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MARKET PERFORMANCE: THE EFFECT OF INTELLECTUAL CAPITAL AND INTELLECTUAL CAPITAL DISCLOSURE

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Abstract

Intellectual Capital is a concept which gives new knowledge-based resources and optimally describes the intangible assets utilized. It enables a company to run its strategies effectively and efficiently without revealing its intangible assets such as knowledge, relationships and image in the financial report. These attributes create differences and describe the company's future opportunities. The research therefore illustrated how Intellectual Capital (IC) and Intellectual Capital Disclosure (ICD) influenced the Market Performance (MP) by using the purposive sampling method. The data used is secondary which was obtained from 102 service companies listed in the Indonesian Stock Exchange (IDX) and analyzed using the multiple linear regression. The result of this research showed that both IC and ICD influenced the MP. This research indicated that the signal presented by the company through ICD minimized asymmetrical information. This proved that maximum management of the IC gave some added values capable of increasing competitive advantages.

INTRODUCTION

Wealth is often used as a benchmark to measure the success of a company, its economic change along with the implementation of knowledge, and prosperity which depends on the creation of transformation and self-capitalization (Sawarjuwono & Kadir, 2003). Shella & Wedari, (2016) stated that there is a gap between the market and company book values, which enables both investors and creditors to make inappropriate decisions due to the inability of the financial statements to reflect the actual conditions. Mukhtarudin, et al (2015) also stated that the financial statements are the final process in accounting. Its purpose is to provide information on financial position, performance, and changes. It is also an important instrument used to support the company's existence following the needs of prospective investors, creditors and other potential financial parties interested in decision-making. Therefore, it required the right information that reflected the actual conditions for the consideration of decision-makers in the company and stakeholders.

Shella & Wedari (2016) revealed that a piece of accounting information cannot be used as a basis in decision-making, rather the increasing gap between the market and book values of the company's equity in the financial market should be utilized. Therefore, financial statements which disclose only tangible assets are not good decision-making tools. Other information should be conveyed to the users of financial statements to explain the value of the company (Sawarjuwono & Kadir 2003). The difference between the market and the company book values is caused by the existence of those that are not reported in the financial statements but are more attractive to the investors. This is known as intellectual capital (IC).

In general, companies in Indonesia still utilize the traditional accounting system which emphasizes the use of tangible assets. However, this technique is not adequate in illustrating the true value of intangible assets (Oktari 2016). The International Federation of Accountants (Oktari; 2016) further stated that traditional accounting practices do not reveal knowledge-based identification and measurement. Furthermore, Sawarjuwono & Kadir (2003) said that the traditional accounting technique used as the basis for making financial statements did not provide information on IC.

The IC phenomena in Indonesia came into existence after the emergence of Statement of Financial Accounting Standard No.19 on intangible assets (non-monetary). In paragraph nine, several examples of intangible assets including knowledge and technology, design and implications of new systems, licenses, intellectual property rights, market knowledge and trademarks were identified. Due to this, companies tended to pay more attention to intangible assets as a business strategy to achieve competitive advantage and implement adequate knowledge.

The knowledge-based enterprise applications are characterized by the existence of the 2005 Indonesian Most Admired Knowledge Enterprise (MAKE) Study organized by Dunamis Consulting, an independent research institution in the field of knowledge management and IC. According to this firm, the form of recognition is given to organizations or companies that manage knowledge into superior products and services that produce more value to shareholders and interested parties (Faradina & Gayatri 2016).

During the 2016 Make Award to celebrate 12 years of its inception, companies from various industrial sectors were selected as winners. Nine organizations received this award organized by Dunamis Organizational Alignment in collaboration with Teleos from England, Adira Dinamika Multi Finance, Binus University, FIF Group, Pembangkit Jawa Bali, Petrokimia Gresik, Engineering Industry, Tigaraksa Satria, Tower Bersama Group & United Tractors. Furthermore, from the nine organizations, five bagged special recognition awards, namely Binus University, Pupuk Kaltim, Tower Bersama Group, Pembangkitan Jawa Bali and Dompet Dhuafa. These five companies were selected due to their improved knowledge of management strategy.

