

# Research on the Relationship Between Strategic Difference Degree and Innovation Performance

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## ABSTRACT

In the era of knowledge economy, the marginal contribution of knowledge to innovation exceeds that of traditional material production factors. The advantage of technological innovation of enterprises is more due to the change of managers' cognition, rather than determined by heterogeneous resources. Innovation is the key driving force to achieve sustainable competitive advantage, and strategic choice is one of the important factors affecting innovation performance. This paper aims to explore the mechanism of the impact of strategic variance on innovation performance, enrich the research on the impact of strategic variance on innovation performance, and provide countermeasures and suggestions for enterprises to realize transformation and upgrading through strategic planning and make full use of financial advantages to improve innovation performance.

## KEYWORDS

Strategic difference degree; Innovation performance; Financial flexibility

## 1. INTRODUCTION

In the ever-changing market environment, innovation has become the fundamental driving force for the survival and development of enterprises. Only by continuously improving innovation ability can enterprises maintain core competitive advantage in the fierce market competition. However, the current global economic landscape is changing dramatically, and the impact of the COVID-19 pandemic has intensified this trend. In response to the great changes in the external environment, China has put forward a new development pattern of "double cycle". This requires enterprises to take the initiative to adjust their strategies and actively promote transformation and upgrading. According to the theory of strategic balance, in the process of internal resource integration and reshaping, enterprises should appropriately maintain the strategic differences with the industry in order to stimulate the power of innovation.

However, excessive strategic differentiation may also lead to a series of problems, such as the increase of operational risks and the intensification of information asymmetry, which will further affect the quality of accounting information and financing channels, and ultimately hinder the realization of innovation performance. Therefore, companies need to find a balance between differentiation and integration, while focusing on the moderating role of key financial factors in this relationship. Only by deeply exploring how the degree of strategic difference affects innovation performance can enterprises find the appropriate strategic positioning under the new development pattern, give full play to the impetus of innovation, and achieve sustainable competitive advantage [1]. This is not only conducive to the development of enterprises themselves, but also conducive to the high-quality transformation of China's economy.

## **2. DEFINITION OF RELEVANT CONCEPTS**

### **2.1. Degree of Strategic Difference**

In his research, Ye Kangtao Outlines the strategic model of the enterprise through six key aspects: marketing behavior, innovation consciousness, production capacity, expansion state, management level and capital management. To some extent, the marketing behavior reflects the target market selection of the enterprise and the sales status of the product in the current market. The innovation consciousness, production capacity and expansion state can partly reflect the training direction of the enterprise's future core competitiveness and the future development prospect direction of the enterprise. The management level and capital management status of the enterprise may show the path of the enterprise to achieve its strategic goals. Generally speaking, the greater the degree of strategic difference, the more the enterprise strategy deviates from the conventional strategy of the industry.

### **2.2. Financing Constraints**

According to modern financing theory, financing constraint refers to the financing predicament that enterprises encounter when they have to seek external financing due to lack of their own funds when facing investment opportunities in the course of operation. On the one hand, the imperfect development of the financial market leads to financing friction in the process of financing, that is, the low efficiency of financing; on the other hand, the enterprises themselves may be in different development stages, such as the start-up and growth stages of smes [2]. Short operating history and lack of sufficient collateral assets lead to financial institutions being in risk aversion and reluctant to lend to them. The realistic dilemma ultimately caused by such financing constraints is that it is difficult, expensive and slow for enterprises to obtain financing, which inhibits them from taking advantage of investment opportunities for long-term healthy development, and even loses the right to future development, which ultimately brings adverse effects on social and economic growth and the improvement of residents' welfare.

### **2.3. Financial Flexibility**

Financial flexibility is the ability of an enterprise to deal with the whole financial system and the internal and external financial environment risks through flexible processing of financial decision-making activities to ensure that the financial system can deal with financial management activities accurately and efficiently.

