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The Moderating Effect of Firm's Behavior on the Relationship Between Internationalization and Firm's Performance

Andreas Santoso and Deddy Marciano

Universitas Surabaya

E-mail: Us31143@gmail.com; marciano@staff.ubaya.ac.id

Abstract: This study aims to determine (1) to understand the influence of corporate behavior's elements, which include slack, and attainment discrepancy, which moderated the relationship between internationalization and performance, (2) to understand the effects of different types of slack towards relationship between internationalization and performance. This study uses a quantitative approach with a model of ordinary least square. This study used a sample of companies in the manufacturing industry, which has listed on the Indonesia Stock Exchange during the period of 2013-2014. The number of observations used in this study was 184 observations. The results showed that low-discretion slack and attainment discrepancy significant positively moderate the relationship between internationalization and performance. The manufacturing industry in Indonesia is in the early phase of internationalization. High-discretion slack variable does not significantly moderate the relationship between internationalization and performance.

Key words: Internationalization, Firm's Behavior, Organizational Slack, Attainment Discrepancy

INTRODUCTION

Globalization in the business world has eliminated geographical restrictions as a prohibitive factor to conduct a business practice. Thus, companies tend to be motivated to expand internationally in order to increase their competitiveness. Pla-Barber and Alegre (2007) stated that there was a significant positive correlation between export intensity and innovation. This research based on the idea that the strategy of international expansion are very important catalyst of growth, this caused by the increasing intensity of competitive pressures.

Internationalization undertaken by a firm will directly affect the firm's performance. Various studies have been conduct to understand the relationship between internationalization and performance of the firm. The mixed results could be due to the differences in research coverage on internationalization phase

(early, mid-stage, high). The success of a firm in maintaining its performance during internationalization cannot be separated from the internal state of the firm itself. Cyert and March (1963), George (2005) and Tseng *et al.* (2007) in Lin *et al.* (2011) stated, “Internal firm-specific characteristics are a crucial determinant of performance progress”. Lin *et al.* (2011) states, the central tenet of firm behavioral theory highlights 6 elements of firm behavior: (1) performance, (2) slack (the difference between the total resource and the minimum resources necessary to produce a number of output), (3) Aspirations (desired level of performance), (4) expectations (anticipated level of actual performance), (5) risks, and (6) the size of the organization.

Lant and Montgomery (1987) combine the expected performance and aspired performance into a single construct called “Attainment discrepancy”. Results stated that the level of attainment discrepancy influences risk taking. If the anticipated level of actual performance is lower than the expected level of performance, the firm will look for ways to improve its expected performance. Efforts to improve firm’s performance often require an increase in risk-taking level. Wiseman and Bromiley (1996) state a direct relationship between attainment discrepancy, slack, and risk taking. Palmer and Wiseman (1999) state a positive relationship between attainment discrepancy and risk-taking whereas slack and risk-taking has a negative relationship. Sharfman *et al.* (1988) in Lin *et al.* (2011) differentiate organizational into high-discretion slack and low-discretion slack. Different types of lack have different influences to the organization (Geiger and Cashen, 2002; Greenley and Okemgil, 1998; Tan and Peng, 2003 in Lin *et al.*, 2011). Based on the results of previous studies, it is not appropriate to ignore attainment discrepancy and organizational slack in understanding the relationship between internationalization and performance of the firm.

LITERATURES REVIEW

One of the requirements of the firm is to improve its growth and performance. One way to improve the growth of the firm is to conduct international expansion (Kim *et al.*, 1989 in Lin *et al.*, 2009). Welch and Luostarinen (1988) in Prange and Verdier (2011) define internationalization as “the process by which firms increase their involvement in operations across borders”. Bartlett and Ghoshal (1989) in Lin *et al.* (2011) stated that globalization and free trade motivate the firm to increase its presence internationally. The firm has many considerations (benefits - costs) of doing internationalization, especially if related to FDI (Foreign Direct Investment). This is due to the high uncertainty that exist in the international market.

