CHAPTER 2: LITERATURE REVIEW

2.1. Introduction

This chapter indicates the contribution of literature about the defined topic. Also, the highlights of the topic in terms of past studies are presented in this chapter. Hence, each appointed variable is defined under the lights of literature along with it its determinants. Moreover, the important relationship of each variable is also determined under this chapter. Later on, from the review of past perspectives recent themes are generated. Each theme is later contributed to generate the conceptual framework. Eventually, the hypothesis is composed out of the defined conceptual framework that in turn is backed up by theoretical backgrounds.

2.2. Relational Capital

The track of the flow of assets through the route that has been configured socially is termed as relational capita. Besides, the joint action under a community is originated through the concept of relational capital (Cai et al., 2014). In simple words, all kinds of relationships between the firm and its stakeholders are denoted as relational capital (Corvino et al., 2019). The importance of relational capital is backed up by the tendency of communication of a firm (Corvino et al., 2019; Zhao et al., 2019).

In action, a wider form of information can be dispersed by the firm with a diverse relational capital (Russell et al., 2015). Consequently, engagement of all the stakeholder acts as a competitive advantage that in turn crown the firm the title of being a market leader (Zhao et al., 2019). Moreover, the organizations are involved in social exchange processes by buying raw material converting it into useful outcomes and delivering to the customers (Cai et al., 2014). Subsequently, the organizations are obliged to develop trust levels for executing the effective

social exchange. For this, the recent firms indulge relational capital for indicating a higher level of trust among the market.

Another critical association of relational capital with a firm's performance is backed up by the diminishing nature of past collaborations. In other words, the firm collaborates with other businesses and temporary stakeholders in the industry for a particular goal. As soon as the goal is accomplished the collaboration diminishes. Whereas, collaboration with key stakeholders (key suppliers, customers, investors, and employees) remains constant throughout the lifecycle of the business (Corvino et al., 2019). Consequently, the businesses can sustain in the market only due to their intangible capital or relational capital. Hence, the performance of any organization is evident to be significantly dependent on the relational capital of that firm.

2.3. Firm Performance

Every organization exists for a certain purpose that determines the legitimacy of that firm. In response, the organizations rate their positions in accordance with the set objectives. This evaluation of any organization in terms of performance is termed as the performance of the firm (Cai et al., 2014). Organizational performance is also denoted as actions that are practiced for the accomplishment of the desired goals (Raithel and Schreck, 2018). In association, the management of every organization is indulged in the enhancement of performance of the firm in terms of profits, people and value preposition (Ljungholm, 2016). Moreover, organizational performance is sensitive to many factors such as; the size of the firm, micro-macro environment, financial assistance, pressure from the stakeholders, etc. (Wang et al., 2014; Russell et al., 2015; Cai et al., 2014). Eventually, the performance of an organization indicates the capability of that organization that is later used by the industry to rank that organization (Zhao et al., 2019).

In correspondence, the higher the performance, the higher the market share is grabbed by the firm. Hence, such an organization is ranked as the market leader (Wang, Wang, and Liang, 2014).

Mehralian, et al. (2016) define the presence of effectiveness in organizational efforts to accomplish its objectives makes up the performance of a firm. Evaluation of a firm's performance assists the management in quantifying the factors that create hinder the accomplishment of the objective of that firm. Therefore, the performance is often in a continuous evaluation phase in terms of the relationship of a firm with its stakeholders, financial performance and managerial concerns. The evaluation of the performance of a firm is a complex process. Therefore, different aspects of modes of evaluations are performed by the analyst to highlight all the aspects of a firm's performance. In action, both pecuniary, as well as non-fiscal measures, are employed by managerial members to measure the performance and rate its effectiveness (Raithel and Schreck, 2018).

2.4. Firm Size

The size of any organization is often quantified in terms of financial decisions. However, it is quite more than just the financial worth of the firm and its market sharing in the market (Raithel and Schreck, 2018). In addition, firm size is determined as the presence of tendency of managerial compensation, variability in financial decisions and estimation of rates of return from the firm's performance. The size of any organization determines its capacity to grow and aid in the economic growth of the region it is operating at. In association with this, assistance from the theoretic background is employed by many analysts to first define the firm size then denote its determinants. In association with this, three theoretical backgrounds are observed from the

literature namely; technology, organization, and institution (Zhao et al., 2019; Ali et al., 2018; Corvino et al., 2019).

