. A cost leadership strategy which is primarily built on generic solutions related to operational efficiency is more susceptible to imitation by competitors and peers resulting in comparative cost advantages that will dissipate over time. Achieving cost leadership is not likely to yield an inimitable source of competitive advantage, especially if the means of achieving it process and operational efficiency is developed by suppliers and sold on the open market Barney, 2002. Being first with a new process only provides a company with a temporary cost advantage because imitation is inevitable Murray, 1988. Another source of cost efficiency is capitalizing on learning or experience effects and some companies may be able to create a durable advantage by following such a strategy. However, if an industry is not characterized by a sufficiently steep learning curve, such a strategy would collapse since it would not lead to any significant cost advantages that can be sustained Murray, 1988.

On the other hand, differentiation, which is achieved through unique products or services that consumers place a premium value on, permits more sustainable advantages to accrue to the company since such attributes cannot be easily imitated by competitors Grant, 1991. A differentiation strategy typically involves company-specific and product-specific innovations and tailored marketing campaigns that are not possible to replicate speedily. While competitors will respond to pricing moves almost immediately, responses to innovation through R&D will take a much longer period. The longer it takes for a competitor to respond to a particular comparative advantage, the greater the opportunity for a company to capitalize on the sustained advantages and to create new ones. Furthermore, differentiating oneself from the competition by concentrating on making reliable and high quality products will have a significant impact on sales. Porter ;1985 posits that this is especially true in more mature industries or in industries in which there is a high cost of poor performance.

To enable long-term superior performance a company has to maintain its unique position vis-à-vis its competitors. Most currently unique advantages of a company can and will be copied and even improved upon by competitors over time. However, certain barriers will be higher than others and hence more difficult for rivals to overcome. Competitor and competitive information is generally available to all companies and new techniques diffuse rapidly Barney, 1986. Therefore, a competitive advantage can be sustained only if it can survive attempts to replicate it by competitors Ghemawat, 1995. Given the discussed ease with which sources of competitive advantage may be imitated, some companies have still been able to generate superior performance over sustained periods of time Wiggins and Ruefli, 2002.

Based on the above discussion we expect that the performance of companies pursuing differentiation will be more sustainable into the future. As a result, capital markets will place a higher value on companies pursuing a differentiation strategy compared to companies pursuing a cost leadership strategy. Formally stated:

H2. Capital markets will place a higher value on companies pursuing a differentiation strategy than on companies pursuing a cost leadership strategy.

DATA, STRATEGY MEASURES AND RESEARCH METHODOLOGY

a. Data

We obtain data for the strategy and performance variables used in our study from the computer data files and stock market returns from CRSP for the period 1989-2009.

b.   Strategy measures

Prior studies have attempted to capture the strategic positioning of companies either through surveys Dess and Davis, 1984; Miller, 1987 or through limited proprietary data Kotha and Nair, 1995; Berman , 1999; Nair and Filer, 2003). We capture the strategic positioning of the companies using realized indicators obtained through companies' financial statements. Following Balsam ,2011, we use three variables (SG&A/SALES, R&D/SALES and SALES/COGS) to measure strategic positioning based on the differentiation dimension and three other variables (SALES/CAPEX, SALES/P&E and EMPL/ASSETS) to measure strategic positioning based on cost leadership. These measures capture the Companies' long-term strategic orientation on the dimensions of differentiation and cost leadership.

Balsam, 2011 review the extant literature in detail and discuss the use of the six variables to construct the strategy of the companies. Based on Balsam, we compute *SG&A/SALES* as the selling, general and administrative expenses scaled by net sales. This variable captures a company's investment in marketing activities to differentiate itself from competitors Berman, 1999; David , 2002; Miller and Dess, 1993; Thomas, 1991. We also compute *R&D/SALES* as research and development expenses scaled by net sales. R&D expenses indicate the ability of companies to offer high quality and innovative products and services which are critical to the success of differentiators Hambrick, 1983; David , 2002; Thomas , 1991. *SALES/COGS* is net sales scaled by cost of goods sold. A higher ratio captures a greater ability to command premium prices, typically linked with differentiators Berman, 1999; Kotha and Nair, 1995; Nair and Filer, 2003.