In 2016, the MAKE Study succeeded in developing and optimizing knowledge capable of improving a company's performance and value. The article contained in this website showed that IC has been developed in Indonesia. It is a concept that provides new knowledge-based resources and describes the intangible assets which allow companies to carry out their strategies effectively and efficiently (Faradina & Gayatri, 2016). It is a subset of intangible capital which indicates the importance of an assessment. However, to date, there are no specific regulations in Indonesia that arrange IC measurement and reports.

This research used the method revealed by Tan, et al., (2007) to measure the IC. It is divided into two categories, namely those that do not use monetary measurements and users of monetary measurements. However, this research made use of the monetary measurements based on the market book value. This method did not only include the methods that tried to estimate the IC money value but also the derivative measures using financial ratios. The market-to-book value is an external measure (Yudhanti & Shanti, 2011). The IC values are generally expressed as differences between the market and company book value from an internal perspective, especially for the current assets and were not included in the balance sheet such as knowledge, relationships and images. In terms of external perspectives, the differences in market values and book values generally describe the company's future opportunities and these items are not assessed in the Balance Sheet.

Intellectual Capital Disclosure (ICD) is a technique used by companies to convey information in the form of annual reports, statements, notes, and records. The three ICD concepts that are generally put forward are adequate, fair, and full disclosure (Faradina & Gayatri, 2016). In Indonesia, ICD is voluntary as the company discloses IC information in its profile section and analyzes the management discussions in its annual report. It combines reports in the form of numbers, which as visually and narratively communicated to internal and external stakeholders such as investors and creditors. This disclosure aims at creating value. In this study, the process of identifying ICDs was carried out in four ways using a numerical coding system developed by Guthrie et al (1999).

ICD is the amount of information disclosure presented in its annual report. It is a modification of the scheme built by Guthrie et al (1999), and a development of the definition offered by Sveiby (1997), Brennan (2001), and Ulum (2015). The modifications are made by adding several items stipulated in the Decree of the Chairperson of Bapepam and LK concerning the Submission of the Annual Report of Issuers or Public Companies (Ulum, 2015).

To create value, the company needs to utilize and develop its resources, for instance, the IC, which is knowledge with potential value. Value creation increases competitive advantage and market perception. It is believed that companies with competitive advantages can compete and survive in a dynamic business environment. This is because investors tend to appreciate those who can create sustainable value by investing more in them.

In this research, an evaluation of the company's MP influences the relationship between IC through market book value and its market performance by using Tobin's Q method developed in 1969. This method uses the calculation of the market value of equity in addition to total liabilities divided by total assets. The research on IC and ICD conducted by Soebyakto, et al. (2015) found that the firm size and profitability have a significant effect on it while the level of GCG and leverage has none. Meanwhile, Faradina & Gayatri (2016) found that IC and ICD had a positive effect on Return on Assets. While Oktari et al (2016) stated that its disclosure had a positive effect on the company value even though the impact was only seen a year or two later. Furthermore, research conducted by Jacub and Oktavia (2012) showed that IC has a positive effect on company value and ICD is the main driver for the creation of FV.

This is follow-up research by Widarjo (2011) on the influence of IC and ICD on a company's value used to conduct initial public offerings with different variable indicator sizes. The difference between this research and others is the IC measurement. This is because previous studies made use of Value Added Intellectual Capital (VAICTM). However, this research utilized the Market-to-book value method. The reason they utilized this method is due to its usage in calculating Is prepared for the public, and in managing decisions following external users. Secondly, the ICD measurements in previous studies were measured using the index Sing & Zhan (2008). However, this study utilized the four-way numeric code system developed by Guthrie et al (1999). This method not only identified the area of the ICD by measuring the quantity, and quality of expression. The ICD in the annual report is given a weight by the projection. MP was measured using the Tobin's Q method developed by Tobin (1969). This ratio can be used to determine the market value. Tobin's Q provides an overview of the fundamental aspects and the extent to which the market values from various aspects are seen by broad parties including investors. Fourth, the sample used is a service company registered at IDX from 2012-2016. The reason why the authors used a sample of service companies is that the industry requires a lot of labour to carry out its activities compared to the needs of physical assets. The company in this sector indicated that IC determined the quality of its services.