### **2.4. Innovation Performance**

Enterprise innovation performance is the result of enterprise innovation behavior and enterprise innovation process, emphasizing the generation, adoption and implementation of novel ideas and processes and the results produced. At present, one of the main models of innovation performance measurement is input-output model. The innovation performance evaluation of input-output model originated from Rozberg, who believed that the focus of innovation performance evaluation was efficiency, so he chose the intuitive input-output ratio as the evaluation criterion. The standard considers R&D input and non-R&D input as innovation input. New products, patents as output. On this basis, an innovation measurement and evaluation system based on input and output is designed.

### **3. RELATIONSHIP ANALYSIS**

#### **3.1. Strategic Variance and Innovation Performance**

According to the theory of strategic management, strategy is the overall, long-term and overall planning of an enterprise, which determines the survival and development of an enterprise. Different strategic choices often produce different innovation results. The degree of strategic deviation represents the difference in understanding of the mainstream trend of the industry and the advantage of internal resources, which will inevitably affect the innovation behavior, innovation mode and innovation performance [3].

First, enterprises with large strategic differences have greater difficulty in obtaining innovation funds. In terms of external financing, enterprises with large strategic differences have lower transparency of accounting information, less relevance of accounting information, more difficult to predict actual operating conditions, and more difficult to detect earnings manipulation. This will lead to problems such as high operational uncertainty and information asymmetry, and increase the rate of return required by external investors, thus increasing the difficulty and cost of external financing. In terms of internal funds, the greater the degree of strategic difference, the higher the operational uncertainty. Enterprises need to use internal funds to prevent potential financial risks, operate unique business models or explore new markets. Limited internal funds are more likely to be occupied by daily operations, which has a crowding out effect on innovation capital investment. At the same time, based on the input-output theory, enterprise innovation is an activity with high input and uncertain income, and the input and consumption of innovative personnel and funds are the basis and prerequisite for enterprises to achieve good innovation performance. Therefore, a large degree of strategic difference is not conducive to the acquisition and investment of innovation funds, and thus inhibits innovation performance.

#### **3.2. Degree of Strategic Variance and Financial Flexibility**

With the increase of strategic differences, the degree of information asymmetry inside and outside the enterprise will increase. On the one hand, because the strategy itself is important non-financial information that transmits corporate value signals, many stakeholders pay attention to it, including analysts' earnings forecasts, auditors' attitudes toward risk, and potential investors' investment choices. When the degree of corporate strategy heterogeneity is high, its connotation information is difficult to be understood by external stakeholders. At this time, investors can neither measure enterprise value through simple financial indicators, nor can they obtain more reliable and effective forecasting information from analyst forecasts. The difficulty of information acquisition for investors is greatly increased, thus increasing the degree of information asymmetry. On the other hand, enterprises with a high degree of strategic difference have a stronger motivation to carry out accrual earnings management activities, and enterprises have a stronger motivation to rely on accounting estimates and other means to distort real performance, which further increases the degree of internal and external information asymmetry. Therefore, because of the high degree of information asymmetry, enterprises with large strategic differences will face higher transaction costs, such as higher financing costs. Therefore, when enterprises choose strategies that differ greatly from those in the same industry, they will inevitably face higher financing constraints in the future. In order to ensure the smooth implementation of the strategy and avoid project failure due to financing difficulties caused by increasing information asymmetry in business activities, enterprises will reserve financial flexibility in advance to ensure necessary financial support.

From an investment perspective, companies with strategic heterogeneity may be more aggressive, preferring internal development or external mergers and acquisitions. Compared with conservative strategy, radical strategy will increase cash gap and strong financing demand in the future period of time. The reserve financial flexibility with "investment motivation" can precisely meet this

investment demand, and improve the future performance of enterprises, so as to maximize the value of enterprises [4]. As a result, firms reserve financial flexibility to seize future investment opportunities.