Performance is the ability of a firm to generate a return at a specific period. The Firm has an obligation to maintain and improve its performance. By doing internationalization, the firm hopes there will be an improvement in performance. Porter (1985) in Krist (2009, p.75) stated, “The internationalization of activities holds benefits such as the utilization of relationships among different businesses and geographic areas”.

The relationship between internationalization and performance has long debated. Previous research has expressed mixed results regarding the relationship internationalization and performance. Indicators used to measure the degree of internationalization and performances that are used are diverse. Hosea (2015) in her research regarding the relationship between internationalization and performance states that the early phase of internationalization began with FSTS of 0% to 18%. In this phase, the firm has not reached economies of scale so that an increase in the degree of internationalization will increase the cost of the firm. After this phase, the firm will enter mid-stage phase of internationalization. In this phase, firm

can exploit the benefits of internationalization. High internationalization starts with FSTS above 67%. In this phase, increasing the degree of internationalization will bring more cost compared to the benefits that can be obtained. This study uses the relationship between internationalization and performance with linear shapes. Based on research Hosea (2015), allegedly negative linear relationship exists on the relationship between internationalization and performance of the sample used.

The success of a firm to maintain its performance when performing internationalization is strongly influenced by the firm's behavior itself. This is because the firm's behavior significantly influences the development of performance (Tseng *et al.*, 2007) in Lin *et al.* (2011). The firm's behavior that became the focus of this research is the organizational slack and attainment discrepancy. Both of these reflect the availability of resources and internal motivation of firm in doing internationalization.

The firm's behavior in this study refers to "A Behavioral Theory of the firm" initiated by Cyert and March (1963). Mahoney (2011) stated, "Cyert and March focus on a small number of key economic decisions are made by the firm and develop process-oriented models of the firms". Lin *et al.* (2011) states, the central tenet of firm behavioral theory highlights 6 elements of firm behavior: (1) performance, (2) slack (the difference between the total resource and the minimum resources necessary to produce a number of output), (3) Aspirations (desired level of performance), (4) expectations (anticipated level of actual performance), (5) risks, and (6) the size of the organization.

One of the moderators of the relationship between internationalization and performance is organizational slack. The amount of slack owned by a firm influences its ability to maintain good performance when doing internationalization. Due to the presence of slack, the firm's management can more freely perform internationalization. Slack is defined as the difference between the total resource and the minimum resources necessary to produce a number of outputs (Cyert and March, 1963 Lin *et al.*, 2011). Lin *et al.* (2009) states, slack has three aspects. First, the slack is a resource that has not been used optimally. Second, slack has the characteristics of the location (absorbed or unabsorbed) and accessibility (immediately or deferred).

Third, the function of the slack is as a buffering mechanism to counter the threat or as a facilitator to take advantage of opportunities. Bourgeois (1981) in Lin *et al.* (2009) states that "organizational slack is that cushion of actual or potential resources which allow an organization to adapt successfully to internal pressures for adjustment or to external pressures for change in policy, as well as to initiate changes in strategy with respect to the external environment". Based on the definition of the Bourgeois, many researchers have tried to classify and elaborate further slack. Sharfman *et al.* (1988) in Lin *et al.* (2011) states that "organizational slack should be anchored along the continuum of managerial discretion, and distinguished between high- and low-discretion slack".

High-discretion slack is readily available resources (Bourgeois and Singh, 1983; Cheng and Kesner, 1997 in Lin *et al.*, 2011). High-discretion slack can be cash and receivables that can be used for various situations. High-discretion slack can be measured using current ratio. George (2005) in Lin *et al.* (2011) states that high-discretion slack has a large influence on performance. With high-discretion slack that more companies can more freely face uncertainty when performing internationalization. Companies can suppress turmoil that is bad for productivity and performance. On the other hand, the availability of high-discretion slack allows the firm to take advantage of opportunities well. Bourgeois (1982) in Lin *et al.* (2009) states that "Organizations can afford to experiment with new strategies when slack is presented".

