UNIVERSITI TEKNOLOGI MARA

FIRMS' FINANCIAL PERFORMANCE FROM INTELLECTUAL CAPITAL AND CAPITAL STRUCTURE PERSPECTIVES: A COMPARATIVE ANALYSIS INTO THREE INDUSTRIES IN MALAYSIA

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ABSTRACT

The world's economy has changed from an industrial economy, in which economic growth was determined by the employment of physical resources, towards a knowledge-based economy in which wealth creation is associated with the development and maintenance of intangible resources particularly knowledge to create competitive advantages. The transition towards a knowledge-based economy is changing the business model and firms operating in the knowledge-based economy require interaction with their environment in order to sustain their business. Since knowledge is a source of competitive advantage, therefore, firms must employ a mechanism to identify, measure and manage it. Knowledge in firms is embedded in their employees, structural design, interaction with their environment and collectively they are referred to as intellectual capital. Due to the importance of intellectual capital capabilities as a driver of growth, more studies involving multiple industries and a model that can better reflect and measure the components of intellectual capital such as MVAIC are required. Meanwhile, capital structure decision as to how do firms choose their capital structure to finance their operations and how does the choice of capital structure financing affect the financial performance of the firm will also be examined in this study and to investigate the role of firm size in moderating the above relationships.To analyse the relationship between independent variables, dependent variable and moderating variable in this study, static panel data procedures were employed. The empirical findings revealed that intellectual capital has a positive and significant association with financial performance of firms in construction and finance. However, no association is found in plantation. As for capital structure and financial performance, it is noted that the findings exhibited significant differences among industries. In construction, long-term debt is positive and significantly associated with ROE. In finance, total debt has a positive and significant relationship with ROE. Whereas in plantation there is a positive relationship between short-term debt and profitability (ROA and ROE). In relation to firm size as a moderator, the result shows a positive moderator effect of firm size on the relationship between intellectual capital and financial performance specifically in construction. The finding suggests that firms' value creation capability increases with firms' size, thus larger firms' are in a better position to generate profit.

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CHAPTER ONE
INTRODUCTION

1.1 Background of Study

Firms resources, according to Edvinsson and Malone (1997) through Skandia Navigator, can be grouped into two categories, financial capital which is tangible in nature and intellectual capital which is intangible resources. Thus, firms have a bundle of resources which are both tangible and intangible. These resources are employed to create value and improve firms' financial performance.

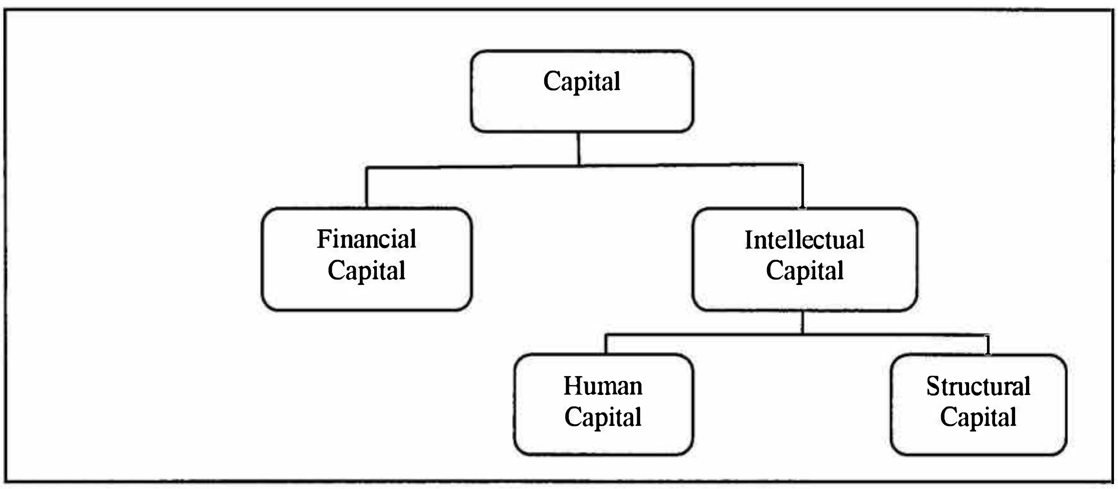

Figure 1.1 Skandia Navigator

Source: Edvinsson and Malone (1997) Intellectual Capital: Realizing your Company's True Value by Finding Its Hidden Brainpower. Harper Collins Publishers, New York, NY.

Apart form the resources available, firms' financial performance are greatly influenced by the country's economy. The Malaysia economy has recorded an average 7 per cent growth over the last three decades (Goh, 2005) and it has undergone substantial changes over the years. The country's economic development can be divided into three phases, phase 1 from 1957 to 1969, phase 2 from 1970 to 1990 and phase 3 from 1991 onwards (Fadhlin, Chai, Kharul and Tan, 2004). Through out the three phases, government had embarked on various economic policies to ensure economic growth and development. These economic policies basically relied on the