BUSINESS STRATEGY: DETERMINANTS AND THEIR EFFECT ON FINANCIAL PERFORMANCE OF LIFE INSURANCE COMPANIES IN INDONESIAN

Yanes Yaneman Matulatuwa¹,², E. Susy Suhendra³, Toto Sugiharto³

¹,²,³Faculty of Economics, Gunadarma University, Indonesia

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Abstract

The purpose of this paper is to empirically explore the influence of managerial competence, market competition, corporate governance and intellectual capital on business strategies and their impact on the financial performance of life insurance companies in Indonesia. This research uses sample of 22 life insurance companies during 2013 – 2020 selected based on the purposive sampling method. Profit margin is used to identify the business strategy applied by the company. Binary logistic regression analysis and linear regression analysis were applied to test the research hypotheses. Business strategy has an effect on the company's financial performance that is represented by return on equity. Managerial competence, market competition, corporate governance and intellectual capital partially and significantly influence business strategy. Business strategy is important for life insurance companies in Indonesia to achieve the goals. The research has implications with regard to the antecedents and consequences of business strategy to gain competitive advantage and finally achieve the financial performance. This research is integrated and comprehensive, as it includes the influence of competition and three internal variables related to human resource management competence.

INTRODUCTION

The increase in gross domestic product and Indonesian population have increased the potential of the insurance market which is accompanied by an increase in the contribution of gross domestic product in the financial services and insurance sectors to gross domestic product. The improvement in the performance of the service and insurance sectors is still low, especially in conducting market development, so that this large market potential becomes a great opportunity for insurance companies to increase market share and can attract local and international investors to enter the insurance market. The performance of the life insurance industry in developing the insurance market is strongly influenced by various factors and the most important factor is the strategy adopted by the company. Insurance companies must develop the right business strategy with a level of competitive advantage and be a guide for the company in achieving the mission and goals that have been set.

Strategy is a map where people can find out their position, know several alternative roads to reach the destination city, the difficulty and ease of each alternative road and finally can determine the path to be traversed effectively and efficiently to achieve the goal. Seedee (2012) explains that business strategy has an important position for the company and is a tool to achieve organizational success (Lewis, 2008) and can determine the company's continuity (Rasheed et al. 2020), as it can create competence for the company. The chosen strategy enables the company to exploit its core competencies to best capture opportunities in the external environment. Porter and Kramer (2006) state that in today's competitive market conditions, competitive advantage is at the heart of company performance. In formulating corporate strategy, companies must take into account dynamic
environmental changes such as changes in consumer behaviour, changes in consumer income, competitor strategies and other external factors so that companies can achieve competitive advantage (Rasheed et al., 2020). Companies that successfully implement business strategies mean that all employees from lower management to top management understand well about their responsibilities and this company has succeeded in reflecting its strategy into key performance management practices (Patel and Cespedes, 2016).

Companies in formulating business strategies are influenced by the level of market competition. High market competition means that all companies in the industry are trying to increase their market share. The Indonesian insurance industry has high level of competition, because Financial Service Authority (2021) reports that the number of life insurance companies in Indonesia are 54 companies. Previous research has shown inconsistent results regarding the impact of market competition on company earnings (Marchiukaityte and Park, 2009 and Markarian and Santalo, 2014), because many companies ignore the interaction of market competition and business strategy. Wu et al. (2015) explain that increasing labour costs and competition from other Asian countries have caused most Chinese companies to change their business strategies from cost-oriented to more differentiation-oriented strategies. How business strategies change as a result of market competition is an important question that appears to be unanswered by researchers. A company that produces a new product with better technology can fail when the product is launched in the market as a result of high levels of competition and competitors are influencing customers with their chosen business strategy.

The company's business strategy is also determined by managerial competence. Managerial skills are important in formulating business strategies and implementing them. Hellriegel et al. (2008) state that managerial competence is a set of knowledge, skills, behaviours and attitudes that contribute to personal effectiveness. Martin and Staines (2008) examine the importance of managerial competence in successful small companies and the role of managers in managing their competence becomes important as Faiz (2014) says that the idea of core competence is trying to focus managers on the important things and encourage them to identify the things that matter, namely things that are not core to the company. Performance is a function of the organization’s ability to acquire and manage resources in several different ways to develop competitive advantage (Iswatia, & Anshoria, 2007). High performance reflects the effectiveness and efficiency of management in utilizing company resources and in turn contributes to the country's economy at large (Naser, and Mokhtar, 2004).

Intellectual capital is a factor that must be considered by management in formulating business strategies. Globalization and increasing competition have led to an era where knowledge along with tangible assets has been used as a factor of production and knowledge has become the building block of intellectual capital (Chaharbaghi and Cripps, 2006). Businesses that have understood the importance of learning have shifted their strategic efforts from managing financial assets – often confidential – to managing the intangible assets of intellectual capital. Intellectual capital refers to all intangible resources that determine the level of competitiveness of the company and can accelerate the development of new products, services, new processes through better innovation, and enhance and support continuous improvement of organizational performance (Schiuma and Lerro, 2008). Al Jaradat et al. (2012) state that controlling intellectual capital effectively will produce a sustainable competitive advantage compared to investments in other fields such as finance and physical resources and Phussvat et al. (2011) conclude that intellectual capital has a positive effect on financial performance in manufacturing companies in terms of profit growth, return on equity, return on assets, and employee productivity. Kamukama (2013) suggests that managers need to realize that physical resources and financial assets need to be linked to intangible resources to gain long-term viability and a competitive position that excels in the market.

The company's internal factor that must be taken into account by the company in formulating a business strategy is corporate governance. If corporate governance is not implemented properly, the company faces serious problems in the form of low resource use. Implementing and enforcing proper corporate governance practices is critical to enhancing the development of companies (as well as the economy as a whole) and their long-term prosperity (Khiari et. al., 2007). Governance failures or weaknesses can reflect the company's inability to take into account and incorporate internal and external aspects into the preparation of corporate governance (Tura, 2012). Poor corporate governance leads to waste, mismanagement and corruption. Whatever the type of company's business, good governance can realize good and sustainable business performance (Chen and Lee, 2012).