SALES/CAPEX is net sales scaled by capital expenditures on property, plant and equipment. *SALES/P&E* is net sales scaled by net book value of plant and equipment. A higher value for these variables indicates a more efficient use of the company's assets Berman, 1999; Hambrick, 1983; Kotha and Nair, 1995; Miller and Dess, 1993. Similarly, *EMPL/ASSETS* is the number of employees scaled by total assets (Hambrick, 1983; Kotha and Nair, 1995; Nair and Filer, 2003) where number of employees is used in the numerator as an alternative proxy for size (output) instead of net sales. All three measures capture a company's efficiency in utilizing its capital investments David 2002.

Similar to Balsam *et al.* 2011, we compute the mean of the previous five years of data for each of the above six variables to capture the long term

strategic orientation of companies and conduct a con-company factor analysis (CFA) to construct the two strategy variables, cost leadership and differentiation. The results of our CFA and indicate reasonable levels of reliability and validity for the two strategy variables. The factor loadings, which range from 0.52 to 0.98, and the *t* -statistics for the two factors suggest that the indicator measures satisfy the convergent validity thresholds suggested in prior literature Bagozzi, 1991; Phillips, 1981. The average variance extracted (AVE), establishes the discriminant validity of constructs by indicating the amount of variance that is captured by an underlying factor in relation to the amount of variance due to measurement error. AVE is well above the recommended threshold of 0.5 for all factors Fornell and Larcker, 1981. The composite reliability which measures the internal consistency of the factors also exceeds the recommended threshold of 0.7 Werts, 1974; Nunnally, 1978 for the two factors. The goodness of fit index and the adjusted goodness of fit index, which evaluate whether the measurement model provided a good fit, are also above the cut-off range of 0.90 and 0.80, respectively, Joreskog and Sorbom, 1989. Additional fit measures such as the comparative fit index Bentler, 1989 and the non-normed index Bentler and Bonett, 1980 are also in the acceptable range. The results of our CFA are similar in tenor to Balsam, 2011.

Thus, as measured by the factor scores in each of the strategy constructs, the two strategy constructs are continuous variables which are orthogonal to each other, forming four quadrants of companies based on their strategies. In other words, we capture both dimensions of differentiation and cost leadership for each company because, consistent with the views of Porter, 1985 and others, the two strategies are not viewed as two ends of the same continuum, but rather as two distinct platforms that can be used in isolation or in combination with each other (which is captured by having two strategy constructs, one for differentiation and one for cost leadership, which are continuous variables).

c.   Research methodology

We measure the market perception in two ways: Tobin's Q and abnormal market returns. We use Tobin's Q Tobin, 1969 to capture the market perception of the companies. Tobin's Q, a measure of a company's market performance, is the ratio of the market value of a company's assets (as measured by the market value of its outstanding equity and debt) to the book value of the company's assets. If a company has value in excess