Low-discretion slack is an untapped debt capacity by the firm. Low-discretion slack can be measured using equity to debt ratio. Burgeois and Singh (1983) in Lin *et al.* (2011) suggest that low-discretion with more slack indicates that the firm has the potential slack or greater debt capabilities. As with any high-discretion slack, George (2005) in Lin *et al.* (2011) suggest that low-discretion slack has a considerable effect on the performance. Companies with more low-discretion slack can easily perform internationalization and creating a good performance. This is caused by firm not having large debt. Martinez and Artz (2006) in Lin *et al.* (2009) suggested a positive relationship between the potential slack and managerial risk taking. This is in line with the threat-rigidity argument which states that “when a firm’s survival is in doubt, it becomes rigid and its risk-taking is reduced” (Staw *et al.*, 1981 in Lin *et al.*, 2009). A company with small debt generally is a firm that is “healthy”. Management will tend to expand when he is confident the state of the firm. Wiseman and Bromiley (1996) states that “potential slack increase of encourages both experimentation and innovation”.

Another moderator of relationship between internationalization and performance is attainment discrepancy. Attainment discrepancy is defined as the difference between the actual and aspired performance (Lant and Montgomery, 1987). Schneider (1992) in Lin *et al.* (2011) defines aspiration level as the “smallest outcome that would be deemed satisfactory by the decision maker.” Attainment discrepancy can be moderated relation to the Performance of internationalization because it can affect the firm’s internationalization strategy. Companies with performance worse than expected is likely to be motivated to carry out projects that are more at risk to increase returns and improve performance. Feigenbaum *et al.* (1996) in Lin *et al.* (2011) states that “individuals adopt risk-seeking behavior when the expected outcomes of Reviews their actions are below a given reference point”.

Age is an important factor affecting the performance of the firm. The relatively young firms are more likely to adapt to internationalization. This is due to the management structure more flexible and proactive in catching opportunities. Zahra *et al.* (2000) in Krist (2009, p.33) states that the phenomenon of “born global” shows that since the 1990s, the firm tends to internationalize early in its life cycle. However, there are other studies that state differently. Yip *et al.* (2000) in Lin *et al.* (2009) states that “older firms are relatively more international market has commitment and organizational resources, which in turn, affect their internationalization”.

The size of the firm is one of the mirror of financial resource availability. Bloodgood *et al.* (1996) in Krist (2009, p.34) states the importance of the availability of resources in the decision to internationalize. Quer *et al.* (2007) in Lin *et al.* (2011) states that “large size also indicates a strong capability and an abundance of resources to deal with complex foreign information”. Both of the above statement is supported by research Zaheer (1995). Zaher (1995) in Krist (2009, p. 34) states that “Often small firms lack the financial resources for investing in assets like internationalization experience”.

One way to control the performance of a firm is to perform bonding mechanism. One way of doing that is by distributing bonding mechanism to the management firm’s shares. Anderson *et al.* (2003) states that “the performance of a firm may increase is with greater insider shareholding losses due to lower agency”. Insider shareholder in this regard include the family, directors and top managers

RESEARCH METHOD

The population used in this study is firm incorporated in the manufacturing sector and has listed on the Indonesia Stock Exchange in 2013-2014. Data testing uses regression test that takes into account the value

of the F-statistic, T-statistic, and R². To ensure that the regression equation was inaccurate, unbiased, and consistent then classical assumption including normality test, multicollinearity test, autocorrelation and heteroscedasticity test are performed.

Regression tests carried out in stages in accordance with the rule of parsimony. The rule of parsimony states that, "an explanation involving fewer components is better than one involving more" (Zikmund, 2009, p. 595). There are 5 models of regression. Regression testing for all models uses the OLS equation (Ordinary Least Square). Below are regression equations used:

Regression Equations Model 1:

$$ROA = X \beta_0 + \beta_1(FSTS) + \epsilon_1$$

Regression Equations Model 2:

$$ROA = X \beta_0 + \beta_1(FSTS) + \beta_2(CR) + \beta_3(FSTS) \times (CR) + \epsilon_2$$

Regression Equations Model 3:

$$ROA = X \beta_0 + \beta_1(FSTS) + \beta_2(EDR) + \beta_3(FSTS) \times (EDR) + \epsilon_3$$

Regression Equations Model 4:

$$ROA = X \beta_0 + \beta_1(FSTS) + \beta_2(AD) + \beta_3(FSTS) \times (AD) + \epsilon_4$$

Regression Equations Model 5:

$$ROA = X \beta_0 + \beta_1(FSTS) + \beta_2(CR) + \beta_3(EDR) + \beta_4(AD) + \beta_5(FSTS) \times (CR) + \beta_6(FSTS) \times (EDR) + \beta_7(FSTS) \times (AD) + \epsilon_5$$

Description

ROA = the average of return on assets prior 3 years.