The results of this study contribute to strengthening the theory of the company business strategy, especially for insurance companies and contribute to top management in conducting internal and external environmental analysis to formulate business strategies in order to improve the company's financial performance. The results of this study can also contribute to the government in changing the behaviour of insurance business actors to create a climate of fair competition; increase the certainty of law enforcement on business competition to ensure a healthy investment climate and supervision of the implementation of a healthy partnership; and improve the quality of management services both internally and externally.

The remainder of our article is organized as follows. Section 2 discusses the literature review and hypotheses development. Section 3 describes our data, methodology and research models. Section 4 presents our empirical results and section 5 concludes the study.

Literature review and hypotheses development.
Relationship business strategy and company performance

Strategy is the creation of a unique and valuable position that involves a number of activities that are superior and different from those of competitors. Business strategy is an important factor in strengthening and improving organizational performance, because it can create a significant competitive advantage in any market, so as to realize sustainable trade development (Rasheed et al., 2020). Bhavik and Frank (2016) explain that strategy is related to making choices to create a sustainable competitive advantage in the market such as superior products and services, more value propositions offered in the market, and the company being able to create activities or processes that support the value proposition (Collis and Ruksdahl, 2008). This value proposition refers to the value the company promises to deliver. For example, Wal-Mart's strategy is to have "low prices every day" for a wide variety of products that are available and geographically convenient by making cost savings through purchasing large volumes of merchandise and through discovering the weaknesses of competing retail stores. Porter (1980) suggests that three business strategies: cost leadership, differentiation and focus can be used as a company's positioning strategy in the industry.

The cost leadership strategy focuses on the efficiency of the production and distribution of goods and services. Sources of cost advantage may include pursuing economies of scale, proprietary technology, and preferential access to raw materials and so on. Vanguard Co., Ltd is a company engaged in game planning/ development/ publishing that has successfully implemented a cost leadership strategy. Differentiation strategy requires companies to be unique in their industry by achieving technological leadership or to create a high level of customer intimacy and must invest more in research and development activities (Bentley et al., 2013). Neutrogena is a company engaged in the field of beauty and skin care products in the world that has successfully applied a differentiation strategy (Porter, 1996). Focus strategy refers to the application of cost leadership or differentiation. Ikea is a furniture and home ware company that has successfully implemented a cost-based focus strategy.

The company cannot directly determine the business strategy to be implemented, but must go through identifying all the weaknesses of the company, its internal resources, and conducting an analysis of the external environment to be able to capture business opportunities and overcome all challenges and threats. Dess et al. (2021) stated that to create and maintain competitive advantage, companies must remain focused on observing the development of customer wants and needs, but not sacrifice their strategic position when they are in a mature position and the market position is developing.

Thomas et al. (2010) conclude that a successful business strategy capable of promoting high growth insurance companies in emerging markets involves high growth rates. Gene et al. (2015) show the results of his research that organizational structure and business strategy had a significant effect on efficiency, profitability, and risk-taking behavior. Yuliansyah et al. (2017) show that business strategy has a full mediating effect on the relationship between RISFM and firm performance. Nambisan and Rindakumar et al. (2011) show that companies with a cost leadership or differentiation strategy perform better than companies that are stuck-in-the-middle.

Pulaj et al. (2015) who examined the direct effect of Porter's strategy on company performance concluded that there is a relationship between Porter's generic strategy (cost leadership, differentiation) and company performance. Ajagbe et al. (2016) concluded that the highly competitive nature of the business environment, full of technology, and intensive knowledge dynamics makes business managers have to emphasize on developing clear mandates in the form of appropriate business strategies that will drive higher organizational performance. This shows with confidence that business strategy determines performance.

Based on the description above, it can be summarized that the implementation of business strategies can improve the company's financial performance. We therefore propose the following hypothesis:

H1. The Company’s business strategy is positively related to the company's financial performance

Relationship managerial competence and company business strategy

Competence is a behavior that includes the necessary knowledge, skills, and attributes, intelligence and talent, a person's underlying characteristics, such as traits, habits, motives, social roles, and self-image, as well as the surrounding environment for successful performance (Hayat et al., 2010). Managerial competence is the awareness and feeling of one's own abilities that can effectively improve the behavioral characteristics of managers and the results can achieve above average performance (Krajcovicova et al., 2012). Stone et al. (2013) explains that an organization must manage competencies to improve performance, integrate HR processes, and align behaviour with company values, selection, development and career paths. In assessing competence, the company must also specify the competence of the workforce as desired, with measurable performance indicators. The competency model approach does not only contain competency components, but also situational variables and outcome criteria (Teresa and Marzena, 2017). Silva et al. (2014) result in the development of a theory of managerial competence which resulted in a combination pattern of certain key competencies for management as a scheme for selecting human resources and as a basis for emphasizing development plans for employee competencies.

Managerial competence plays an important role in preparing the company's business strategy in order to win the level of
Yue and XinLin (2011) define market competition as a way of optimally allocating company resources and economic factors will have certain competitiveness to be able to win competition in the market. The general theory of market competition has given rise to the theory of the firm which is related to market structure and leads to a generalization by seeing the market as a unified whole with different levels of competition and different levels of market share. Perfect competition market is a type of market where the number of sellers and buyers (consumers) is very large and the products or goods being sold are of the same type. Monopoly is seen as a situation where there is no competition. Oligopoly market and monopolistic competition are in between the two competitions. In strategic conflict theory, a non-cooperative game is used to analyze the company's strategic design under conditions of imperfect competition, where competitor behavior is influenced, and competition develops in a good direction for the company (Chai, 2011).

There are many empirical findings regarding the influence of various forms of competitive market with business strategy. Wang (2014) states that organizations need to develop strategies in response to the industrial structure in which organizations compete to gain competitive advantage. Dixit and Stiglitz (1977) explain that the higher the market competition and the higher the substitutability between products, the lower the number of competitors in the market and the firm’s incentive to invest in R&D depends mainly on the level of technological competence, because with a higher level of technological competence, companies can increase their R&D activities when facing increasingly fierce market competition (Lee, 2009). Hahn (2010) develops a model regarding the effect of competition on firm innovation where it depends on switching costs. When switching costs are low, firms with high levels of competition are more likely to innovate while monopolists do not.

