Analysis of Cost Leadership Strategy and Differentiation Strategy in Creating Competitive Advantages and their Impact on Performance

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Abstract: One of the determinants of business success that must be considered by business owners or managers, especially in facing business competition is to create competitive advantage. The competitive advantage of a company is determined by the company's ability to create value or benefit from the product or service felt by the buyer in excess of the cost incurred by the company to create it. There are two main strategies that can create competitive advantage is the strategy of Cost Leadership and Differentiation strategy. This study aims to analyze the role of Cost Leadership strategy and Differentiation strategy to create competitive advantage in facing business competition and with competitive advantage possessed able to improve business performance. The research object is Micro, Small, Medium Enterprises (MSMEs) of woven ikat handicraft in West Southeast Maluku Regency, Maluku Province. The samples were taken from 74 respondents, owners and managers spread in 91 units of woven ikat handicrafts business in 3 (three) subdistricts of South Taninbar Subdistrict, Wertamタンalan Subdistrict, and Wermaktian Subdistrict, as an affordable population in this research. Data collection is done by direct survey method with questionnaire instrument. The analysis was done by using PLS-SEM method with SmartPLS 2.0 software. The result of the research confirms that small-scale woven ikat handicraft business in West Southeast Maluku district build their competitive advantage by using Differentiation strategy more than the Cost Leadership strategy. The result of the research shows the performance resulted from the effort to build the competitive advantage in the Differentiation strategy has increased for the last 3 years.

Keywords: cost leadership strategy, Differentiation strategy, competitive advantage, performance, business, micro and small business

1. Introduction

The national economic development cannot be separated from the strategic role of Micro, Small, Medium Enterprises (MSMEs) as a driver of economic growth and employment. In addition, MSMEs also have a role in the distribution of development results. Competitive advantage is defined as a company that develops in a unique position compared to its competitors. (Bamberger in Cater and Pucko 2005), Day and Wensley (1988) also argue that competitive advantage is a form of strategy to help the company maintain its survival. Similarly, Ferdinand (2003) points out that in a competitive market, the ability of a firm to produce performance depends heavily on the degree of competitive advantage. Competitive advantage is the company's strategy to achieve the ultimate goal but is a means to achieve the ultimate goal of the company, which is to improve the company's performance. Seeing the magnitude of the influence of MSMEs in driving economic growth (Ariani, 2013, Supriyanto, 2006; Tambunan, 2003) then the improvement of MSMEs performance is expected. Along with the increasing performance of UMKM will have a positive impact on the improvement of economic performance and growth rate of a nation (Tambunan, 2003).

As a response, the Province of Maluku as part of the Unitary State of the Republic of Indonesia (NKRI) continues to move with an active role to support the government's integrated programs by increasing welfare and growth economic areas. One of the ways is by supporting the growth of business sectors, especially micro and small businesses that touch the joints of people's lives. The policy is as a responsibility form in the effort of improving national competitiveness in order to encourage the growth of the national economy.

The number of MSMEs in Maluku Province as many as 31,188 spread throughout the district / city and 6,719 units of which are in the District of West Southeast Maluku with 5,972 units of micro businesses and 747 units of small businesses without medium-scale business in the area. (Department of Cooperatives, Small and Medium Enterprises, Maluku Province, 2015). One of the mainstay of the area is the business of woven ikat handicraft. Woven ikat handicraft in West Southeast Maluku Regency is the nation's cultural heritage, which since hundreds of years ago has become an important part of the civilization of the people of Southeast Maluku especially in West Southeast Maluku which its existence must be preserved. Woven ikat fabric used to be only as daily traditional clothing by the people of West Southeast Maluku Regency and as the purposes of traditional ceremonies because the fabric has its own sacred value for the community in the District of West Southeast Maluku. However, since tens of years ago they have begun to see the commercial opportunities of the woven fabric by selling the fabric they produce to meet their economic needs but It has not been able to lift most of the people there from the poverty line. According to data of Central Bureau of Statistics in 2013, West Southeast Maluku Regency is the...
poorest district in Maluku Province with the percentage of poverty rate of 29.75% followed by Southwest Maluku Regency in second rank with 29.25% and Aru Islands District with a percentage of 27.34% third ranked.