of what it would cost to rebuild it, then that extra value is due to a premium placed on the company by stock markets. Hermalin and Weisbach (1998) argue that Tobin's Q is an equity-based measure of company performance which incorporates not just the results from contemporaneous actions of management, but also the market's expectations of future performance. Tobin's Q may also be used as a measure of a company's market (or stock price based) performance Yermack, 1996; Coles *et al.* , 2008) and future growth opportunities. [34] Lang and Litzenberger (1989) justify the utilization of Tobin's Q as a measure of growth opportunities. They show that a Tobin's Q above 1 is a necessary condition for a company to be at a level of investment that maximizes its value and that a Tobin's Q below 1 characterizes a company with limited future opportunities. We use the equation below to test the extent to which market premium on the level of cost leadership or differentiation is reflected in Tobin's Q: Equation 1 TQ_t is Tobin's Q for company j in year t, computed according to Brown and Caylor (2006) as (total assets+market value of equity-total common equity-deferred taxes)/total assets. $Differentiation_t$ and Cost $Leadership_t$ refer to the strategies pursued by a company as determined by individual factor scores described in the earlier section. Control variables used are $Size_t$, Age_t Brown and Caylor, 2006) and $Dividend_t$ Servaes, 1996. $Size_t$ is the natural logarithm of total assets which controls for company size. This is to account for the well documented size discount whereby large companies have a relatively lower Tobin's Q compared to their smaller counterparts McConnell and Servaes, 1990; Lang and Stulz, 1994). In accordance with these studies, we expect a negative relationship between Tobin's Q and company size. Younger companies are generally faster-growing, and more intangible asset-intensive, hence we expect a negative relationship between Tobin's Q and age. Age_t is the natural logarithm of company age in years to control for the company's age. $Dividend_t$ is natural logarithm of cash dividends and as in Servaes (1996) we use $Dividend_t$ as a proxy to capture the individual company's access to capital markets. We expect a positive relationship between Tobin's Q and $Dividend_t$ since better access to capital would result in greater company value. We expect b_1 and b_2 to be positive and significant in accordance with our *H1* and we expect b_1 to be greater than b_2 in accordance with our *H2* . Our analyses in regression models (1) and (2) (below) are not based on separate samples for cost leadership companies and differentiation companies. Instead, we employ a single data sample from companies

and using commonly available accounting data items from that dataset, compute proxies that measure the degree to which each company displays either cost leadership properties or differentiation properties. Hence a typical company will have both a score for the cost leadership proxy and the differentiation proxy.

d.   Portfolio returns

The Tobin's Q analysis explained above evaluates the *ex ante* market perception of companies' strategy. A different way of analyzing the market's perception of companies' strategic orientation is to examine long term realized returns which highlight the ex-post perceptions. Therefore, we evaluate whether the realized returns of companies depend on the extent to which companies pursue their strategic orientations. We calculate the future abnormal return for a company as the difference between the year k (k=t+1, t+2, t+3) return of the company, measured over a year from July of year k to June of year k+1, and the median return of its control portfolio over the same time period. We adopt the methodology developed by Lyon, 1999 and used in Henderson, 2010 as a "three-step approach" to construct control portfolios. According to this approach, control portfolios are formed at the end of June of each year t+1, based on book to market ratio, market value of equity, and 12-month buy-and-hold returns. First, we rank all NYSE/AMEX/Nasdaq stocks by their book to market ratio (book value of equity divided by market value of equity), and assign each stock to one of five equally sized portfolios. Then within each book to market portfolio, we assign stocks to one of the six portfolios based on market value. Lastly, within each 30 book to market and market value of equity portfolio, we allocate stocks to one of the three 12-month buy-and-hold portfolios based on prior-year returns.

For each of the 90 control portfolios thus formed, we measure median return over a period of one year from July of year k to June of year k+1. Then, we assign each of our observations to one of these 90 portfolios based on book to market, size and returns of the observation. We compute the abnormal returns for an observation as the raw returns over the year from July of year k to June of year k+1 less the median portfolio returns.
Once abnormal returns are computed for each company, we compute a different set of portfolios based on the company's level of cost leadership or differentiation. The entire sample is divided into quintiles based on the degree of Differentiation (cost leadership). Each quintile is a portfolio and we compute the mean abnormal returns for each

such portfolio. The final computation creates hedge portfolios by going long on the portfolio consisting of the highest quintile of Differentiation (cost leadership) companies, and going short on the lowest quintile of Differentiation (cost leadership) companies. If the market fails to incorporate the superior performance of either strategy completely into contemporaneous stock price, we would expect high differentiation (cost leadership) portfolios to yield higher abnormal returns over a long term compared to low differentiation (cost leadership) companies. Furthermore, and in accordance with our *H2* , we expect high differentiation portfolios to yield greater returns compared to high cost leadership portfolios.