### **3.3. Financial Flexibility and Innovation Performance**

Maintaining the financial flexibility of the manufacturing industry can not only adapt to the future liquidity requirements of the market, but also improve the stable source of funds for enterprises and improve the level of research investment, thus ensuring the stable development of technological innovation activities. Many studies have shown that obtaining financial flexibility for a company can greatly stimulate innovative projects. Wang Jing, Zheng Qionge and others found that innovation activities require huge investment. In this way, the company can also obtain suitable funds from its own country, which is easy to call on whenever the company needs, so as to solve the daily needs. Research and innovators will be able to use the remaining debt capacity to quickly access financing in the future to alleviate research funding shortfalls. Greater financial flexibility allows the company to use more flexibility in financing, to seize important financing opportunities for technological innovation, to deploy excellent research teams, and to set some rules to improve initiatives. In this way, the work efficiency and resources of employees are improved, and the innovation performance of the company is improved with efficiency. Strong finance encourages the development of innovative projects and the establishment of patented technologies, promotes the technological innovation achievements of enterprises, and thus improves the technical management level of the company. Without special financial resources to mobilize innovation investment, it is difficult for companies to achieve technological innovation performance.

### **3.4. Financing Constraints and Innovation Performance**

First of all, according to the theory of financing priority, the most preferred financing method for enterprises is internal financing, but the funds that enterprises themselves and shareholders can provide are only a small amount after all. In the current severe economic situation, the surplus funds of enterprises are not enough to support a series of investment activities, so they have to raise funds from the outside world. However, whether it is equity or bond financing, it involves a series of issuance costs and other expenses, and the financing cost is high [5]. Second, according to the principal-agent theory, the interests of corporate executives and shareholders are inconsistent, which leads managers to make adverse selection or moral hazard behaviors in order to pursue personal interests. For example, managers may give up reasonable financing behaviors to reduce the debt ratio and financial risks of enterprises, which will further aggravate the financing constraints of enterprises. Third, like banks and other credit companies, external investors such as shareholders and creditors tend to be more cautious about investment in high-tech enterprises with fewer physical assets and higher operating risks under the background of information asymmetry, which makes it more difficult for high-tech enterprises to finance.

On the other hand, the core of an enterprise's investment decision is around the principle that the expected return is greater than the input cost, and this principle will be more prominent when the enterprise is facing financing constraints or financial difficulties. In other words, when facing financing constraints, the first thing enterprises do is often to reduce those projects with large input costs and uncertain expected benefits as much as possible. Therefore, the improvement of financing constraints will reduce the innovation performance of enterprises.

## **4. RESEARCH CONCLUSIONS**

Innovation is the main driving force for China's economic development, and it is also the top priority for the high-quality development, transformation and upgrading of China's manufacturing industry.

For enterprises, how to transform innovation consciousness into innovation behavior, and then into innovation performance, is the key to obtain core competitiveness and foothold in the market. The existing literature on innovation performance generally ignores the role of corporate strategy on innovation performance from the perspectives of government behavior, innovation network, enterprise characteristics, R&D investment and management characteristics, etc. Whether the strategy implemented by an enterprise conforms to the mainstream trend of the industry will certainly have an impact on its innovation performance. The basic conclusions drawn by this analysis are as follows:

First, the degree of strategic difference has an inhibitory effect on innovation performance, that is, the greater the degree of deviation of an enterprise's strategy from the conventional strategy of its industry, the lower the innovation performance. In terms of innovation capital investment, innovation activities require large and stable R&D capital investment, while enterprises with large strategic differences face great obstacles in obtaining external financing due to information asymmetry and low legitimacy, and occupy too much internal capital, resulting in crowding-out effect of capital investment in innovation activities, and thus adversely affecting innovation performance. In terms of innovation risk taking, innovation is a high-risk investment activity, and enterprises with large strategic differences often bear higher operational risks, so they are not willing to bear excessive innovation overlapping risks, which inhibits innovation performance.