Several research results regarding the relationship between market competition and company performance with the addition of different independent variables and implicitly indicate the company's individuality. Brown and Dwyer (2000) conclude that domestic product market competition, import competition, and local labor market competition have a strong positive influence on productivity. Scott (2006) states that the market will continue to evolve and become more efficient and in a perfect market, there is some insight into what companies expect and what strategies will be effective when the going gets tough. When the market is perfect, the company must also have a perfect strategy. Companies listed in China achieve lower performance when faced with higher product market competition (Liu et al., 2017). Januszewski et al. (1999) include corporate governance and concluded that firms operating with more intensive product market competition experienced higher productivity growth rates.

Park and Shin (2016) conclude that family companies show superior company performance compared to non-family companies when the level of product market competition is weak. Chuang and Wu (2012) conclude that the greater
the competition, the stronger the impact of shareholder interlock on company performance. The relationship between the depth of shareholder interlock and firm performance is even more positive when market competition is higher than when market competition is low. Reza et al (2015) add to conclude that changes in competition lead to increased performance directly and indirectly through changes in MAS (Management Accounting System) and changes in strategy lead to higher organizational performance through changes in MAS.

Pooyan et al. (2021) add the variable the effectiveness of performance pay and conclude that competition gives rise to two opposite effects, namely the residual market effect and the response effect of competitors which vary according to competition and together produce a curved relationship between PIP effectiveness and competition. Weak competition reduces PIP reaction because there is only a small residual market, whereas strong competition reduces PIP drive, because competitors are more likely to give a balanced response. Therefore, PIP has a very strong influence in conditions of moderate competition. Kaunyangi (2014) concludes that competition has an impact on company performance. The majority of respondents indicated that new entrants, competition and purchasing power affect the company's performance.

Based on the description above, it can be summarized that market competition can be classified into weak, moderate and high market competition. Companies must determine the type of level of market competition in formulating a company strategy to gain competitive advantage. We therefore propose the following hypothesis:

H3. Market competition is related to the company's business strategy

Relationship of corporate governance and company's business strategy

Corporate governance is a set of principles accepted and applied by management from the inalienable rights of shareholders as actual owners of the company and the role of managers as trustees on behalf of shareholders. In the modern corporate regulatory system, there are four pillars, which are accountability, transparency, fairness, and disclosure (Bhasin, 2017). In the insurance industry, good corporate governance is the structure and process used and implemented by corporate organs to improve the achievement of business results targets and optimize the Company's value for all stakeholders in an accountable manner and based on laws and regulations and ethical values (Financial Service Authority Regulations).

Kobuthi et al. (2018) conclude that strategy implementation mediates the relationship between corporate governance and non-financial performance of companies listed on the Nairobi Stock Exchange. Ogbechie et al. (2009) conclude that there is a high level of board involvement in the strategic decision-making process. Al-Zu’bi, and AL-Zoubi (2016) conclude that corporate governance has a significant effect on the strategic orientation of Jordanian Islamic

Banks and Hove-Sibanda et al. (2017) state that it can improve competitiveness and company performance.

Eberhart (2012) concludes that there is a significant increase in firm value (Tobin's q) for firms that adopt the Anglo-American type of committee system. Corporate governance system with committees results in higher firm value than traditional auditor governance. The choice of a business strategy that materially increases the marginal productivity of assets at a small marginal cost, then the market value of the company can increase. Cuevas-Rodriguez et al. (2016) conclude that the importance of new ownership of the company has an impact on the company's strategy after privatization. The control system and performance evaluation were clearly in line with the company's post-privatization strategy. Jian et al. (2011) conclude that corporate governance is an intermediary variable between cross listing strategy and company performance. The cross-listing strategy does improve the company's performance. Rubino and Napoli (2020) conclude that there is a positive relationship between board independence and the adoption of environmentally responsible practices. Better environmental performance of the company can be obtained by increasing the provision of resources for board members. There is a positive effect of a large board on the company's environmental performance.

A number of powers and responsibilities that have the power to influence management decisions and reduce the opportunity for managers to make policies are referred to as corporate governance mechanisms (Sharma, 2017) which act as control tools to create a balance between the interests of the owners and agents of the company, ensuring the achievement of stakeholder desires. In a company, there are two types of governance mechanisms, namely internal and external mechanisms of the company (Azim, 2012, Sharma, 2017 and Jan, 2019).

Internal mechanisms are ways and methods used by companies that assist management in increasing shareholder value and as part of internal governance oversight must have properly defined reporting lines, setting job descriptions that include job descriptions, inherent powers and responsibilities. These internal corporate governance mechanisms include the board of directors, board committees, financial reports and auditors, ownership structure, and share-based compensation. On the other hand, external governance mechanisms include auditors, market characteristics such as market competition, brand policies and product sales, various regulations that affect products, governance codes of ethics, stock market fluctuations, creditors and debtors, and so on. Generally, external governance mechanisms are proposed by stakeholders at the general meeting of shareholders so that the company's operations are in line with expectations. The board of directors is the main people of the company who have more authority and responsibility than the company and monitor and control all management activities to maintain business performance and protect the interests of stakeholders.
Corporate governance has received international attention as a result of the decline in professional behavior in some companies. Enron and WorldCom in the US are prominent examples of corporate collapse. Directors are expected to act in a socially responsible manner. Corporate social responsibility behavior is related to important social, safety, health and environmental factors that must be adequately considered by company management (Al-Azzam et al., 2015). Poor corporate governance causes company performance to decline, financial reports are manipulated, and stakeholders are disappointed (Bhasin, 2017).