Through IC disclosure and measurement, companies have the opportunity to build trust with the stakeholders, enhance external reputation, reduce asymmetry information in the capital market, lower capital costs, and reflect the MP. It is an investor's perception of the success rate closely related to its stock price (Shella & Wedari, 2016). Based on the previously described, the purpose of this study therefore is to obtain the empirical evidence regarding the effect of IC and ICD on MP. Along with the configuration of the global economic network, there has been a paradigm shift in the dimensions of human life. It is from the old paradigm which emphasizes physical wealth that the new one which focuses on the IC values is created. Canada's Society of Management Accountants (SMAC) defined IC as an item of knowledge possessed by humans which enters into a company that produces future profits. It is also considered as knowledge with potential value if it provides benefits. Furthermore, an organization in essence cannot create knowledge of its own business.

The financial reports which focus on a company's performance are often inadequate in determining the financial performance. Accounting is believed to have the ability to recognize and measure IC. It tends to only focus on assets that are real. As a result, the value of the company is never known by the outside parties. Even the company itself is often not aware of the advantages it has because such are not easily managed or measured.

The IC concept has gained great attention from various circles, especially accountants. This phenomenon requires them to look for more detailed information relating to the management of IC. It starts by identifying and measuring the disclosure in its annual report. In this research, the IC measurement used a market-to-book value where the researchers wanted to determine the difference between the market and company book values. From an internal perspective, the differences between these two such as knowledge, relationships and images are currently not included in the balance sheet. Furthermore, in terms of external perspectives, their differences described the company's future opportunities and these items were not assessed in the financial position statement.

In addition, the authors also wanted to see IC disclosure by analyzing it from a monetary perspective, while the ICD variable was determining the information provided in the form of statements, notes, and additional disclosures of information. This disclosure can be seen in a company profile section and management discussion analysis in its annual report. The ICD identification process is carried out in four ways according to a numerical coding system developed by Guthrie et al (1999). The use of the numeric code system not only identifies the area of the ICD from the quantity aspect but also the quality of its disclosure.

The framework is a conceptual model of how theory relates to various factors identified as important problems (Sugiyono, 2010: 91). As a basis for formulating the hypothesis, the following figure described the framework that illustrated the effect of IC variables and ICD on MP.

As previously described, to create value, companies need to utilize and develop potential resources, such as IC. Sveiby (1997) provided a representative model and the underlying principles of standard theory for IC. It includes the individual competency assets and internal and external structure assets. The creation process produces value-added services capable of increasing its competitive advantage. By having a competitive advantage, the market perception of MP increases because it is believed that companies who possess it can compete and survive in a dynamic business environment. The investors give more appreciation to companies that can create sustainable values by investing larger amounts of money.

The research on IC relations has been carried out by several researchers including Jacub & Oktavia (2012) who conducted a study on it using a sample of pharmaceutical companies in Indonesia. The results of the study stated that IC had a positive influence on value. Furthermore, Shella & Wedari (2016) research also showed a positive influence between IC and MP while Widarjo (2011) found that it harms firm value. Based on the results of these studies, the first hypothesis in this study is H1: There is an influence between Intellectual Capital and Market Performance.

The companies that conducted ICD on their annual reports created value added. It provides an overall image of a company to investors because financial information alone did not adequately describe its entire wealth. The existence of an ICD can provide information to investors about a company's ability to manage its resources and create added value for the interests of stakeholders. In addition, the higher the ICD, the more the company will be assessed by investors as credible or trustworthy due to the open information disclosed in its annual report, the increase of investor confidence is believed to raise the demand for the shares and assessment.

Ulum (2015) stated that ICD is communicated to internal and external stakeholders by combining numerical reports, visualizations and narratives aimed at value creation. The voluntary disclosure of IC information will be a very effective medium for companies to convey signals of the superior quality they possess following the owner for future welfare creation (Guthrie & Petty, 2000; Whiting & Miller 2008). For those with adequate IC, voluntary disclosure distinguishes them from lower-quality companies. It is believed that educating investors on the various attributes of IC, for example, the disclosure of annual reports yields several benefits such as increasing its reputation, attracting potential investors, reducing capital costs and stock volatility, creating an understanding of products or services, and more importantly, improving relations with stakeholders (Vergauwen & Alem, 2005, Sing & Zhan, 2008).

The research conducted by Widarjo (2011) stated that ICD has a positive effect on firm value. The research by Shella & Wedari (2016) stated that it has a significant negative effect on MP. Based on the results of these studies, the second hypothesis in this research is H2: There is an influence between Intellectual Capital Disclosure on Market Performance.