The methodology used to compute abnormal returns, by construction, controls for size and risk. However, there are other variables that may impact abnormal returns such as the level of R&D spending and capital expenditure. Therefore, we conduct a multivariate analysis to evaluate the abnormal returns generated by the market for companies pursuing differentiation or cost leadership. We use the following empirical model based on Henderson *et al.* (2010) for our analysis: Abnormal Ret $_{t+1,t+3}$ is abnormal returns computed as described above over a three year period. Differentiation D_t (Cost Leadership D_t) is a dummy variable equal to one if the company is in the topmost quintile according to the degree of differentiation (cost leadership). $R\&D_t$ is research and development expense scaled by sales revenue, Adv_t is advertising expense scaled by sales revenue, $CapEx_t$ is capital expenditures divided by sales revenue, $LogSales_t$ is natural logarithm of sales revenue and $SD(EarnQ)_t$ is standard deviation of quarterly earnings before extraordinary items scaled by quarterly sales for prior three years. We include $SD(EarnQ)_t$ as a measure of total risk to control for any risk factors which we might not have controlled for in constructing abnormal returns. Further we include $R\&D_t$, Adv_t , $CapEx_t$ and $LogSales_t$ as additional control variables following Henderson, 2010.

EMPIRICAL RESULTS

a. Descriptive statistics and correlations

The first two variables are the strategy measures, Differentiation$_t$ and Cost Leadership$_t$. By construction, these measures have a mean of 0 and a standard deviation of 1. The two dependent variables are TQ$_t$ and AbnormalRet$_{t+1,t+3}$ (abnormal returns). They have means (median) of 1.77 (1.43) and 0.12 (-0.01), respectively. Total assets and total sales have means (medians) of $2,329 million

($474 million) and $2,422 million ($554 million), respectively. The average Company spends 3 percent of its sales on R&D expenses, 1 percent of its sales on advertising and 6 percent on capital expenses.

In general, the correlations in panel A are not too high with the largest correlation being 0.6963 between Log (Assets)$_t$ and Log (Dividends)$_t$ (both of which are control variables). Differentiation$_t$ shows positive and significant correlations with the dependent variable, TQ$_t$. The results are consistent for both Spearman and Pearson statistics. Panel B again show consistent and expected results for Differentiation$_t$ with the dependent variable AbnormalRet$_{t+1,t+3}$. The results are positive and significant for both Spearman and Pearson statistics. However, Cost Leadership$_t$ is negative and insignificant for both Spearman and Pearson statistics.

b. Market of Company strategy

To test our hypotheses relating to the market valuation of the company strategies, we estimate model (1) on our data sample by regressing TQ$_t$ on the independent variables, Differentiation$_t$ and Cost Leadership$_t$.

Column 1 tabulates the results of TQ$_t$ regressed against control variables and Differentiation$_t$. The results show that in accordance with *H1* , Differentiation$_t$ is positive and significant (estimated coefficient=0.26; *t* -stat.=22.7) with a very high *t* -statistic. This indicates that TQ$_t$ increases with higher levels of differentiation. A higher TQ$_t$ means that the market imputes a greater differential to the company's book value and market value, implying expectations of superior performance in the future. These results indicate that the market places higher value on companies with higher levels of differentiation. Column 2 tabulates the results of TQ $_t$ regressed against Cost Leadership$_t$. The coefficient on Cost Leadership$_t$ (estimated coefficient=0.03; *t* -stat.=7.11) is positive and significant. These results further support *H1* and show that the market places a positive value on companies pursuing a cost leadership strategy. Together, the results of columns 1 and 2 show that as per *H1* , the market placed a positive value on companies pursing either a differentiation or a cost leadership strategy. In column 3, we regress TQ$_t$ against both strategy proxies simultaneously. Both Differentiation$_t$ (estimated coefficient=0.26; *t* -stat.=23.29) and Cost Leadership$_t$ (estimated coefficient=0.04; *t* -stat.=8.53) retain their signs and statistical significance. Moreover, the magnitudes of the coefficients in column 3 do not change substantially from columns 1 and 2.

Regressing both coefficients together enables us to compare the differential impact of the two strategies on TQ $_t$. A formal comparison of the two coefficients using Wald's F-test enables us to reject the null hypothesis of equality at a probability of less than 1 percent. The results show that in accordance with $H2$, the market places greater emphasis on companies pursuing a differentiation strategy compared to companies pursuing a cost leadership strategy. As discussed earlier, this may be due to the potential ease with which a cost leadership strategy could be replicated compared to a differentiation strategy.