Based on the description above, it can be summarized that corporate governance is a guideline that must be applied in a company, both based on theory and regulations from the competent authority, so that this factor can increase the company's competitiveness. We therefore propose the following hypothesis:

H4. Corporate governance is positively related to the company's business strategy

Relationship of intellectual capital with company's business strategy

Several researchers have different ways of measuring intellectual capital. Kozak (2011) suggests that the concept of intellectual capital still does not have a uniform definition that is accepted to identify its subcomponents. Ramezan (2011) identifies components of intellectual capital including human capital, organizational capital or structural capital, technological capital, social capital and business process capital or customer capital. Khalique et al. (2011b) introduce a new concept and combined the main components of intellectual capital namely human capital, customer capital, structural capital, social capital, technological capital and spiritual capital in one model. Intellectual capital is an important factor for the success of organizations in a knowledge-based economy to explore and utilize the main components of intellectual to be able to enjoy a competitive advantage in the market.

In economic theory, Radjenović and Krstić (2017) state that knowledge recombination is a necessary prerequisite to produce new innovative products. Unique intangible intellectual resources become a key determinant of business performance and emphasize the importance of management in using available internal resources, namely their experience and skills in turning resources into products that will meet consumer needs, thereby contributing to the exploitation of market opportunities.

Resource-based theory has played an important role in economic theory and the focus of strategic research on competitive resources has shifted from industries with external environments to specific organizational characteristics, namely the internal environment. In this resource approach, the competitiveness of the organization is based on its resources and capabilities. Resource-based development of enterprise theory is mainly focused on building the relationship between resources and competitiveness, as well as knowing the impact on creating a sustainable competitive advantage and improving company performance. The resource-based theory of the firm observes strategy as an instrument in aligning the firm's resources and capabilities with external environmental conditions (Radjenović and Krstić, 2017a). Company resources include all assets, capabilities, organizational processes, company characteristics, information, knowledge, and so on that are controlled by the company and implement strategies to improve efficiency and effectiveness (Daft, 2010).

Firm resources can be classified into three main categories (Barney, 1991). Material resources (physical capital) related to the technology used in the company, plant and equipment, geographic location, and access to raw materials. Human resources (human capital) related to the training, experience, assessment, intelligence, relationships and insights of individual managers and employees in a company. Organizational capital related to the formal reporting structure within a company, formal and informal planning, control and coordination systems, as well as informal relationships between groups within the same company and other external companies.

Pirogova et al. (2020) explains that intellectual capital is caused by several factors, namely a) annual investment in intangible assets in companies and investment continues to increase until it exceeds investment in tangible assets; the concept of enterprise management on the basis of values, which is actively developed; b) this concept makes it possible to identify the financial levers on the success of the company's operations management and development; c) development of the knowledge economy and infrastructure that contributes to the formation, accumulation, and effective use of the company's activities; d) development of the theory of corporate resources.

The competitive advantage of a company is formed because of its ability to combine and allocate available resources to achieve competitive advantage, providing a higher rate of return on invested capital. Nikolova (2019) states that among all the factors of production that have the greatest added value is knowledge, because knowledge becomes the intellectual basis that allows companies to generate profits in the long term by ensuring the company's competitive advantage.

Companies can gain sustainable competitive advantage through implementing strategies that use the strength of internal resources and respond to opportunities outside the company and neutralize external threats as the basis for understanding competitive advantage. This view was later replaced by a new perspective - the resource-based theory believes that competitive advantage can not only be achieved through the combination of different products and markets in a given industry, but through the differences that exist in the combination of various resources in a given industry.

Altarawneh (2017) concludes that the strong significant influence of intellectual capital (human capital, relational capital and structural capital) on competitive advantage in Jordanian pharmaceutical companies and these results
support the results of research conducted by Taie (2014) in Egyptian hospitals. Igîelski (2018) concludes that the role of intellectual capital in building competitive advantage in companies is especially in improving and maintaining service quality and optimizing the staff employed. Alnachef et al. (2017) conclude that there is a significant positive correlation between human capital and structural and relational capital and competitive advantage.

There is a positive relationship between structural capital and relational capital and competitive advantage. Marczewska et al. (2020) conclude that knowledge sources can create competitive advantages that include excellence in research and development, knowledge of competitors, customers, domestic green technology market, and foreign market for green technology. Green-technology companies in Poland have a model for acquiring new knowledge that serves as the basis for the company to gain different competencies.

Goll et al. (2007) conclude that knowledge capability affects changes in strategy, which in turn affects firm performance. The environment serves as a moderator in the relationship between strategic change and firm performance. Savitri and Syahz (2019) conclude that human capital affects financial performance and competitive strategy. Competitive strategy has an effect on financial performance. Human resources are important to choose the right competitive strategy. Selection of the right competitive strategy improves financial performance.

Selection of the right competitive strategy is needed in the creation of strategies and product variations. Kuo-An et al. (2013) conclude that intellectual capital has a significant impact on business strategy and financial performance across all samples, as well as in the years before and after the financial crisis. Business strategy has a significant effect on financial performance in all samples and before the financial crisis, but not in the post-financial crisis.

Reshepi et al. (2013) conclude that entrepreneurs can better understand and use intellectual capital in the formulation of corporate strategy by investing in intellectual capital to better formulate and implement strategies in companies. By making better use of and investing in intellectual capital, entrepreneurs and their workforce can discover new business opportunities and increase their competitive advantage in the market place.

Based on the description above, it can be summarized that intellectual capital is an important capital for the company, because in carrying out the business processes of this sector company mostly relies on human resources such as planning new products, calculating premiums, calculating the insured value, marketing products and so on. These factors are factors that must be taken into account in determining the company's strategy to achieve competitive advantage. We therefore propose the following hypothesis.

H5. Intellectual capital is positively related to the company's business strategy.

Based on the previous literature review, we propose a research model in the following figure.

![Figure 1 Proposed research model](image)

**METHOD**

The subject of this research is life insurance companies in Indonesia and the object of research is the company's financial performance, company business strategy, market competition, managerial competence, corporate governance, and intellectual capital. The sampling method in this study is purposive sampling with the criteria that companies issue financial statements from 2013 to 2020 obtained from the websites of their respective companies, the Indonesian Life Insurance Association (AAJI) and the Financial Services Authority of the Republic of Indonesia (OJK).