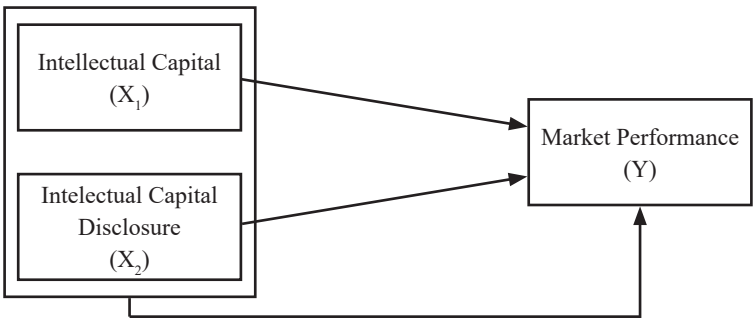

Figure 1. Research Framework

METHODS

The population of this research is a service company registered at IDX. Its services consist of the following sectors property and real estate, infrastructure, utilities and transportation, financial service and trade, as well as investment institutions. The sample is determined by using purposive sampling with the following features (a) Service Companies listed in IDX from 2012-2016, (b) Service Companies that have published financial statements in a row for 5 years 2012-2016, (c) Service Companies with net income for 5-years, and (d) the Company that presents financial summaries in rupiah. Based on the sampling technique, it can be concluded that those who meet the criteria used in this research are 102 companies.

The IC referred to in this research is measured using Market-to-book value. This aims at measuring the difference between the market value of a company and its book value. The market valuation is calculated by dividing its capitalization value by the total net assets.

The ICD comprises an index score used to bring up a number for each company. It is carried out by adding up the disclosure score divided by the cumulative score. The ICD identification process is carried out in four ways using the numerical coding system developed by Guthrie et al. (1999). This method not only identifies the extent of the ICD from the quantity aspect but also the quality of its disclosure. The disclosure of IC information in annual reports is given weight under the projections. The numeric code used is as follows: 0 = items not disclosed in the annual report; 1 = items disclosed in narrative form; 2 = items disclosed in numerical form; and 3 = items disclosed in monetary value. Furthermore, the ICD was made an index score to bring up one number for each company by summing the disclosure score divided by the cumulative score. ICDs are divided into three categories which can be seen in the table below.

Table 1. Items of ICD Components, Scale, and Cumulative Score

Category	Disclosure Item	Scale	Cumulative Score
Human Capital	Number of Employees (M)	0-2	2
	Education level	0-2	4
	Employees Qualification	0-2	6
	Employees Knowledge	0-1	7
	Employees Competence	0-1	8
	Education and Training (M)	0-2	10
	A related type of training (M)	0-2	12
	Employees Turnover	0-2	14
Structural Capital	Vision and Mission (M)	0-2	15
	Code of Ethics (M)	0-1	16
	Patent	0-2	18
	Trademarks	0-2	22
	Management Philosophy	0-1	23
	Organization Culture	0-1	23
	Management Process	0-1	25
	Information System	0-2	27
	Network System	0-2	29
	Corporate Governance (M)	0-3	32
	Violation reporting system (M)	0-1	33
	Analysis of Comprehensive Financial Performance (M)	0-3	36
	Ability to Pay Debt	0-3	39
	Capital Structure (M)	0-3	42
Relation Capital	Brand	0-1	43
	Customer	0-2	45
	Customer Loyalty	0-1	46
	Company's name	0-1	47
	Distribution Network	0-2	49
	Business Collaboration	0-1	50
	License Agreement	0-3	53
	Profitable contracts	0-3	56
	Franchise Agreement	0-2	58
	Award	0-2	60
	Certification (M)	0-1	61
	Marketing Strategy (M)	0-1	62
	Market Share (M)	0-2	64

Source: Alum et al., (2014)

The Market Performance (MP) is measured by Tobin's Q method developed by Tobin (1969). This version was modified and simplified by Chung and Pruitt (1994) on the formula made by Lindenberg and Ross (1981), and Wolfe and Sauaia (2003).