Second, maintaining financial flexibility can effectively mitigate the negative impact of strategic variance on innovation performance, that is, the higher the level of financial flexibility, the weaker the negative impact of strategic variance on innovation performance. Financial flexibility is an enterprise's ability to call financial resources in time, prevent adverse business risks, and take advantage of investment opportunities. Maintaining high financial flexibility can alleviate the negative impact of strategic differences on innovation performance from the aspects of capital supply and risk taking.

Third, under the conditions of different industry characteristics, regional distribution and product market competition, the relationship among strategic differentiation, financial flexibility and innovation performance of enterprises has certain similarities and differences. The similarity lies in that, regardless of whether the industry of the enterprise is traditional manufacturing or advanced manufacturing, whether the region is in the eastern region or non-eastern region, and whether the product market competition environment is fierce, strategic variance is significantly negatively correlated with innovation performance, and financial flexibility has a significant mitigating effect on the negative correlation between strategic variance and innovation performance [6].

## **5. COUNTERMEASURES AND SUGGESTIONS**

(1) Enterprises should make timely dynamic adjustments to strategies to alleviate the conflicts between strategies and internal and external risks. The results of this paper show that increasing the degree of strategic difference will bring risks and uncertainties, lead to intensified financing constraints, and thus inhibit the improvement of enterprise innovation performance. First, enterprises should accurately assess their own risks and conduct comprehensive and multi-angle analysis of internal and external environment. Select strategic objectives that match the current development level. Secondly, after the formulation of strategic objectives, refine the strategic information evaluation index system, formulate a phased strategy implementation inspection table, regularly report the implementation of corporate strategies to stakeholders, and disclose relevant information to the public, so as to reduce business risks brought about by strategic differences. Thus, the problem of information asymmetry and agency cost can be alleviated.

(2) Enterprises should actively cultivate financial flexibility and steadily improve their own innovation performance. Financial flexibility can alleviate the negative impact of strategic variance on innovation performance. First of all, enterprises should enhance the awareness of financial

flexibility reserve, realize the importance of financial flexibility, and consciously cultivate and enhance the financial flexibility of enterprises by establishing good business reputation, expanding financing channels, strengthening the construction of the capital market within the group, etc. Secondly, enterprises can implement equity incentive plans to further release the potential of financial flexibility. The implementation of equity incentive plan can effectively alleviate the agency cost problem of enterprises and enhance the financial flexibility of enterprises. Empirical research finds that the cash flexibility level of enterprises with high equity incentive is higher than that of enterprises with low equity incentive, indicating that the application of equity incentive can improve the utilization efficiency of enterprises' retained funds to a certain extent.

(3) State-owned enterprises and non-state-owned enterprises should adopt different strategies to improve the degree of strategic difference. State-owned enterprises with rich financial resources will be more radical in strategic decision-making, constantly expand industrial boundaries, and achieve leapfrog development. In order to realize the efficient allocation of financial resources, state-owned enterprises should pay special attention to the capital flow and strengthen supervision during the implementation of the strategy. Reasonable use of financial resources can effectively solve the problems of owner absence and resource redundancy which have long plagued state-owned enterprises. For non-state-owned enterprises, they need to fully consider the impact of financing constraints on business operations when making strategic decision-making objectives.

## 6. CONCLUDING REMARKS

There is a complex relationship between the degree of strategic difference and innovation performance and financial flexibility. Enterprises with large strategic differences are faced with such challenges as information asymmetry and financing difficulties, so they tend to improve their financial flexibility to meet future investment needs. The enhancement of financial flexibility can provide necessary financial support for technological innovation of enterprises, so as to improve innovation performance. These three show a dynamic relationship of mutual influence and mutual promotion. Enterprises need to accurately grasp the balance between strategy, finance and innovation, and scientifically allocate resources to continuously improve their comprehensive competitiveness.

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