The sampling procedure, the number of companies sampled in this study, and the determination of the research sample size are presented in the following table. The sampling procedure, the number of companies sampled in this study, and the determination of the research sample size are presented in the following table.

The data analysis methods used in this study are (a) statistical descriptive analysis which includes the minimum value, maximum value, arithmetic mean value, and standard deviation, and (b) inferential analysis consisting of multiple logistic regression and simple linear regression model with the independent variable in the form of a dummy variable.

Binary logistic regression model was used to analyze the effect of managerial competence, market competition, corporate governance, and
intellectual capital variables on business strategy which was represented in the form of a dummy variable in which life insurance companies that implemented differentiation strategies were assigned a value of 1 (one) and the company life insurance that implements a cost leadership strategy is assigned a value of 0 (zero). Simple linear regression model with the independent variable (business strategy) is used to analyze the effect of business strategy on the financial performance of insurance companies.

The mathematical model of this research is shown in the regression line equation as follows:

\[
\ln \left( \frac{P_{it}}{1 - P_{it}} \right) = \beta_0 + \beta_1 \text{ManCit} + \beta_2 \text{MarkCit} + \beta_3 \text{CGit} + \beta_4 \text{ICit} + \epsilon_{it} \quad (3.1)
\]

where

- \( \ln \left( \frac{P_{it}}{1 - P_{it}} \right) \): Probability of life insurance company implementing a differentiation strategy with code 1 or cost leadership with code 0
- \( \text{ManCit} \): managerial competence of life insurance companies
- \( \text{MarkCit} \): market competition of life insurance companies
- \( \text{CGit} \): corporate governance of life insurance companies
- \( \text{ICit} \): intellectual capital of life insurance companies
- \( \beta_0 \): Constant
- \( \beta_i \): regression coefficient
- \( \epsilon_{it} \): error
- \( i = 1, 2, 3, \ldots, t \) indexes cross-section; \( t = 1, 2, 3, \ldots \) indexes time

To test the causal relationship between business strategy and the company's financial performance can be shown in a simple regression equation as follows.

\[
F_{pit} = \delta_0 + \delta_1 B_{sit} + \epsilon_{it} \quad (3.2)
\]

where

- \( F_{pit} \): financial performance of the life insurance company (represented by return on equity)
- \( B_{sit} \): business strategy of the life insurance company is in the form of dummy variable (companies that apply differentiation strategy = 1 and companies that apply cost leadership strategy = 0)
- \( \delta_0 \): Constant
- \( \delta_1 \): regression coefficient
- \( \epsilon_{it} \): Error
- \( i = 1, 2, 3, \ldots \) indexes cross-section; \( t = 1, 2, 3, \ldots \) indexes time

RESULT AND DISCUSSION

Descriptive statistics

Report of summary statistics of variables used in the study is shown in the following table.

<table>
<thead>
<tr>
<th>Table 2 Descriptive Statistics</th>
<th>Variable</th>
<th>n</th>
<th>Min</th>
<th>Max</th>
<th>Mean (SD)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>ManC</td>
<td>176</td>
<td>238.00</td>
<td>1,230.00</td>
<td>109.414,34</td>
</tr>
<tr>
<td></td>
<td>MarkC</td>
<td>176</td>
<td>0.0000</td>
<td>0.2706</td>
<td>0.0420</td>
</tr>
<tr>
<td></td>
<td>CG</td>
<td>176</td>
<td>1.0000</td>
<td>9.0000</td>
<td>4.2800</td>
</tr>
<tr>
<td></td>
<td>IC</td>
<td>176</td>
<td>-6.1900</td>
<td>24.5500</td>
<td>2.7897</td>
</tr>
<tr>
<td></td>
<td>PM</td>
<td>176</td>
<td>-0.4800</td>
<td>0.3600</td>
<td>0.0894</td>
</tr>
<tr>
<td></td>
<td>ROE</td>
<td>176</td>
<td>-0.7600</td>
<td>1.0800</td>
<td>0.1319</td>
</tr>
</tbody>
</table>

Return on equity has minimum value of -0.7600, maximum value of 1.0800, mean value of 0.1319 with a standard deviation of 0.2278, showing that the degree of financial performance of insurance companies vary greatly. Profit margin as proxy of business strategy has minimum value of -0.4800, maximum value of 0.3600, and mean value of 0.0894 with a standard deviation of 0.1012, showing that half of the insurance companies apply differentiation strategy and some others apply cost leadership strategy.

Classification of life insurance companies based on business strategy

To identify insurance companies that implement a cost leadership or differentiation business strategy, profit margin is used according to the research of Wu et al. (2015) by determining its mean value.

Insurance companies that have a mean profit margin value below the average profit margin value are classified into insurance companies that apply a cost leadership strategy and insurance companies that have a mean profit margin value equal to or above the average profit margin value are classified into insurance companies that implement a differentiation strategy. Based on table 2, it is known that the mean value of profit margin is 0.0894, so insurance companies that implement a cost leadership or differentiation business strategy are presented in the following table.
Table 3 Classification of Companies Based on Business Strategy

