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The Role of Strategic Capabilities and Differentiation Strategy in Improving Organizational Performance

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ABSTRACT

Strategic capability is a complex and accumulated set of skills and knowledge that enables an organization or business unit to coordinate activities and use its assets to create economic value and sustainable competitive advantage. A competitive advantage can be supported by activities that uselow cost and create something different or differentiation. Competitive advantage is a process in which a company is able to use its resources and capabilities in creating uniqueness and degrees of difficulty for other actors to follow or imitate, thereby providing added value or more for its customers. This paper discusses the relationship between strategic capabilities and differentiation strategies in improving organizational performance.

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KEYWORDS: *Strategic Capability, Differentiation Strategy, Organizational Performance*

INTRODUCTION:

Every organization was founded to achieve certain goals desired by the founders of the organization. Therefore, the organization always strives in such a way that what is its goal can be achieved. One of the guarantees for achieving organizational goals is organizational performance in carrying out daily routines. Good performance depends on many factors including the organization's strategy, especially the compilers and executor of the strategy itself, namely the manager and other key factors such as the owner of the organization. . Strategic capabilities represent a key component of resources that form the basis for achieving an organization's competitive advantage (DeSarbo, 2005). Strategic capability is a complex and accumulated set of skills and knowledge that enables an organization or business unit to coordinate activities and use its assets to create economic value and sustainable competitive advantage. This paper discusses the relationship between strategic capabilities and differentiation strategies in improving organizational performance

Dynamic Capability and Strategic Capability

Resource dependency theory is the basis for understanding the importance of dynamic capabilities. In the perspective of strategic management, the theory of resource dependence has changed to a resource-based approach (Gudono, 2014). The resource-based approach (Resource-based View = RBV) assumes that an organization's success in competition depends on its resources. These resources must be valuable, rare, difficult to imitate and difficult to substitute.

Dynamic capability is the implementation of RBV towards strategic management (Permana, Laksmana&Ellitan, 2017). RBV emphasizes the importance of resources in determining organizational success. However, the resources owned by an organization do not necessarily become dynamic capabilities if they are not developed through routine activities within the organization so that different competencies can be created from these resources. The concept of capability was first put forward by Penrose (1959 in Sigh & Oberoi, 2013) as a "comprised of bundle of potential services". Resources can be shared by all organizations but the capabilities to integrate, manage and implement them effectively can vary widely in different organizations.

Dynamic capabilities are organizational capabilities related to adapting changes in the external environment to the interior and exterior of the organization (Teece et al., 1997). Permana and Ellitan (2020) suggest that dynamic capabilities are a set of specific and identifiable processes such as product development, strategic decision making and alliances. Dynamic capabilities are also defined as competencies that enable organizations to quickly configure organizational structures and routines to respond to new opportunities (Fan, et al., 2004 in Sigh &Oberi, 2013)

Dynamic Capabilities

Teece et al. (1997) suggested 3 typologies of dynamic capabilities, namely integration, transformation, and learning. Resource integration capability refers to the knowledge, know-how, and routines used in the organization to synergistically combine existing resources. Resource transformation capability refers to the organization's ability to develop its resources to suit the needs of the organization in facing competition or increasing internal efficiency. Resource learning capability refers to the organization's ability to create new knowledge for the development of innovation and solutions to problems faced by the organization. Eisenhardt & Martin (2000) added a fourth typology to the typology developed by Teece, et al. (1997). The fourth typology is the capability of acquiring and releasing resources. This fourth capability is almost the same as the third capability, namely learning. However, the emphasis on this fourth capability is not on acquiring resources but on releasing resources. The ability to release resources is the ability of the organization to share its resources with the parts of the organization that need it.

Datta. (2009) classify dynamic capabilities into 6 classifications, namely financial management capabilities, product development capabilities, human resource management capabilities, strategic planning capabilities, sales and marketing capabilities, and partnership management capabilities. One of the rational reasons for the importance of discussing dynamic capabilities in the management process is research which finds that organizational resources do not automatically affect organizational performance (Sigh &Oberi, 2013). Sigh &Oberi, (2013) found that in an unstable environment, organizational resources do not have a direct effect on performance. Resources affect performance through the dynamic capabilities of the organization.

Differentiation Strategy and Organization Performance

Govindarajan (1988) conducted research on 24 companies in the United States. The sample in this study were managers and supervisors at these 24 companies. The results of this study indicate that companies that implement differentiation strategies and their managers have high internal locus of control have high performance. On the other hand, companies that implement cost leadership and their managers have high external locus of control have high performance. This study confirms the importance of conformity between the characteristics of managers and the strategy adopted by a company.