The control variables show a negative relationship between Tobin's Q and company size and also Tobin's Q and company age. This potentially indicates the market's perception of lack of future growth opportunities for large older companies compared to their more dynamic younger and smaller counterpartsEvans, 1987. The results also show a positive relationship between Tobin's Q and dividends, indicating that markets prefer high dividend payouts. The variance inflation factors (VIF) indicate that multi-collinearity is not a problem in any of the regressions. Panel B tabulates the results of our analysis when we include industry adjusted scores of the strategy measures. These results are very similar to our main results company the robustness of our results.

c. Abnormal returns and Company strategy

The results indicate that the market places a premium on both the differentiation and the cost leadership strategies; however the premium placed on companies pursuing differentiation strategy is higher than on companies pursuing a cost leadership strategy. We conduct additional analysis on this by forming portfolios based on the extent to which companies pursue these strategies. First, we compute abnormal returns for each company by taking the difference between the 12-month returns of individual companies and the median returns of its control portfolio (based on size, book to market ratio and returns momentum. Next, we form five portfolios based on the extent of differentiation of the company and compute the difference between the mean returns of the portfolio with the highest Differentiation and the portfolio with the lowest Differentiation. The portfolio return differences are computed for t+1, t+2 and t+3 years, respectively, with t being the current year. The same process is repeated with portfolios based on the extent of cost leadership as well.

The difference between the highest differentiation and the lowest differentiation portfolios yields an abnormal return of 5.76 percent in the first year after portfolio formation, 5.41 percent in the second year after portfolio formation and 4.47 percent in the third year after portfolio formation. All of the returns are statistically significant, implying that high differentiation companies earn statistically significant abnormal returns compared to low differentiation companies, whereas such a relationship does not exist for high/low cost leadership companies. The difference in the returns for the high/low cost leadership portfolios are statistically insignificant in all the three years; moreover the magnitudes are less than or equal to half a percentage. The results indicate that high differentiation companies generate significant abnormal returns over a three year window compared to low differentiation companies, whereas such is not the case for high/low cost leadership companies. We conducted similar analysis using industry adjusted scores of the strategy measures. The market is still not fully pricing the superior future performance of high differentiation companies as evidenced by the ability of high differentiation companies to earn abnormal returns over the next three years high market premium due to difficulty in replicating by competitors; and underpricing by the market.

We also perform multivariate analysis of three-year abnormal future stock returns to company that the results we observed robust to other variables that may not have been adequately controlled for by the procedure employed Lyon, 1999; Henderson *et al.*, 2010 to compute abnormal returns. The results of the model (2) the standard errors have been corrected for heteroskedasticity, serial- and cross-sectional correlation using a two-way cluster at the Company and year level Petersen, 2009.

Column 1 of Panel A tabulates the results of AbnormalRet$_t$ (abnormal returns) regressed against DifferentiationD$_t$ (a dummy variable defined as equal to 1 if the Company is in the top quintile of the differentiation variable, 0 otherwise) and Cost LeadershipD$_t$ (a dummy variable defined as equal to 1 if the company is in the top quintile of the cost leadership variable, 0 otherwise) and other control variables that may potentially impact long term returns. The control variables are R&D expenses, advertising expenses, capital expenditure and sales. The results in column 1 company show that even after controlling for variables that may potentially impact abnormal returns, the Differentiation D $_t$ variable is positive and significant (estimated coefficient=0.083; t-stat.=7.29) indicating that the high differentiation portfolio continues to earn statistically significant returns, due to mispricing of the differentiation strategy. Cost Leadership D $_t$

is insignificant (albeit positive), indicating that there is no mispricing of the cost leadership strategy. Column 2 shows results of Abnormal Ret regressed against the strategy variables, control variables discussed in Column 1 and in addition, earnings volatility SD(EarnQ) $_t$ which is calculated as the standard deviation of quarterly earnings before extraordinary items scaled by quarterly sales for prior three years, and proxies for earnings risk. To company that our results are not driven by omitted risk factors, we estimate the model with and without the total risk measure, SD(EarnQ) $_t$. Our results remain qualitatively similar to column 1 with the alternative specifications. VIF show that multi-collinearity is not a problem. Again, the results using industry-adjusted strategy factor scores tabulated in Panel B company those discussed in Panel A validating the robustness of the results.