<table>
<thead>
<tr>
<th>No.</th>
<th>Company</th>
<th>Profit Margin</th>
<th>Type of Business Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Ace Life</td>
<td>0.050</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>2</td>
<td>Indosurya Sukses</td>
<td>-0.010</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>3</td>
<td>Alianz Life</td>
<td>0.083</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>4</td>
<td>Sequis Life</td>
<td>0.233</td>
<td>Differentiation</td>
</tr>
<tr>
<td>5</td>
<td>Sinarmas</td>
<td>0.023</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>6</td>
<td>AIA</td>
<td>0.111</td>
<td>Differentiation</td>
</tr>
<tr>
<td>7</td>
<td>Avrist</td>
<td>0.148</td>
<td>Differentiation</td>
</tr>
<tr>
<td>8</td>
<td>Mega Indonesia</td>
<td>0.130</td>
<td>Differentiation</td>
</tr>
<tr>
<td>9</td>
<td>Tugu</td>
<td>0.114</td>
<td>Differentiation</td>
</tr>
<tr>
<td>10</td>
<td>Adi Sarana</td>
<td>0.020</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>11</td>
<td>Kresna</td>
<td>0.034</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>12</td>
<td>Generali</td>
<td>0.018</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>13</td>
<td>Bringin Life</td>
<td>0.126</td>
<td>Differentiation</td>
</tr>
<tr>
<td>14</td>
<td>Equity</td>
<td>0.050</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>15</td>
<td>Panin Daichi</td>
<td>0.098</td>
<td>Differentiation</td>
</tr>
<tr>
<td>16</td>
<td>Prudential</td>
<td>0.238</td>
<td>Differentiation</td>
</tr>
<tr>
<td>17</td>
<td>Indolife</td>
<td>0.024</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>18</td>
<td>Taspen</td>
<td>0.121</td>
<td>Differentiation</td>
</tr>
<tr>
<td>19</td>
<td>BNI</td>
<td>0.055</td>
<td>Cost leadership</td>
</tr>
<tr>
<td>20</td>
<td>Mandiri</td>
<td>0.108</td>
<td>Differentiation</td>
</tr>
<tr>
<td>21</td>
<td>Manulife</td>
<td>0.163</td>
<td>Differentiation</td>
</tr>
<tr>
<td>22</td>
<td>Heksa Eka</td>
<td>0.035</td>
<td>Cost leadership</td>
</tr>
</tbody>
</table>

Table 3 shows that there are 11 life insurance companies that apply a differentiation strategy and 11 life insurance companies that apply a cost leadership strategy.

**Hypothesis testing**

Simple regression is used to test the effect of business strategy on financial performance and the output is presented in the following table.

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.456*</td>
<td>.208</td>
<td>.204</td>
<td>.203240</td>
</tr>
</tbody>
</table>

Table 4 Model summary

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1.891</td>
<td>1</td>
<td>1.891</td>
<td>45.774</td>
<td>.000*</td>
</tr>
<tr>
<td>Residual</td>
<td>7.187</td>
<td>174</td>
<td>.041</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>9.078</td>
<td>175</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 5 ANOVA

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.032</td>
<td>.021</td>
<td>1.491</td>
</tr>
<tr>
<td></td>
<td>BS</td>
<td>.207</td>
<td>.031</td>
<td>.456</td>
</tr>
</tbody>
</table>

Table 6 Coefficients

a. Dependent Variable: ROE

b. Predictors: (Constant), Business Strategy

Yuliansyah et al., 2017; Ilmudeen and Bao, 2020; human resources, communication, strategy formulation, corporate culture and organizational structure (Nguyen and Nguyen, 2017); corporate culture (Tasgit et al., 2017).
Tables 5 and 6 show that the business strategy has significance value of 0.000 and less than alpha value of 0.05. This means that business strategy has a significant effect on the financial performance of life insurance companies and the regression equation can be written as follows:

$$FP_t = 0.032 + 0.207 BS_t$$

Binary logistic regression analysis was applied to analyse the effect of independent variables including managerial competence, market competition, corporate governance and intellectual capital on life insurance company's business strategy—whether a differentiation strategy or a cost leadership strategy. The results of binary logistic regressions are presented in the following table.

Table 7 Variables in the Equation

<table>
<thead>
<tr>
<th>Variable</th>
<th>B</th>
<th>S.E.</th>
<th>Wald</th>
<th>Df</th>
<th>Sig.</th>
<th>Exp(B)</th>
</tr>
</thead>
<tbody>
<tr>
<td>ManC</td>
<td>0.225</td>
<td>.000</td>
<td>17.127</td>
<td>1</td>
<td>0.000</td>
<td>1.000</td>
</tr>
<tr>
<td>MarkC</td>
<td>-491.245</td>
<td>121.291</td>
<td>16.404</td>
<td>1</td>
<td>0.000</td>
<td>0.000</td>
</tr>
<tr>
<td>CG</td>
<td>1.655</td>
<td>.516</td>
<td>10.298</td>
<td>1</td>
<td>0.001</td>
<td>5.233</td>
</tr>
<tr>
<td>IC</td>
<td>1.861</td>
<td>.640</td>
<td>8.448</td>
<td>1</td>
<td>0.004</td>
<td>6.428</td>
</tr>
<tr>
<td>Constant</td>
<td>-11.459</td>
<td>3.183</td>
<td>12.965</td>
<td>1</td>
<td>0.000</td>
<td>0.000</td>
</tr>
</tbody>
</table>

Source: Output of SPSS

Based on the results of the analysis presented in the table above, the following logistic regression equation is obtained:

$$\ln \left( \frac{P_{it}}{1-P_{it}} \right) = -11.459 + 0.225 \text{ ManC}_t - 491.245 \text{ MarkC}_t + 1.655 \text{ CG}_t + 1.861 \text{ IC}_t$$

Since all independent variables have a significance value below the alpha value of 0.05, it can be concluded that managerial competence, market competition, corporate governance and intellectual models partially and significantly affect the business strategy of life insurance companies. The relationship between managerial competence, corporate governance and intellectual model with business strategy is positive while the relationship between market competition and business strategy is negative.

This indicates that the higher the managerial competence, corporate governance, intellectual capital and the lower the level of market competition, the higher the probability of a life insurance company to implement a differentiation strategy.

The Omnibus tests of model coefficients indicates how well the model performs, over the one with none of the predictors entered into the model. Output of overall influence of managerial competence, market competition, corporate governance and intellectual capital on business strategy of insurance companies and the summary of the model presented in the table 8.

Table 8 Omnibus Tests of Model Coefficients and Model Summary

<table>
<thead>
<tr>
<th>Omnibus Tests of Model Coefficients</th>
<th>Model Summary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chi-square</td>
<td>Df</td>
</tr>
<tr>
<td>186.141</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: Output of SPSS

Table 8 shows that new model is significantly better as the chi-square is highly significant (chi-square=186.141, df=4, p<.000) and that 87.6 percent of the variance for business strategy of insurance companies is explained by managerial competence, market competition, corporate governance and intellectual capital in a regression model.