This poverty is an important note for West Southeast Maluku District Government whose territorial waters are directly adjacent to Australia and Timor Leste to be able to overcome them. Therefore, the government made various efforts. One of them is by continually encourage the growth of Micro, Small and Medium Enterprises (MSMEs) especially to the business of woven ikat handicraft.

**Woven ikat** from West Southeast Maluku regency or well known with the name ikat Tanimbar, has the opportunity and the potential to be developed. Various products either fashion products or other products made from *ikat* such as; shoes, handbags, shawls, ties, scarves, pendants, hair clips, hats, tablecloths, pillowcases for chairs, frames, tissue coverings, cover cases, furniture upholstery, or interior decorators etc. in terms of quality and beauty.

To create and develop competitive advantage, create a sustainable and profitable position in an industry, Porter (1992) proposes competitive strategies that are (1) Cost Leadership, (2) Differentiation and (3) Focus. This competing strategy aims to build a favorable and sustainable position against the decisive forces in industrial competition. Therefore, in order to win the MSMEs industry competition, it is necessary to have a clear and precise competitive strategy in order to have a better performance in the face of increasingly fierce competition.

For this study, the authors only limit the strategy of Cost Leadership and Differentiation Strategy without looking at the use of focus strategy. It is caused the information that the writer got through observation in the field revealed that *woven ikat* business does not restrict its business only by producing cloth used for certain custom or ceremonial events or just purchased and used by certain circles. The business has grown by adding its product line by creating casual fashion products as well as various other products made from typical *ikat* cloth of West Southeast Maluku Regency such as women and men clothing, bags, shoes, wallets, hats, fans, and tissue boxes and others at a cheaper price that is affordable to all levels of society.

A company that implements a Cost Leadership Strategy will achieve competitive advantage by being the lowest cost manufacturer or service provider in the industry. The Cost Leadership Strategy requires aggressive construction of efficient facility scale, aggressive efforts to achieve cost reduction due to experience, cost control and tight overhead, avoiding marginal customers and minimizing costs in areas such as research and development, service, sales force, advertising and etc.

Companies with Differentiation strategy can create something new that the whole industry perceives as unique. Approaches in Differentiation can be various forms such as brand, technology, special characteristics, customer service, distribution network (distributor) or other dimensions.

Pelham (2000) also reported that Differentiation strategy for MSMEs markets have a greater impact on profits than cost-benefit strategies, while Dess and Davis (1984) in Leitner and Guldenberg (2010) found that cost-benefit strategies have a higher return on assets than Differentiation.

Carter and Pucko (2005) reported that all forms of competitive advantage by both Cost Leadership and Differentiation have a positive effect on all performance indicators especially for financial indicators. Each competitive advantage in both Cost Leadership and Differentiation has a different effect on the company's performance (Gemnaife et al, 2018). However, based on the research findings, Differentiation strategy has influence that is more significant to most of the company's performance indicators.

### 2. The Research Problem

Based on the explanation presented above, the formulation of the problem with regard to the woven ikat crafts industry is as follows 1). Does the strategy of Cost Leadership have a positive and significant impact on competitive advantage?, 2) Does the Differentiation strategy have a positive and significant impact on competitive advantage?, 3) Does the Cost Leadership Strategy have a positive and significant impact on business performance?, 4) Does the Differentiation Strategy have a positive and significant impact on business performance?, 5) Does competitive advantage have a positive and significant impact on business performance ?, 6) Does the Cost Leadership Strategy have a positive and significant impact on business performance through competitive advantage ?, 7) Does the Differentiation Strategy have a positive and significant impact on business performance through competitive advantage ?.

### 3. Literature Review

The Cost Leadership Strategy is an attempt by the company to produce competitive advantage by achieving the lowest cost in its industry (Porter, 1992). The focus of the company to apply the Cost Leadership strategy is to tight cost control and efficiency in all areas of operation. Having a low cost position will make the company get above-average earnings results in its industry despite the enormous competition power.

In a Differentiation Strategy, the company strives to be unique in its industry in a number of particular dimensions that buyers generally value. The company chooses one or more attributes that many buyers in the industry consider important, and puts itself uniquely to meet this need. Due to its unique (distinctive) position, the company feels it deserves to place a premium price. (Porter, 1985)

According to Bamberger cited in Cater and Pucko (2005), a competitive advantage can be defined as a company that develops in a unique position compared to its competitors. Furthermore, Porter (1985), Competitive advantage grows from the values and benefits that the company can create for its buyers beyond the cost of the company to create it.
Buyers will be willing to pay for these more value and benefits. The superior value comes from offering the lowest price compared to the competitor's price for an equivalent benefit or with a unique benefit offering that exceeds the offered price.