X = control variable consisting of firm age (AGE), firm size (SIZE), and insider ownership (IND).

(FSTS) = Degree of internationalization as measured by foreign sales to total sales.

(CR) = Current ratio

(EDR) = Equity to debt ratio

(AD) = Attainment discrepancy

Beta coefficient test performed on moderator variables that have been shown to significantly moderate the relationship between the independent variable and the dependent variable. Test done by dividing the sample into two categories then regression performed between FSTS and ROA.

1. Firm with more high-discretion slack : $CR > \text{Mean } CR + 1\text{StDev } CR$
2. Firm with less high-discretion slack : $CR < \text{Mean } CR - 1\text{StDev } CR$
3. Firm with more low-discretions slack : $EDR > \text{Mean } EDR + 1\text{StDev } EDR$
4. Firm with less low-discretion slack : $EDR < \text{Mean } EDR - 1\text{StDev } EDR$
5. Firm with higher attainment discrepancy : $AD > \text{Mean } AD + 1\text{StDev } AD$
6. Firm with lower attainment discrepancy : $AD < \text{Mean } AD - 1\text{StDev } AD$

RESULTS AND DISCUSSION

Based on the test results of the F-statistic and T-statistic on model 1, the degree of internationalization which measured by foreign sales to total sales has significantly negative effect on the firm's performance which measured by return on assets. This means that the higher the degree of internationalization, the firm's performance would be worse. Based on the determinant coefficient test, it is knows that variables in Model 1 are able to explain the dependent variable by 17% while 83% is explained by other factors. These results are consistent with the initial allegations of researcher, which based on research done by Hosea (2015) which states that in the early phase of internationalization (0% -18%), the cost of the firm will increase.

The sample used has a degree of internationalization with a mean of 25%, a median of 16%, a maximum of 100%, and a minimum of 0.018%. Such data proves that the manufacturing sector in Indonesia is in the early phase of internationalization so that the relationship between internationalization and performance is negative.

Table 1
Results Summary of Regression Testing

Variabel	Model 1		Model 2		Model 3		Model 4		Model 4 (Common Effect)		Model 5	
	Coefficient	T-Statistic	Coefficient	T-Statistic	Coefficient	T-Statistic	Coefficient	T-Statistic	Coefficient	T-Statistic	Coefficient	T-Statistic
AGE	0.001424***	3.030072	0.001433***	3.064844	0.001439***	3.148111	-0.004216***	-25.43856	0.001503***	4.4414412	-0.005789***	-15.90406
SIZE	0.029446***	2.63014			0.026105**	2.39433	-0.009632***	-3.185583	0.036103***	4.024625	-0.00328	-0.594639
IND	-0.059395	-0.77247	-0.060655	-0.77785	-0.090367	-1.20126	-0.090067**	-3.276972	-0.059551	-0.001126	-0.057466	-0.850444
FSTS	-0.102516***	-3.64623	-0.129283***	-3.53558	-0.144097***	-4.89253	-0.092516***	-32.15731	-0.068721**	-2.391846	-0.091021***	-10.67709
CR			0.000418	0.103883							0.001263***	4.085802
EDR					-0.001333	-1.196597					-0.000793***	-5.758482
AD							0.170406***	41.38423	-0.099481	-0.991247	0.168804***	28.29577
FSTS*CR			0.01618	1.317793							-0.006178	-1.315714
FSTS*EDR					0.048760***	3.794589					0.032131***	4.117313
FSTS*AD							0.100461***	5.368006	-0.218922	-0.691815	0.098912**	3.371455
R-Squared	0.16983		0.184839		0.230556		0.999985		0.282508		0.999794	
F-Statistic	9.154614***		6.689156***		8.839389***		60023.24***		11.61545***		3944.731***	
Δ F-Statistic			-2.465458		2.150233		60014.40		2.776061		-56078.51	
P < 1%	***											
P < 5%	**											
P < 10%	*											