The Hosmer-Lemeshow test is a goodness of fit test for logistic regression, especially for risk prediction models and a goodness of fit test tells you how well your data fits the model. The output of this test is shown in the following table.

Table 9 Hosmer and Lameshow Test

| Chi-square | Df | Sig. |
| 2.181 | 8  | 0.975 |

Source: Output of SPSS
Table 9 shows that the chi-square value for the Hosmer-Lemeshow Test is 2.181 with a significance level of 0.975, ($p=0.975 > 0.05$), indicates that sample data fits the model.

**Discussion**

Table 6 shows that the company's business strategy has a positive and significant relationship with financial performance at the level of 0.00, indicating that the company's business strategy can improve the financial performance of insurance companies and this supports hypothesis 1. The results of this study support the research of Nandakumar et al. (2011) which states that business strategy is highly correlated with achieving organizational performance in the short and long term and minimizes problems; Pulal et al. (2015) stated that there is a significant positive effect of cost leadership and differentiation strategies as well as a focus on performance, so that it can help managers to design better competitive strategies to compete; Xhavit et al. (2020) stated that the implementation of a differentiation strategy has increased the company's performance to a higher level than Porter's two generic strategies, namely cost leadership and focus; Seifzadeh and Rowe (2019) stated that there is a business unit strategy and company control that has a significant effect on the financial performance of the business unit; Ajabge et al. (2016) stated that business strategy has a major role in improving organizational performance; Gene et al. (2015) who stated that organizational structure and business strategy had a significant impact on efficiency, profitability, and risk-taking behavior; Thomas et al. (2010) who stated that overall, a successful business strategy for life insurance companies entering or growing in the market developing countries have increased growth and firm size; and Seedee (2012) who stated that Thai manufacturing companies that use cost leadership and differentiation strategies place great emphasis on strategy as an important one.

Table 7 shows that managerial competence has a positive and significant relationship with business strategy at the level of 0.00, indicating that stronger managerial competence can increase profit margins, which means insurance companies have a greater probability of implementing a differentiation strategy and this supports hypothesis 2. On the contrary, managerial competence which is relatively weak lowers profit margins and this causes insurance companies have a greater probability of implementing a cost leadership strategy. The results of this study support the results of research by Agha et al. (2012) which explained the importance of various core competency dimensions on competitive advantage and organizational performance; Marczewskas et al. (2020) which stated that the new knowledge development model in Poland serves as the basis for manufacturing companies to acquire specific competencies where resources are an important factor for companies to gain a competitive advantage in a particular market; Ismail et al. (2014) concluded that managerial competence has a significant effect on competitive advantage and Nimsmith et al. (2016) explained that core competencies are the combination of knowledge pools and technical capacities that enable businesses to be competitive in the market and there is a significant relationship between core competencies and competitive advantage among Sri Lankan banking firms.

Managerial competence in insurance companies which is relatively weak (slightly) and focuses on several factors such as increasing production scale, implementing the latest technology, increasing efficiency and restricting products, tends to implement a cost leadership strategy. Porter (1998) explains that companies that implement a cost leadership strategy must have the ability to invest in sustainable capital and access to capital, process engineering skills, intensive labor supervision, products designed for ease of manufacture, and low-cost distribution systems with organizational requirements that include strict cost control, high frequency and detailed control reports, structured organization and responsibilities and incentives based on meeting strict quantitative targets.

Stronger and deeper managerial competencies are needed to implement a differentiation strategy. Companies that implement this strategy try to convince customers to pay a premium price for the product by providing unique and desirable features. Porter says that a company gives the impression that customers receive special benefits and are greater than the value paid. This managerial competence according to Porter (1998) includes high marketing ability, product engineering, creative talent, strong ability in basic research, has a company reputation in quality and technology leadership, long tradition in the industry or a combination of unique skills and excellent cooperation with distribution channels with organizational requirements that include strong coordination between engineering and development functions, product development, and marketing; use subjective measures and incentives and quantitative measures to attract highly skilled workers, scientists, or creative people.

Table 7 shows that market competition has a negative and significant relationship with business strategy at the level of 0.00, indicating that higher market competition can increase profit margins which means insurance companies have a high probability of implementing a differentiation strategy and this supports hypothesis 3. On the other hand, lower market competition decreases profit margins and this causes insurance companies have high probability of implementing a cost leadership strategy. The source of this strategy comes from the unit cost that is lower than the average unit cost of the insurance industry. This relative cost advantage allows insurance companies to price insurance products lower than competitors to increase market share and still make a profit.

Insurance companies that implement a differentiation strategy are characterized by increased profit margins. This differentiation advantage is felt by customers in the form of higher product quality with a lower level of risk compared to product quality and risks from competitors. This advantage allows insurance companies to charge higher prices for insurance products with superior product quality and service delivery compared to costs paid by customers and compared to competitors. This superior product can be in the form of a higher insurance value, ease of communication with insurance companies,
flexibility and convenience in policy payments, ease of redeeming cash value, flexible products and so on.

The source of cost advantage or differentiation from this insurance company comes from the ability of internal resources in designing, providing services and marketing as well as after-sales service for insurance products involving several competent departments or people such as actuaries, finance, underwriters, marketing and investment departments with due regard to financial services authority regulatory factors, economic conditions, level of competition, company and market resource capabilities. They must design insurance products according to the market segments served and position their products in the market according to the business strategy used and companies that apply cost leadership or differentiation strategies must be superior in their respective market segments compared to competing products.

In designing these insurance products, investment activities, product marketing and information technology, digital and communication, the human resources of insurance companies are always enhanced with their abilities and skills. This improvement in human resource competence is proven by every human resource working in an insurance company is required to have a certification of expertise according to their respective levels, and insurance companies' budget for education and training costs every year to increase the competence of their human resources.