The descriptive statistics model is used to provide an overview of the characteristics of the research variables. It used the minimum value, maximum value, average value and standard deviation. This analysis was conducted to measure the strength of the relationship between IC, ICD and MP variables. The regression equation in the study is:

$$Y = a + b_1 X_1 + b_2 X_2 + e_i$$

Where Y denotes Market Performance, while a indicates constant value and b_1,...,bn are regression coefficient values. While X_1 indicates Intellectual Capital, X_2 indicates Intellectual Capital Disclosure and e_i denotes Disturbing Variables. The t-test is carried out to prove the hypothesis of the influence of IC (X_1) and ICD (X_2) on MP (Y) partially. The steps are (a) Determining the null and alternative hypothesis, (b) Determining the degrees of freedom, df = n - k, and df2 = n-k, (c) Determining the real level testing (significance) with 5% (0.05) used in this partial test.

The Simultaneous Significance Test is conducted to prove the hypothesis, namely the influence of IC (X_1) and ICD (X_2), on MP (Y). The steps carried out are: (a) Determining the null and alternative hypothesis, (b) Determining the degrees of freedom for df1 = k – 1 and df2 = n-k, (c) Determining the real level testing (significance) with 5% (0.05) used in this partial test.

This test is used to determine the best level of accuracy in the regression analysis. In this case, it is aimed at the magnitude of the coefficient of determination (R2) and used to ascertain the percentage effect of the independent variables on the dependent variable. Based on the results of the coefficient of determination (R^2), the quantity of the independent variable can explain the dependent variable, while the rest is explained by other factors outside the model.

RESULTS

Before testing the hypothesis, the value of each variable and model should be described first. From the 510 data used in this research, 20 are outliers, therefore, the total will be 490 as presented in Table 2. The IC average is 1.0176 with a standard deviation of 1.74076. The minimum value for IC is 0.00 and the maximum value is 14.42. The average ICD is 0.6449 with a standard deviation of 0.15060. The minimum value for ICD is 0.02 and the maximum value is 0.86. Furthermore, the average MP is 1.5898 with a standard deviation of 1.71521. The minimum value for MP is 0.26 and the maximum value is 14.86.

Additionally, the method of multiple linear regression analysis was used to determine the effect of the dependent and independent variables. The results obtained are shown below.

Table 2. Results of Multiple Linear Regression Test

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	.224	.044		5.027	.000		
	IC	.979	.006	.993	171.173	.000	.997	1.003
	ICD	.574	.066	.050	8.688	.000	.997	1.003

a. Dependent Variable: Market Performance

Source: Processed Data

From the results of the tests above, the regression equation can be formulated as follows:

$$MP = 0.224 + 0.979\ IC + 0.574\ ICD + e_i$$

The t-test aims at determining the presence of an effect of partial independent variables on the dependent variable. The testing of the regression results is conducted using the t-test at 95% confidence level or α = 5%. Based on the results of the t-test table, showed that the IC has a t-count value of 171,173 with a significance value of 0,000 <0,05. The IC affects MP. Therefore, the first hypothesis is accepted. Based on the table, it showed that the ICD has a count value t of 8.688 with a significance value of 0.000 <0.05 or the ICD has an effect on MP. Thus, the second hypothesis is also accepted.

The F test in principle aims at determining the effect of all independent variables simultaneously on the dependent variable. The basic test decision is taken based on significance values.

Table 3. Hypothesis Testing for F Test

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1415.086	2	707.543	14650.348	.000[b]
	Residual	23.520	487	.048		
	Total	1438.606	489			

a. Dependent Variable: Market Performance

b. Predictors: (Constant), ICD, IC

Source: Processed Data

The results of the test table showed a significance value of 0,000. Due to this, it can be concluded that all independent variables simultaneously influence the dependent variable. The coefficient of determination explains the variance of influence as a proportion of all independent and dependent variables. It can be measured by the value of R-Square or by adjusting it. In calculating its value, this research used the Adjusted R-Square. From the results of the data processed, the coefficient of determination values are as follows:

Table 4. Test of Determination Coefficient

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.992[a]	.984	.984	.21976	1.504

a. Predictors: (Constant), ICD, IC

b. Dependent Variable: Market Performance

Source: Processed Data

The results of the coefficient of determination analysis indicate that the adjusted R2 value is 0.984 (98.4%). This showed that the dependent variable (MP) can be explained by 98.4% of independent variables namely IC and ICD. While the remaining 1.6% is explained by other variables outside this research.