At first, the technological theories define firm size as the tendency to bear set-up costs for different tasks of that firm (Zhao et al., 2019). In detail, assigning every human capital with a specialized task incurs certain set-up costs for that task performance. For instance, a worker is hired to perform a production task in the production unit, so to increase the productivity the company is mandated to appoint more workforce. Hence, for every specialized task, a cost is incurred by the fir. Hence, the higher the specialized tasks are practiced by a firm it determines the size of that firm.

Secondly, the organizational concept of theories from literature denotes that contractual cost, transaction cost, and critical resources determine the size of a firm (Ali et al., 2018; Mehralian et al., 2016; Raithel and Schreck, 2018). In-depth explanation, the contractual costs define a firm's size as a configuration of contracts that are entertained by the firm at the contemporary stage (Zhao et al., 2019). With reference to the transactional cost aspect, organizational size is the length of transactions that take place in that firm. For instance, the higher the rate of transaction cost is practiced by a firm, the larger its size is considered (Josefy et al., 2015). Eventually, the critical resource defines that transactions can take place under the contractual or enforced entity, but the non-contractual source that governs the performance of transactional actions is the critical resource. Hence, an organizational size can be measured under organizational theories in terms of several contracts, transactional tendencies, and critical resources.

Ultimately, the institutional backup of organizational size id categorized into two namely; regulatory and financial (Russell et al., 2015). In action, the forces that govern the operations of a

firm are determined as an institutional aspect. For instance, legal obligations on firms enforce actions like environmental sustainability, corporate social responsibility, etc. on the firms to legitimate their existence in the market. Similarly, regulatory institutions obliged organizations as per their sizes and tendency to hold obligations. Likewise, financial institutions impose obligations in terms of financial decisions such as taxes, duties, tariffs, rate of return, interest rates, etc. (Ali et al., 2018). The higher the number of obligations from regulatory and financial institutions is enforced on any firm, the larger its size is considered.

2.5. Relationship of Relational Capital and Firm Performance

Relationship with different stakeholders develops relational capital. Suppliers, customers, stockholders, and employees are the most critical stakeholders that shape up the relational capital of a firm. In association, agility is referred to as the ability to move from one place to another. In terms of businesses, the agility is referred to as the supply chain system of the organization (Byun et al., 2019). In other words, the efficiency in moving the inventory from point of origin to point of consumption effectively often denotes the performance of a firm. The supply chain management is the track record of the movement of a raw inventory from its origin to converting point where it gets modified or manufactured into another form that eventually becomes a usable product. Later, the modified product is delivered to the end-user for consumption (Yayla et al., 2018). Concerning supply chain agility, it is referred to as a firm's capacity of cohesion between the key suppliers and customers of that firm (Mehralian et al., 2016).

In other words, the environment changes with time resulting in pressure for change in the relationships of any organization. Similarly, a trustworthy and proactive relationship with key stakeholder aid every organization in its performance. For instance, any change in the environment such as; the rate of inflation, exchange rate, and employment rate can result in

altered charges of raw material and its transportation cost as well. In response, collaborative suppliers will aid the firm in mitigating such forces by induction of strategies like bulk supplies or collaborative supplies, etc. (Yayla et al., 2018). Consequently, the firm can fulfill the requirement of customers and grab their share in the market as well. In contrast, any hinder in the supply chain becomes a costly action for the firm. In practice, higher rates of supply and raw material will mandate the firm to raise prices of the product due to an increase in cost, this point will limit consumers from buying the same product at a higher price. Eventually, the firm is at risk of negligence and a downturn.

2.6. Relationship between Firm Size and Performance

To gain performance, firm size is considered as an imperative characteristic. There are large amount of resources and greater capacity for the purpose of production in large firms. The financial performance of the firm is improved through this way. When it comes to the smaller firms, the smaller firms are considered more flexible in nature than the larger firms, albeit it is believed that as compare to smaller firms, in lager firms there are better perquisites for behavior (Kioko, 2013). Given that, the larger firms are more compatible to involve in the process of inter-firm networking as they are well equipped as compare to their smaller counterparts. As compare to smaller firms, there is more trust is placed by the cooperative partners on the larger firms. This trust greatly emboldens the larger firm because the cooperative partners of the firm believe in the integrity and reliability of the firm. There is less potential drawback in the larger firms as they are characterised by high level of trust by the cooperative partners. Therefore, in this way the financial performance of the firm is increased and its cost is greatly reduced.