Powers & Hahn (2004) conducted research on banking in the United States. Data collected from 98 CEOs were analyzed and showed that cost leadership strategies were more effective than focus strategies and differentiation strategies. The effectiveness of cost leadership in this study is due to the fact that banking consumers are price sensitive consumers. Another study which shows that there is no influence of differentiation strategy on organizational performance is the research conducted by Valipour&Honarbakhah (2012) on 45 companies in Iran. Researchers classify companies based on the strategy used. The cost leadership strategy has been shown to have a positive effect on company performance. While the differentiation strategy, although proven to have an effect on performance, the direction of the effect is not as expected. In this study it is proven that the differentiation strategy has a negative effect on organizational performance. Likewise, research conducted by Aliqah (2012) on 33 industrial companies in Jordan. This research examines the effect of differentiation strategy and firm size on organizational performance. The results of the study do not show the effect of differentiation strategy on organizational performance. Firm size is proven to have an effect on organizational performance.

Leitner &Guldenberg (2010) conducted research on small and medium-sized companies in Austria. This study compares the use of cost leadership strategies and differentiation strategies. Both strategies have been proven to generate good profits and growth for SMEs who implement them. SMEs that implement a cost leadership strategy and those that apply a differentiation strategy have higher financial performance and growth than SMEs that do not have a strategy that is not proven. Meanwhile, SMEs that implement a combination strategy are proven to have higher financial performance and growth than SMEs that do not have a strategy.Prajogo (2007) conducted research on companies in Australia. This research analyzes the effect of differentiation strategy and cost leadership on the quality of organizational performance. The differentiation strategy is proven to have an effect on the quality of organizational performance while the cost leadership strategy is not proven. This study also found that there is a positive interaction between cost leadership strategy and differentiation strategy in predicting the quality of organizational performance.

Strategic Capability and Organizational Performance

Desarbo et al. (2005) conducted research on 709 companies in 3 countries, namely China, Japan and the United States. In this study, it was found that there are differences in strategic capabilities, environmental uncertainty, and performance in a group of companies based on the Miles & Snow strategic framework. Parnel et al. (2011) conducted research on retailers in Argentina, Peru and the United States. In this study it was found that there is a positive influence of cost leadership strategy, focus strategy, and differentiation strategy on organizational performance. Strategic capabilities affect the organizational performance of retailers in America and Peru, while in Argentina not all strategic capabilities affect organizational performance (only marketing linkage capabilities).

Successful businesses that emphasize focus strategies have higher strategic capabilities in marketing capabilities. Successful businesses that emphasize differentiation strategies have higher strategic capabilities in technology capabilities. Meanwhile, successful businesses that emphasize cost leadership strategies have higher strategic capabilities in management capabilities. Sigh & Oberoi (2003) conducted a study on 102 manufacturing companies in India. The purpose of this study is to evaluate the relative impact of dynamic capabilities on various dimensions of strategic flexibility. In this study, Sigh & Oberoi (2013) found a significant contribution from dynamic capabilities (human resource capabilities, innovation capabilities, technological capabilities, alliance capabilities, and research and development capabilities to management flexibility at various strategic levels of manufacturing companies in India.

Relationship between Differentiation Strategy and Organizational Performance

Organizations that implement product differentiation strategies are required to develop unique products or services to increase customer loyalty to certain brands (Valipour, et al., 2012). An organization that implements a differentiation strategy will tend to invest heavily in research and development. The uniqueness of these products can be in the form of higher quality or different product features than product features produced by other organizations.

Govindarajan (1988) found that companies that implement a differentiation strategy and their managers have a high internal locus of control have high performance. On the other hand, companies that implement cost leadership and their managers have high external locus of control have high performance. Research conducted by Leitner &Guldenberg (2010) on small and medium-sized companies in Austria. This study compares the use of cost leadership strategies and differentiation strategies. Both strategies have been proven to generate good profits and growth for SMEs who implement them.