DISCUSSION

The results showed that IC as measured by Market to Book Value affected MP. In the first hypothesis testing, the value of the β1 coefficient = 0.979. It indicates that if the IC rises by one unit then the company's MP increases by 0.979. Therefore an increase in IC number raises the value of the company's MP. This research indicates that the market gives a higher value to companies with high IC. The influence of IC on MP is per RBT where the maximum management of IC creates value added capable of increasing competitive advantage. The value added is the result of the value creation process in the market. Shella & Wedari (2016) explained that to develop a competitive advantage, companies must have superior resources and capabilities or exceed their competitors. The effective and efficient use of IC contributes significantly to achieving a competitive advantage. This increases the market perception of MP for it is believed that companies that have competitive advantages can compete and survive in a dynamic business environment. The investors give more appreciation to companies able to create sustainable values by investing larger amounts of money. This affects the increasing demand for its shares which ultimately increases the MP.

This research also supported the stakeholder theory which stated that individuals, groups or organisations either in whole or in part that have power, interests and face risks due to company activities either directly or indirectly (Kusuma, 2015). It explained how to maintain relationships that include workers, communities, suppliers, investors and creditors. The relationships between the company and the parties involved must be properly managed for mutual influence and to seek profit. A company with good IC will have its financial performance increase the stakeholders' trust thereby, prompting them to invest. The company maximizes the use of its assets to encourage the quality of employees, therefore, it has to increase profits. The results of this research are consistent with the research by Shella & Wedari (2016), Chariri & Prasetyanto (2013), Jacub and Oktavia (2012) which stated that IC had a positive effect on MP.

The results showed that ICD had a positive effect on MP. In testing the second hypothesis, the coefficient value β2 = 0.574 shows that if the number of ICDs increases by one unit, then MP increases by 0.574. It indicates that the higher the ICD, the higher the MP after the initial public offering. This indicates that investors capture the signals given by companies through ICD and the use of information in analyzing and making investment decisions. This research indicated that the signals conveyed by the companies through ICD reduce the information asymmetry. The more items in ICD that are disclosed in the annual report (human, structural, and relational capital), it turns out it makes it easier for the prospective investors to know the prospects and overall performance. They give a higher rating to companies that increase the ICD.

The acceptance of the second hypothesis is influenced by the successful delivery of the company's positive signals to the investors through the expansion of the ICD under the signalling theory. The information about ICD is expected to provide a positive signal for investors. According to this research, the appropriate results that the high ICD gives to companies provide a positive signal for investors. The information disclosed will be beneficial to the company. The existence of detailed disclosures about company information acquaints investors with the advantages possessed by the company. The knowledge of company excellence has a positive impact on MP, where the investors can add to their investment funds. An increase in the level of investment leads to a rise in the company's MP. The results of this research are consistent with the research conducted by Widarjo (2011) and Jacub and Oktavia (2012) which stated that ICD has a positive effect on firm values.

CONCLUSIONS

This is empirical research that aims at determining the effect of independent variables on the dependent. The independent variables used are IC and ICD, while the dependent tested is MP. This research has obtained 510 observation data with 20 data including outliers. Therefore, only 490 data can be processed, with the data used extracted from the official website of the Indonesia Stock Exchange from 2012-2016. The test in this research used the multiple linear regression analysis. Before testing the hypotheses, a descriptive analysis was carried out to have a general overview of the data obtained and a classic assumption test was conducted to ensure that the research model used had fulfilled the basic requirements in the multiple linear regression.

The test results from the first hypothesis gave the results that followed the hypothesis stated. It is where IC has a significant effect and can provide added value or increase MP. Furthermore, testing the second hypothesis gave the same results as the first. Therefore, the second hypothesis is accepted. Moreover, ICD has a positive and significant effect on MP. The research has several limitations that require improvement and development. Thus, the limitations in this research are found in the following points (1) The independent variables are only limited to two variables, namely IC and ICD, (2) This research is only limited to service companies listed on IDX, and (3) The research year is relatively short that the company is not necessarily able to describe the actual situation of the MP.

There are some suggestions to be conducted in future in the following points (1) The research considered adding variables, (2) The future studies are expected to consider changing the size of the IC variable indicator, using the VAICTM, (3) In addition, it is expected that further research can be conducted outside the service companies. Therefore they described the condition of the company in Indonesia as a whole, and (4) Using a longer observation will be able to analyze the patterns of relationships between variables over a longer period and produce stronger research results.

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