According Wibowo (2008), performance is the result of work or work performance. But performance is not only meaningful as a result of work, but how the process takes place a job. Another opinion of Armstrong and Baron in Wibowo (2008) is performance is the result of work related to organizational strategic goals, customer satisfaction, and contribute to the economy.

Micro, Small and Medium Enterprises (MSMEs) are the largest business group and can strengthen the national economy. MSMEs also proved resilient to various economic crisis shocks, so it needs an effort to enlarge and promote micro, small and medium enterprise groups through appropriate policies, regulations and strategies. Business criteria that are included in Small and Medium Micro Enterprises have been regulated in law.

MSMEs according to law Number 20 of 2008, as stated in article 1 as follows,
1) Micro Enterprises is productive economic enterprises owned by individual and / or business entities that meet the criteria of Micro Enterprises as stipulated in this Law.
2) Small-scale business is a stand-alone productive economic enterprise, conducted by an individual or a business entity that is not a subsidiary or not a branch of a company owned, controlled or part of, directly or indirectly from a Medium-sized Business or Large Enterprise meet the criteria of Small Business as referred to in this Law.
3) Medium Business is a stand-alone productive economic enterprise undertaken by an individual or a business entity not being a subsidiary or branch of a company owned, controlled or part of either directly or indirectly with a Small or Large Business with a net worth or annual sales proceeds as provided in this Law.

According C.W. Hofer & W.R. Sandberg (in Wheelen and Hunger, 2002), in accordance with the level of influence there are three factors that affect MSMEs performance, especially for new business, namely:
1) **Industrial structure.**
Characteristics of industrial products have a direct influence on the success of new companies. First, the new company will be more successful when it enters a heterogeneous industry than a homogeneous one. Heterogeneous industries make new companies differentiate their products from competing products with unique products and focus on market segments that have unique needs. Second, according to the data, the new company will be more successful if its product is a relatively unimportant product to the total purchase needs of consumers than if the product is important.

2) **Business Strategy**
The key to success for most new companies is: (a). differentiating products from competitors' products in terms of quality and service, and (b). focusing the product on the needs of the consumer in the market segment entered to gain a niche market (Porter's competitive Differentiation strategy).

3) **Entrepreneurial Characteristics**
Four behavioral factors affect the success of new companies, namely: (a). Successful entrepreneurs are usually better at identifying potential business opportunities than others. The important thing is that they focus more on the opportunity aspect, not on the issue, and always learn from the failures. (b). Successful entrepreneurs usually have a sense of urgency that makes them having orientation on action. High need for achievement that motivates them to develop ideas into action (c). Successful entrepreneurs have knowledge of the key factors needed to succeed in the industry and the physical stamina necessary for their work (d). Successful entrepreneurs will develop relationships with outside parties to complement their skills, knowledge and abilities.

**Conceptual Framework of Research and Hypotheses**
MSMEs has an important role in woven ikat handicraft. It is as one of the driving forces of growth and economic development in West Southeast Maluku Regency especially on the economic improvement of the community. It needs special attention from the government and society, especially businessmen so that this business can continue to survive and develop in the face of increasingly tight competition today.

![Conceptual Framework of Research Model](image-url)

**Figure: Conceptual Framework of Research Model**

| H1 | Cost Leadership strategy has a positive influence on competitive advantage |
| H2 | Differentiation Strategy has a positive influence on Competitive Advantage |
| H3 | Cost Leadership strategy has a positive effect on MSMEs performance |
| H4 | Competitive advantage has a positive effect on MSMEs performance. |
| H5 | Competitive advantage has a positive effect on MSMEs performance. |
| H6 | Cost Leadership strategy has a positive effect on MSMEs performance through competitive advantage |
| H7 | Differentiation strategies have a positive effect on MSMEs performance through competitive advantage |
4. Methods

This type of research used survey research method with quantitative research approach. Survey research is a quantitative study using the same structured question on everyone, then all the answers obtained by the researcher are recorded, processed, and analyzed. Such structured questions are called questionnaires.