Taken together, the results company two hypotheses. The results show that the market places a premium on companies that pursue either of the strategies; however the results also indicate that the premium is greater for companies pursuing a differentiation strategy compared to companies pursuing cost leadership strategy. Furthermore, the results of our analysis show that the market initially fails to fully price a differentiation strategy, leading to abnormal returns for companies that pursue a higher level of differentiation.

d. Analysis

As a sensitivity analysis, we first compute dummy variables based on our strategy measures, so that a company could be classified as following one or the other of the strategies. Hence for each company, we create dummy variables Differentiation$_t$ _D and Cost Leadership$_t$ _D, based on whether its differentiation (cost leadership) score is above or below the 50th percentile. Next, we re-estimate model (1) by replacing the continuous independent variables with the dummy variables Differentiation$_t$ _D and Cost Leadership$_t$ _D. Untabulated results of the analysis are qualitatively similar to the providing credence that our findings are robust to alternative specification of the strategy variable.

As an additional refinement of the above analysis, we compute four additional, more refined dummy variables, HighDfHighC$_t$, HighDfLowC$_t$, LowDfHighC$_t$, and LowDfLowC$_t$. HighDfHighC$_t$ is a dummy variable equal to 1 if the Company is above the 50th percentile for both differentiation and cost leadership scores and 0 otherwise. HighDfLowC$_t$ is a dummy variable equal to 1 if the company is above the 50th percentile for

differentiation and below the 50th percentile for cost leadership scores and 0 otherwise. LowDfHighC$_t$ is a dummy variable equal to 1 if the company is below the 50th percentile for differentiation and above the 50th percentile for cost leadership scores and 0 otherwise, and finally LowDfLowC$_t$, is a dummy variable equal to 1 if the company is below the 50th percentile for both differentiation and cost leadership scores and 0 otherwise. We re-estimated model (1) by replacing the two continuous independent variables with the first three dummy variables described above. Untabulated results show that all three independent variables are positive and significant. However, HighDfLowC $_t$ shows the largest magnitude, implying that performance is highest for companies that concentrate on a differentiation strategy. Overall, the sensitivity analyses company the robustness of our results to alternative model specifications.

e. Control for Company-specific effects

Our main research hypothesis is to examine the strategy-market performance linkage as a cross-sectional phenomenon. While there are substantial differences in strategy across companies, strategy is a long-term phenomenon and companies are not likely to change their orientation on a year-to-year basis; accordingly strategy does not vary much over time within the same company. In this regard we note that the average correlation with lagged strategy measures is 0.99 for both differentiation and cost leadership. Similar to the context of managerial ownership in finance, most of the variation in our study also occurs in the cross-section rather in the time-series. Hence, using company fixed effects will not be appropriate in our context and, if used, can lead to erroneous conclusions Beck, 2001; Baltagi, 2001; Wooldridge, 2002; Hsiao, 2003. Accordingly we do a sensitivity analysis including prior performance as an independent variable in our main empirical models. This helps to capture company-specific effects that do not change over time.

f. Impact of diversification

Our companies being large for the most part, operate in more than one line of business. Consequently, it is possible that subsidiaries follow differing strategies across the cost leadership/differentiation continuum. However, since we are looking at the market perception of the strategy pursued by companies, capital markets will typically react to the company as a whole, hence the overall or blended strategy is relevant. Tabulate the results of our analysis incorporating the effect of diversification in our estimation

model. The results indicate that the market perception of the strategy pursued by a company is not impacted by the company's degree of diversification. This result signifies that investors consider companies' overall strategy, not their strategy in individual sub-business segments. We believe that diversification strategy and the company strategies of differentation or cost leadership are independent of each other. We acknowledge that there may be interesting insights from a study that explores the three-way interactions between diversification, company strategy and performance. This however is beyond the scope of our study and could be explored in future studies.