The test results of the F-statistic and T-statistic on Model 2, the interaction between high-discretion slack with the degree of internationalization moderates insignificantly positive ($\hat{\alpha} > 5\%$) the relationship between internationalization and performance. Based on the determinant coefficient test, it is knows that variables in Model 2 are able to explain the dependent variable by 18% while the remaining 82% is explained by other factors. The insignificant moderating effects of high-discretion slack on the relationship between internationalization and performance can be caused by the dispersed characteristics of the sample used. Based on the results of the statistical description, it is known that the moderator variable FSTS*CR has the largest standard deviation (0.668269) compared to the other moderator variables.

On Model 3, the interaction between low-discretion slack with the degree of internationalization moderates significantly positive the relationship between internationalization and performance. Based on the determinant coefficient test, it is known that variables in Model 3 are able to explain the dependent variable by 23% while the remaining 77% is explained by other factors. Based on the test results of the beta coefficient, proved that the firm's performance with more low-discretion slack becomes less negative when performing internationalization compared to firm with less low-discretion slack. It can be seen through the beta coefficient differences in the two samples. Firm with more low-discretion slack has a beta coefficient of -0.655738 while firm with less low-discretion slack has a beta coefficient of -3.513178. These results are consistent with the initial allegations of researcher based on the research of Burgeois and Singh (1983) in Lin *et al.* (2011) which states that "higher level of low-discretion slack indicates more potential slack or greater borrowing power", and research and Bromiley Wiseman (1996) which states that "the potential slack both increase and encourages experimentation and innovation". Firm with more low-discretion slack can more easily perform better when doing internationalization because not burdened by a huge debt.

Based on the test results of the F-statistic and T-statistic on Model 4, the interaction between the attainment discrepancies with the degree of internationalization moderates significantly positive moderates the relationship between internationalization and performance. Based on the determinant coefficient test, it is known that the variables in Model 4 are able to explain the dependent variable by 99%, while the remaining 1% is explained by other factors. Based on the test results of the beta coefficient, proved that the firm's performance with higher attainment discrepancy becomes less negative when performing internationalization compared with firm with lower attainment discrepancy. It can be seen through the beta coefficient differences in the two samples. Firm with higher attainment discrepancy has a beta coefficient of -0.233266 while firm with lower attainment discrepancy has a beta coefficient of -1.741402. These results are consistent with the initial allegation of researcher and research results Feigenbaum et al (1996) in Lin *et al.* (2011) which states that "individuals adopt risk-seeking behavior when the expected outcomes of their actions are below a given reference point". Firm with higher Attainment discrepancy would be more motivated to perform internationalization in order to improve performance.

CONCLUSIONS AND RECOMMENDATIONS

Based on the obtained results of hypothesis testing, the high-discretion slack, low-discretion slack and attainment discrepancy positively moderate the relationship between internationalization and firm performance in the manufacturing sector listed in Indonesia Stock Exchange period 2013-2014.

For further research, it can be used as reference material by adding the longer study period, measuring instrument of degree of internationalization (foreign assets to total assets), measuring instruments of firm size (log total assets), using return on equity as the dependent variable, using internationalization with quadratic and cubic forms as independent variables and testing the moderating effects simultaneously. It is given that this study has limitations that moderating effects testing only done partially. These references are expected to make the results more accurate.

For investors, it can be used as consideration in making an investment decision on the capital markets. Internationalization phase favorable for the firm is a mid-stage internationalization with the degree of internationalization between 18% and 67%. Therefore, investors should consider the degree of internationalization undertaken by a firm, in this case, export. It is expected that firm in mid-stage

internationalization phase can generate greater returns than the firm in the early internationalization phase and high internationalization phase.

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