Insurance companies in setting life insurance premium rates need to consider: (a) pure premiums calculated based on interest rates, mortality tables, or morbidity tables used (b) acquisition costs, administrative costs and other general costs; and (c) forecasted investment returns from premiums. A life insurance policy must contain the minimum requirements: (a) when the coverage is effective (b) a description of the agreed benefits (c) the method of payment of premiums or contributions (d) grace period for payment of premiums or contributions (e) the exchange rate used for the insurance policy in foreign currency if the payment of Premiums or Contributions and benefits are linked to rupiah currency (f) the time recognized as the time when the payment of Premiums or Contributions is received (g) the Company's policy is determined if the payment of Premiums or Contributions is made past the agreed grace period (h) the period when the Company cannot review the validity of the insurance contract (incontestable period) on long-term insurance products (i) cash value table, for insurance products marketed by life insurance companies that contain cash value (j) calculation of dividends on insurance policies or the like, for insurance products marketed by life insurance companies that provide insurance policy dividends or the like (k) termination clause of coverage, both from the Company and from the policy holder, insured, or participant, including the terms and causes (l) terms and procedures for filing a claim, including relevant supporting evidence and requirements in filing claims (m) procedures for settlement and payment of claims (n) a dispute settlement clause which includes, among other things, a settlement mechanism inside and outside the court and the selection of the domicile for dispute resolution and (o) the language used as a reference in the event of a dispute or difference of opinion, for insurance policies printed in 2 (two) language or more.

Table 7 shows that corporate governance has a positive and significant relationship with business strategy at the level of 0.001, indicating that stronger corporate governance can increase profit margins, which means insurance companies have a high probability of implementing a differentiation strategy and this supports hypothesis 4. The results in line with the results of research by AL_Qatawneh (2015) and Kobuthi, et al. (2018) which states that corporate governance affects the achievement of competitive advantage; Al-Azzam et al. (2015) which states that Venture Capital companies with few employees, the company's board of directors and its investment committee play an important role in helping managers drive corporate strategy and achieve the goals and objectives set; Hove-Sibanda et al. (2017) which states that the implementation of corporate governance by SMEs significantly and positively affects competitiveness and performance; and POJK number 73/POJK.05/2016 regarding good corporate governance for insurance companies which states that insurance companies are required to have at least three members of the board of directors. This regulation indicates that the greater the number of members of the board of directors, the fewer duties and responsibilities of each member of the board of directors with increasing work quality.

Table 7 shows that the company's intellectual capital has a positive and significant relationship with business strategy at the level of 0.004, indicating that the stronger the company's intellectual capital can increase profit margins, which means insurance companies have a high probability of implementing a differentiation strategy and this supports hypothesis 5. Intellectual capital is an asset in the form of various knowledges, skills, expertise possessed by the company's human resources that support competitive advantage to achieve goals by providing added value for stakeholders. According to Moltar et al. (2015) that the main components of intellectual capital include human capital, customer capital, structural capital, social capital, technological capital, and spiritual capital. This human capital includes the expertise, knowledge and competence of the workforce for certain fields in insurance companies. This customer capital relates to the ability and knowledge of marketing channels and relationships with insurance customers. This structural capital includes the ability and knowledge of systems and organizational structures, infrastructure, data and information and procedures and policies in insurance companies. This business capital includes the ability and knowledge of business processes and stakeholders in insurance companies. This social capital includes skills and knowledge regarding the formation and improvement of social networks, informal relationships, formal relationships and public trust in insurance companies. Technological capital includes the ability and knowledge of information technology, research and development and protection rights implemented in insurance companies. This spiritual capital includes the ability and knowledge related to
religion and ethical values applied in insurance companies.

An insurance company that implements a differentiation strategy emphasizes increasing skills, expertise and knowledge in order to create a competitive advantage in the market by providing superior and unique products and services that are perceived by customers as compared to competitors. The results of this study support research from Altarawneh (2017) which states that intellectual capital construction has a competitive advantage; Rochmadhona et al. (2018) which state that sources derived from the intellectual capital component can create competitive advantage; Rexhepi et al. (2013) who state that through better use and investment in intellectual capital, employers and workers can find opportunities for new businesses and increase their competitive advantage in the market; Taie (2014) which states that there is a correlation between human capital, structural capital and relational capital and competitive advantage; and Igielski (2018) which states that the role of intellectual capital in building competitive advantage in the surveyed companies - especially in fields related to improving and maintaining service quality and optimization.

CONCLUSION

In this study, we examine the relationship between business strategy and financial performance and the relationship between managerial competence, market competition, corporate governance and intellectual capital with business strategy using a sample of life insurance companies in Indonesia from 2013 to 2020. We divide business strategy by profit margin proxy based on Wu et al. (2015) into cost leadership and differentiation based on Porter's (1980) strategy typology and financial performance proxied by return on equity. First, we examine the relationship between business strategy and financial performance of life insurance companies and find that business strategy has a significant effect on the financial performance of life insurance companies. Life insurance companies that implement a business differentiation strategy with market segments (middle income customers and above) which are characterized by increased profit margins tend to have improved financial performance. Life insurance companies that implement a cost leadership business strategy with market segments (lower middle income customers) which are marked by a decrease in profit margins also tend to have improved financial performance. Second, we conduct further research by partially testing the effect of managerial competence, market competition, corporate governance and intellectual capital with business strategy. Our findings show that managerial competence, market competition, corporate governance and intellectual capital have a partial and significant effect on business strategy. This indicates that life insurance companies that have strong managerial competence face a higher level of market competition, have better corporate governance and intellectual capital tend to implement a business differentiation strategy, but life insurance companies that have weak managerial competence face a higher level of business differentiation. Strong market competition, weak corporate governance and intellectual capital tend to implement a cost leadership business strategy. The results show that business strategy plays an important role in improving the financial performance of insurance companies. The determination and implementation of a life insurance company's business strategy is influenced by managerial competence, market competition, corporate governance and intellectual capital. These four factors either simultaneously or partially affect the business strategy applied by life insurance companies. Therefore, in determining a business strategy, whether a differentiation strategy or a cost leadership strategy, life insurance companies need to consider these four factors. The differentiation strategy is more suitable for life insurance companies that have good managerial competence, corporate governance and intellectual capital with higher level of market competition, but on the other hand life insurance companies that have good managerial competence, corporate governance and intellectual capital with level of lower market competition is more suitable for implementing a cost leadership strategy.

REFERENCES


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