This research was conducted on the business of woven ikat in West Maluku Regency. The object of research in this research is 126 units of woven ikat handicraft business in Regency of West Southeast Maluku. The sampling technique used in this research is Simple Random Sampling is the simplest and easiest sample selection technique. Data obtained from the results of research and then processed using data analysis techniques namely Partial Least Square (PLS).

5. Result and Discussion

Hypothesis Testing H1
The H1 hypothesis states that the Cost Leadership Strategy has a positive and significant impact on competitive advantage. The result of t-test on path coefficient on this relationship is 0.745 with positive signified coefficient but its influence is not significant (p-value = 0.069), so it can be concluded that H1 is rejected.

Hypothesis Testing H2
H2 hypothesis states that Differentiation strategy has a positive and significant influence on competitive advantage. The result of t-test on path coefficient on this relationship is 1.266 is significant (p-value = 0.005), so it can be concluded that H2 is accepted.

Hypothesis Testing H3
H3 hypothesis states that Cost Leadership Strategy has a positive and significant impact on Business Performance. The result of t-test on path coefficient in this relationship is 0.12 with positive signified coefficient but its influence is not significant (p-value = 0.705), so it can be concluded that H3 is rejected.

Hypothesis Testing H4
H4 hypothesis states that Differentiation Strategy has a positive and significant influence on Business Performance. The result of t-test on path coefficient in this relationship is 0.156 with positive signified coefficient but its influence is not significant (p-value = 0.665), so it can be concluded that H4 is rejected.

Hypothesis Testing H5
H5 hypothesis states that the competitive advantage (X1) has a positive and significant influence on business performance (Y). The result of t-test on path coefficient in this relationship is 0.75 is significant (p-value = 0.000), so it can be concluded that H5 is accepted.

Hypothesis Testing H6
Hypothesis H6 states that the Cost Leadership Strategy has a significant influence on business performance through competitive advantage. The result of t-test on path coefficient on the relationship of indirect influence between Cost Leadership Strategy (X1) on Business Performance (Y) through Competitive Advantage (X3) is 0.55875. While the Direct Influence Strategy of Cost Leadership to Competitive Advantage is not significant on coefficient of 0.745, and Direct Influence of Competitive Advantage to Business Performance has significant effect on coefficient of 0.75 it can be concluded there is no significant indirect influence between the Cost Leadership Strategy (X1) on Performance Business (Y) through Competitive Advantage (X3). From these results it is concluded that H6 is rejected.

Hypothesis Testing H7
Hypothesis H7 states that Differentiation Strategy has a significant influence on Business Performance through Competitive Advantage. The result of t-test on path coefficient on the relationship of indirect influence between Differentiation Strategy (X2) on Business Performance (Y) through Competitive Advantage (X3) is 0.9495. While Direct Influence Diferensiasi Strategy to Competitive Advantage significantly on the coefficient of 1.266 and the Direct Influence of Competitive Advantage to Business Performance has a significant influence on the coefficient of 0.75 it can be concluded there is a significant indirect influence between the Cost Leadership Strategy (X1) on Business Performance (Y) through Competitive Advantage (X3). From these results it is concluded that H7 is accepted.

The Influence of Cost Leadership Strategies on Competitive Advantages

The result of data analysis shows that Cost Leadership Strategy has positive but not significant influence to competitive advantage. This means that the Cost Leadership Strategy cannot afford to create competitive advantage. This result differs from previous research conducted by Yamin S., et al. (1997) which shows that the Cost Leadership Strategy significantly impacts on competitive advantage. This can happen because of the characteristics of small-scale business with little capital, which is classified into a handicraft business that minimal labor and rely on simple equipment in the production process, so that with these conditions will make it difficult if you want to offer various products or develop various product lines and innovate in the process production. In addition, due to infrastructure constraints and difficult geographic location for the distribution of raw materials, the procurement of low-cost raw materials will be very difficult, resulting in the cost of production becoming expensive so that efficiency is difficult to achieve. If that happens then of course the price offered will be high. This is why the Cost Leadership Strategy does not significantly affect the competitive advantage in the woven ikat business in West Southeast Maluku regency.

The Influence of Differentiation Strategies to The Competitive Advantage

The result of data analysis shows that Differentiation strategy have positive and significant effect to competitive advantage. This means that by increasing efforts in Differentiation...
strategy, woven ikat business will be able to create competitive advantage. The results of this study support Lestari’s research (2005), that product Differentiation, service Differentiation and image Differentiation shows a positive and significant impact on competitive advantage. Mintzberg, 1988; Dean and Evans 1994 in Amoako-Gyampah and Acquaah, 2008 in his research also found that pursuing a Differentiation strategy helps companies avoid potential price competition because of their ability to offer products with greater reliability, greater durability, greater features and aesthetics, as well as superior performance.