There is lively debate on the impact of firm size on the performance of the firm. It is believed that smaller firms are easily outperformed by the larger firms. However, when it comes

to harsh economic conditions, it usually becomes the cause collapsing of large firm. There are many advocates of smaller firms who argue that the niche markets knowledge and unique sort of offerings enable to small firms to get competitive edge. Nevertheless, there is a perception that the larger firms are more profitable as compare to the smaller firms. There are a very few people who questioned the creditworthy of the large firms. This is reason that most of capital provider more likely to invest in the larger firm (Mazhinduka, 2015). The products of lager firms are marketed on large scale, besides there is great spending on research and development on larger firms. The great spending on research and develop by the larger firms provides benefit to smaller firm in the long run as well. The reason behind the perception that the larger firms are profitable than the smaller firms is based on the aforementioned advantages. Whatsoever, the firm size of the organisation is considered the most considerable aspect, and it is considered by many of the scholars that the size of the firm plays an imperative role in determining the performance of the firm. Although, there are advocate of lager firms and smaller firms who create complexities in understanding that what size of the firm will be considered most appropriate for the performance of the firm.

2.7. Impact of moderating effect on Firm Performance

The organizational performance or the firm performance has been explained above that a firm tends to achieve its desired objective. Concerning the moderating effect of any organization, it is referred to the interactional effect of a third variable on the relationship of two variables (Byun et al., 2019). This effect is used by analysts to determine the impact of the relationship between two such variables that are complex or extremely volatile. In the case of firm performance, it is sensitive to several factors, hence induction of a third variable to measure the extent of change in organizational performance is essential. With reference to this, the impact of the moderating effect on organizational performance is directly proportional.

Any stimulating factor can be employed as a moderating effect to measure the performance of the firm and it's positioning in society. For example, the impact of stockholders can be employed as a mediating effect to measure the company's performance in terms of rate of return. Similarly, the tendency of brand trust can be investigated and moderating force to quantify the relationship between customer loyalty and perceived value (Ljungholm, 2016). In fine, the effect of any moderating variable is observed to be significantly and directly associated with the performance of the firm. For instance, any change in the moderating variable like supply chain, customer’s perception, environment, etc. will directly stimulate the performance of the organization (Josefy et al., 2015). Consequently, the efficiency and effectiveness levels in the performance of any firm are dependent on the various variable. To list an explicit view of a firms' performance and its size, the researcher must align the third variable and keep the research in a specified direction.

2.8. Moderating Effect of Firm Size on Firm Performance

In the reviewed literature, the firm size has been observed as a primary factor to stimulate the profitability of a firm. Also, the induction of economies of scale has entitled firm sizes as a critical determinant of a firm's performance (Raithel and Schreck, 2018). As stated previously, the determination of firm size and its determinants varies in accordance with the different theoretical backgrounds (Ali et al., 2018). In response, firm size can be considered with respect to its capacity to own leadership in the marketplace. For instance, larger-sized manufacturing companies own cost-leadership over the smaller ones. The reason for this is larger organizations have defined and diversified work with high set-up costs. Besides, the contractual cost and transactional cost is also higher for such an organization due to the rate of production. Hence, the size of a firm can aid in defining its operational performance and set a competitive edge over the market.

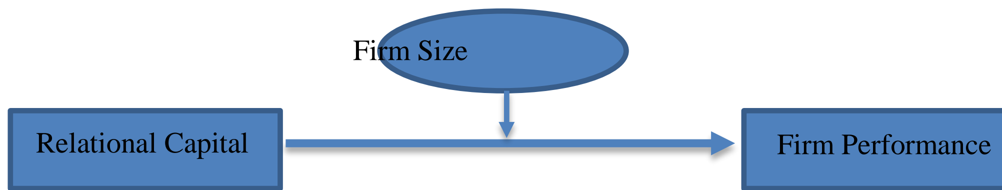
In contrast, the relationship between firm size and firm performance is significant, but not always proportional. Some studies support the fact that the firm size can inversely affect the performance of a firm (Corvino et al., 2019; Ali et al., 2018; Raithel and Schreck, 2018). In association, larger-sized organizations are complex to manage whilst smaller ones are easily (Josefy et al., 2015). Similarly, the induction of transparency in huge organizations is again a hinder. Moreover, decision making and style of leadership also becomes complex with expansion in the size of a firm. Consequently, firm size is considered as a moderator to estimate the impact of another variable on a firm's performance. In correspondence, the impact of environmental factors in the determination of a firm's performance is also crucial as it directly stimulates the size of the firm (Wang et al., 2014). Hence, firm size and environmental impact are essential moderators of firm performance.