CONCLUSIONS

Porter :1980 and Hambrick 1983 posit that companies pursuing either a cost leadership or a differentiation strategy are better able to gain competitive advantages and accordingly achieve superior performance over competitors. In this paper we evaluate how capital markets evaluate the strategic positioning of the companies. According to the efficient market hypothesis, all relevant information about a company or stock is incorporated in the stock price. Accordingly, capital markets would place a positive value on a company pursing either a differentiation or a cost leadership strategy. In this study, we investigate the market pricing of the strategic orientations of companies, and further whether there is any potential mispricing of the strategies.

We use the Balsam *et al.* 2011 methodology to develop proxy variables for the two types of strategies pursued by companies. These variables capture the strategic positioning of the companies using publicly available data. We regress these strategy variables against Tobin's Q which is a widely accepted measure of market's perception of value Morck, 1988; Yermack, 1996; Brown and Caylor, 2006. We further compare the abnormal returns based on portfolios of high differentiation (cost leadership) companies with those of low differentiation (cost leadership) companies. For our final analysis, we regress abnormal returns against the strategy variables and additional control variables. We find that Tobin's Q is positively and significantly related to both the differentiation and the cost leadership. However, the coefficient of differentiation is significantly larger than that of cost leadership. Thus, our results indicate that capital markets place a higher premium on companies pursuing both cost leadership and differentiation. However, it places a greater premium on differentiators compared to cost leaders. We also find that a portfolio made up of

high differentiators will generate positive and significant abnormal returns compared to a portfolio of low differentiators. However, we do not observe similar results for cost leaders. The difference in abnormal returns for the high and low cost leader portfolios is statistically insignificant. Similar results are observed in a multivariate analysis of abnormal returns. These results again company the premium placed on company strategy, especially differentiation. Moreover, they show that although the market places a premium on a differentiation strategy, the market still underprices differentiation, which leads to abnormal returns in the future. The higher premium initially placed on differentiators by the market shows recognition of the difficulty of copying a successful differentiation strategy. The underpricing by the market again points to the complexity of a differentiation strategy and shows that even sophisticated capital markets are unable to fully comprehend the profitability of a successful differentiation strategy.

This paper has several important contributions. First we point to the importance of successfully following a competitive strategy in order to generate shareholder returns. Second, we show that markets value both differentiation and cost leadership strategies when successfully implemented. However, the market places a greater premium on differentiators pointing to greater sustainability of a differentiation strategy. Third, we demonstrate that markets systematically underprice a differentiation strategy. Leading directly from our third contribution, our fourth contribution is to demonstrate an additional strategy to earn abnormal returns. A portfolio of either high differentiation companies or high cost leadership companies will generate abnormal returns with the former generating greater returns.

Our study has several implications for corporate managers, financial analysts and investors. Corporate managers of Companies that follow differentiation strategies should provide sufficient information to the market to enable it to form a better understanding of the future potential of the company. This will eventually reduce the cost of capital for such companies. Financial analysts too should be aware of the strategy being followed by companies since analysts are the financial intermediaries who will interpret information provided by companies. Finally, our study provides investors with another investment strategy for earning abnormal returns.