Influence of Cost Leadership Strategy to Business Performance

The result of the research shows that Cost Leadership Strategy has positive but not significant influence to Business Performance. This means that the Cost Leadership Strategy is not able to improve the performance of woven ikat business. This result differs from previous research conducted by Doss and Davis (1984) in Leitner and Guldenberg (2010), finding that Low Cost Leadership strategy has higher return on assets (ROAs) than differentiators do.

The Influence of Differentiation Strategies on Business Performance

The result of research shows that Differentiation strategy has positive but not significant influence to Business Performance. This means that direct Differentiation strategy that is implemented cannot improve the performance of woven ikat business. This result differs from previous research conducted by Pelham (2000) who reported that for SMEs, Differentiation strategies have a greater impact on the advantages of cost leadership strategies.

The Effect of Competitive Advantage on Business Performance

The results showed competitive advantage positively and significantly to business performance. This means that increasing competitiveness will give more impact to the performance improvement of woven ikat business. These results support Carter and Pucko’s (2005) study finding that all forms of competitive advantage by both Cost Leadership and Differentiation have a positive effect on all performance indicators especially for financial indicators. However, the competitive advantage in Differentiation has more significant effect on performance than Cost Leadership.

Lestari (2005) also showed that competitive advantage in product Differentiation, service Differentiation and image Differentiation showed a positive effect on marketing performance improvement.

The Effect of Cost Leadership Strategy on Business Performance Through Competitive Advantage

The results showed no significant indirect effect between the Strategy of Cost Leadership to Business Performance through Competitive Advantage. This means that the Competitive Cost Leadership Strategy is not able to create competitive advantage and does not affect the improvement of business performance of woven ikat. This is in contrast to the findings of Yamin, Mavond, Gunasekaran, and Sarros, (1997) that overall, business performance is closely related to low cost strategies through competitive advantage achieved. These results are also different from Powers and Hahn (2004), that the results of his research indicate a relationship between generic strategies and the concept of competitive advantage and that the Cost Leadership Strategy has significant relationship and influence on the performance of the “stuck in the middle” company.

The Influence of Differentiation Strategies on Business Performance Through Competitive Advantage

The result of the research shows that there is a significant indirect influence between Differentiation Strategy on Business Performance through Competitive Advantage. This means that increasing the Differentiation strategy will increase the competitive advantage owned. Moreover, it will be able to give impact to the increasing performance of woven ikat business.

These results support the Lestari (2005) study, which shows that Differentiation strategies have a positive and significant impact on competitive advantage that indicates an increase in marketing performance. Similarly, Carter and Pucko (2005) found that Differentiation strategies have impact that is more significant on performance than Cost Leadership through competitive advantage.

6. Conclusions and Recommendations

6.1 Conclusion

Based on the results of the analysis conducted, it can be concluded as follows. First, Cost Leadership strategy has positive but insignificant effect on competitive advantage. Second, Differentiation Strategy have positive and significant impact to competitive advantage. Third, Cost Leadership Strategy have positive but not significant influence to Business Performance. Fourth, Differentiation Strategy have positive but not significant effect to Business Performance, Fifth, Competitive Advantages have a positive and significant impact on Business Performance. Sixth, Cost Leadership Strategy has no significant effect to Business Performance through Competitive Advantage. The last, Differentiation Strategy has significant effect to Business Performance through Competitive Advantage.

6.2 Suggestion

Based on the results of the research and conclusion, it can be stated the following suggestions. For the owners of MSMEs in Indonesia, especially the woven ikat business in West Southeast Maluku Regency, the results of this study are expected to be a reference in choosing a strategy to compete appropriately with the situation and business conditions and the market faced. They can choose Differentiation strategy because it is able to create competitive advantage and can give the highest contribution on business performance. For institutions related to MSMEs, the results of this study can be used as a reference for the development of MSMEs, especially on the right competitive strategy for business growth and improvement of business performance of woven ikat.
ikat. Similarly, in terms of training and capital assistance either in the form of loans and grant to be consistently done until small micro businesses can be independent.

References