2.9. Conceptual Framework

From the review of related literature, the relationship between relational capital and firm performance is ranked as significant. In addition, their association with each other is observed to be critical (Corvino et al., 2019; Ali et al., 2018; Raithel and Schreck, 2018). In such circumstances, the literature has indicated that the induction of a moderator for such evaluating complex relations is an effective fit. Consequently, important moderators are evident in the literature such as environmental impact, size of the firm, etc. Ultimately, the size of the firm has been viewed as the most stable and stimulating moderator of a firm's performance (Ali et al., 2018; Wang et al., 2014; Corvino et al., 2019).

Moreover, firm size is found to be backed up by different theoretical frameworks namely, technological, organizational and institutional (Cai et al., 2014). Besides, the emphasis of every theory coincided with a point that firm size is directly associated with the performance of that firm. In association with relational capital, it has been viewed as a critical as well as the sensitive aspect of a business. From the literature, it has been outlined that firms with widen standardization of works hold stronger relational capital. On the other hand, companies with limited exposure to stakeholders encounter limited relational capital.

From the considered review, the conceptual framework for this study has been generated in terms of three basic variables namely relational capital, firm size and firm performance. Among these, relational capital is the independent variable whilst firm performance is a dependable one. Provided, firm size is quantified as a moderating variable to observe its impact on the relationship of relational capital and firm performance.



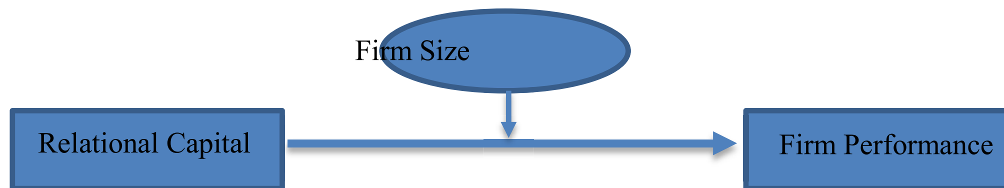
From the defined conceptual framework, the following hypothesis is generated. These will be tested in the study;

- H1 A firm's relational capital is positively related to its size
- H2 The relationship between relational capital and firm performance is mediated by firm size
- H3 A firm's relational capital is positively related to its performance

2.10. Chapter Summary

So far under this chapter, it has been reviewed that the moderating effect is essential for determining any two complex correlations. In addition, three basic variables were defined by the literature. At first, the relational capital has been viewed as the intangible capital of a firm that indicates its market reputation. Secondly, firm size is observed as a determinant of a firm's performance. Thirdly, the firm performance has been analyzed as the tendency of an organization to accomplish its defined objective. Ultimately, the literature has assisted in the formation of themes for the conceptual framework that indicates relational capital as the dependent variable and firm performance as a dependent one. Provided, firm size has been employed in a moderating effect.

2.11. Hypotheses



From the defined conceptual framework, the following hypothesis is generated. These will be tested in the study;

- H1 A firm's relational capital is positively related to its size
- H2 The relationship between relational capital and firm performance is mediated by firm size
- H3 A firm's relational capital is positively related to its performance

2.10. Chapter Summary

So far under this chapter, it has been reviewed that the moderating effect is essential for determining any two complex correlations. In addition, three basic variables were defined by the literature. At first, the relational capital has been viewed as the intangible capital of a firm that indicates its market reputation. Secondly, firm size is observed as a determinant of a firm's performance. Thirdly, the firm performance has been analyzed as the tendency of an organization to accomplish its defined objective. Ultimately, the literature has assisted in the formation of themes for the conceptual framework that indicates relational capital as the dependent variable and firm performance as a dependent one. Provided, firm size has been employed in a moderating effect.

2.11. Hypotheses

H1: A firm's relational capital is positively related to its size

H2: The relationship between relational capital and firm performance is mediated by firm size

H3: A firm's relational capital is positively related to its performance