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TINJAUAN YURIDIS PERJANJIAN ASURANSI
DALAM HUKUM POSITIF INDONESIA

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Abstrak: Tujuan dari penelitian ini untuk mengetahui tinjauan yuridis perjanjian asuransi dalam hukum positif Indonesia, bentuk perlindungan hukum tertanggung dalam perjanjian asuransi, serta prosedur penyelesaian sengketa perjanjian asuransi. Adapun metode penelitian yang digunakan adalah penelitian hukum normatif (*doctrinal*), dimana pada penelitian jenis hukum ini, seringkali hukum dikonsepkan sebagai apa yang tertulis dalam peraturan perundang-undangan (*law in book*) atau hukum dikonsepkan sebagai kaidah atau norma yang merupakan patokan berprilaku bagi manusia yang dianggap pantas. Pendekatan yang digunakan pada penelitian ini adalah Pendekatan Perundang-Undangan (*Statute Approach*) dan Pendekatan Konsep (*Conceptual Approach*). Bahan hukum yang digunakan adalah bahan hukum primer, sekunder dan tersier. Sedangkan teknik pengumpulan bahan hukum dilakukan dengan studi kepustakaan, dan analisa bahan hukum dengan cara deskriptif kualitatif sedangkan cara penarikan kesimpulan dengan cara deduktif. Tinjauan yuridis perjanjian asuransi dalam hukum positif Indonesia terdiri dari beberapa prinsip yaitu kepentingan yang dapat diasuransikan, itikad baik, keseimbangan, subrogasi, sebab-akibat, dan kontribusi. Selain prinsip tersebut terdapat juga unsur-unsur dari asuransi yaitu merupakan suatu perjanjian, adanya premi, adanya kewajiban memberikan penggantian kepada tertanggung serta adanya suatu yang belum pasti terjadi. Bentuk perlindungan hukum bagi tertanggung dalam pembayaran klaim asuransi yang diberikan oleh negara yaitu melakukan upaya hukum berupa gugatan ke lembaga peradilan, karena hubungan hukum yang timbul antara penanggung dengan tertanggung adalah hubungan hukum yang berasal dari kontraktual yang merupakan domein hukum privat. Sedangkan prosedur penyelesaian sengketa antara tertanggung dengan penanggung dalam pembayaran klaim asuransi pada umumnya diselesaikan melalui lembaga arbitrase sesuai dengan klausula dalam polis, akan tetapi apabila dalam polis tersebut tidak ditentukan lembaga mana yang menyelesaikan sengketa kadangkala seringkali mengajukan upaya hukum baik di Pengadilan maupun di luar Pengadilan.

Kata Kunci: Tinjauan, Yuridis, Perjanjian, Asuransi

PENDAHULUAN

Kemajuan zaman dan perkembangan teknologi modern yang begitu serba cepat, menyebabkan tingkat risiko yang terjadi terhadap setiap aktifitas manusia juga semakin meningkat, baik yang mengancam diri atau harta benda miliknya sehingga manusia berupaya untuk mengatasinya. Salah satu cara manusia mengatasi risiko adalah melalui peralihan risiko kepada pihak lain dalam hal ini melalui lembaga asuransi.

Asuransi sebagai lembaga pengalihan dan pembagian risiko mempunyai kegunaan yang positif baik bagi masyarakat, perusahaan maupun bagi pembangunan Negara. Dimana mereka yang mengikatkan diri dalam perjanjian asuransi akan merasa tentram sebab mendapat perlindungan dari kemungkinan tertimpa suatu kerugian. Sedangkan bagi suatu perusahaan yang mengalihkan suatu risikonya melalui perjanjian asuransi akan dapat meningkatkan usahanya dan berani menggalang tujuan yang lebih besar. Demikian pula premi-premi yang terkumpulkan dari asuransi dapat diusahakan dan digunakan sebagai dana untuk pembangunan dan hasilnya akan nikmati oleh masyarakat.

Asuransi adalah salah satu bentuk manajemen atau pengendalian risiko, dengan cara mengalihkan risiko (*transfer of risk*) atau membagi risiko (*distribution of risk*) dari pihak yang memilki kemungkinan menderita karena adanya risiko kepada pihak lain. Pembagian atau pengalihan risiko tersebut tentu saja didasari oleh aturan atau prinsip-prinsip yang berlaku dalam perjanjian asuransi. Namun perlu diteliti lebih lanjut apakah aturan tersebut saling melengkapi atau bertentangan, kemudian bagaimana pengaturan perlindungan bagi nasabah serta prosedur penyelesaian masalahnya.

Adapun rumusan masalah yang diajukan dalam tulisan ini, yaitu: 1. Tinjauan yuridis perjanjian asuransi dalam hukum positif Indonesia, 2. Bentuk perlindungan hukum tertanggung dalam perjanjian asuransi, 3. Prosedur penyelesaian sengketa perjanjian asuransi.

Tujuan dari penelitian ini untuk mengetahui tinjauan yuridis perjanjian asuransi dalam hukum