SMEs that implement a cost leadership strategy and those that apply a differentiation strategy have higher financial performance and growth than SMEs that do not have a strategy that is not proven. Meanwhile, SMEs that implement a combination strategy are proven to have higher financial performance and growth than SMEs that do not have a strategy. This research was conducted by Prajogo (2007) on companies in Australia. This research analyzes the effect of differentiation strategy and cost leadership on the quality of organizational performance. The differentiation strategy is proven to have an effect on the quality of organizational performance while the cost leadership strategy is not proven. This study also found that there is a positive interaction between cost leadership strategy and differentiation strategy in predicting the quality of organizational performance. Parnell (2011) who examined retail companies in 3 countries showed that cost leadership strategies and product differentiation strategies had an effect on retail performance in America. Based on the description above, it can be concluded that the more differentiated the strategy adopted by the organization, the higher the organizational performance.

The Role of Technology Capability on the Relationship of Differentiation Strategy with Organizational Performance

Ownership of technology capabilities allows companies to create systems and processes that enable companies to share solutions to problems facing the organization, develop and implement prototypes, and incorporate and absorb knowledge about certain technologies from outside the company (Leonard & Barton 1995). Thus, companies that have technological capabilities will have better performance than companies that do not have technological capabilities. Companies that fail to have adequate technological capabilities may be faced with the fact that their products or product features do not produce commercial success.

Ellitan,(2002) found that the effectiveness of the link between technology strategy and business strategy is the main determinant of organizational performance, especially in the field of research and development. The relationship between technology policy and corporate strategy, both differentiation and cost leadership, was also identified by Ellitan (2002). They find good performance in companies that implement a differentiation strategy while simultaneously implementing aggressive technology adoption policies. Likewise, Parnel (2011) found that companies that have successful organizational performance and those organizations implement a differentiation strategy actually have high technological capabilities. Ownership of technology capabilities will increase the influence of differentiation strategy on organizational performance of an organization

The Role of Marketing Capability on the Relationship of Differentiation Strategy with Organizational Performance

The existence of marketing capabilities allows organizations to understand the immediate needs and future needs of their customers in order to provide better services and enable the acquisition of new customers. Marketing capabilities also enable organizations to effectively analyze their competitors. Thus, marketing capability is the main driver of an organization to achieve superior performance. Russel (1992) examined the factors that influence organizational performance which found that market orientation had an effect on organizational performance. Market orientation is part of marketing capabilities. Thus, research by Russell (1992) confirms the relationship between marketing capabilities and organizational performance. Organizations that have marketing capabilities will be better able to know the products and services that customers need and want so that they can differentiate products and or services appropriately. Ownership of marketing capabilities will increase the effect of differentiation strategy on performance.

The Role of Management Capability on the Relationship between Differentiation Strategy and Organizational Performance

Management capability is a manager's skill/expertise related to functional areas, namely operational/production, human resources, finance, marketing, and information systems. Parnel (2011) found that there is a positive relationship between ownership of management capabilities and organizational performance. Likewise with the research of Maes, et al. (2005) who found the influence of the characteristics of managers who are also owners of small and medium-sized companies on the company's financial performance. These results are consistent with research by Russell (1992) which found that managerial characteristics affect organizational performance because managerial characteristics can be associated with management capabilities. More or less the same results were also presented by Chinomona (2013) who found that the expertise of the manager who is also the owner has an effect on organizational performance.

From a strategic research perspective, SME Managers must have an understanding of the company (internal conditions) and the industry (external conditions) in which they operate as well as managerial skills/capabilities to develop a competitive strategy. Therefore, the managerial ability of the manager will affect the competitive strategy carried out by an organization.

Russell (1992) suggests that the decision to adopt a specific strategy depends on two things, namely the characteristics of the business environment, capabilities, aspirations, and the background of the manager who is also the owner. In other words, managers/leaders make decisions to adopt a competitive strategy by considering the existing strategic capabilities within the organization which will have an impact on higher organizational performance. Ownership of management capability will increase the influence of differentiation strategy on organizational performance of an organization.

Conclusion

The practical implication of this article is to develop knowledge and thinking of business organizations in adapting to environmental changes and developing dynamic capabilities in an effort to increase competitive advantage. Every business organization has a responsibility to ensure that when they are faced with environmental dynamism, they need to seek or get support to develop dynamic capabilities (i.e., make adjustments and if necessary make changes to their capabilities. Improvements in the ability to adapt to changes in the environment and dynamic capabilities) said to be successful if there is an increase in competitive advantage. This paper is intended to provide knowledge and understanding for organizations about the importance of efforts to plan and adjust business strategic patterns, especially differentiation strategies which are the emphasis so that the company's competitive advantage can be continuously improved.

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