

A Research on the Matching of Firm Capability with Customer Value

Liu Shilan

School of Business, Guangdong University of Foreign Studies, Guangzhou, P.R.China, 510006
(E-mail: runnyreddy@yahoo.com.cn)

Abstract The potential to create value for customers stems from firm capabilities. More and more managerial practices have made it clear that supplier's capability is the key factor of evaluating its potential of value creation and is a major indicator for industry customers to select suppliers. The paper discusses the effects of firm capability on customer value separately from supplier and customer perspectives, and constructs the matching framework of capability to customer value based on analyzing the characteristics of different types of customer value. The matching framework that the paper description is of important implications for firms how to create customer value through developing and using capabilities.

Key words Suppliers' capability; Customer value; Matching

1 Introduction

Creating and delivering value to customers has long been a marketing leitmotiv. Customer value has been seen as a new source of firm competitive advantages (Woodruff, 1997), and the competence of creating superior value for customers by suppliers has been regarded as one of the most successful strategies in 1990s (Gronroos, 1997). Many managerial practices on customer management, however, have suffered from huge difficulties, even disastrous costs. The research by (Gartner 2001) found that 55 percent of projects of customer value management did not gain expected benefits. (Thomas 2003) thought, the main reason for it is that customer value in managerial practices is often seen as a managerial idea, while not as an organizational activities associated with firm capabilities.

In fact, more and more managerial practices have already showed that, suppliers' capabilities are a key indicator that customers assess suppliers' future value creation potential and choose optimum suppliers, while suppliers' products and services are main factors that customers assess suppliers' present value creation potential. But in the existing theories, the researches on how suppliers use their capabilities to create value for customers are too rare. Based on this, the purpose of this paper is to discuss the matching issue of firm capability to customer value.

2 Literature Review

2.1 The definition and types of customer value: capability-based perspective

The majority of scholars believe that customer value is the trade-off between the benefits and the sacrifices perceived by customers of suppliers' offering in market transaction. (Ulaga and Eggert 2005) have identified four characteristics of the customer value concept: (1) the customer's subjective perception and evaluation; (2) the trade-off between the perceived benefits and the perceived sacrifices; (3) the benefits and sacrifices are two multidimensional concepts; (4) Value perception of a certain offering is a process of comparing with other competitive offering. We believe that there are some defects in the above definitions. Firstly, this understanding regards value mainly from the perspective of customers, while ignores the perspective of suppliers; Secondly, this point of view pays main attention to the result of value creation, and holds that value dimension is typically embodied in the offering—and in particular products and services dimensions—proposed by the supplier following market research aimed at identification of the customers' needs, while it does not emphasize the process of value creation, especially the co operational activities carried out by suppliers and customers; thirdly, this point of view does not provide further guidance for suppliers and customers to engage in value-creating activities, thus its implication for managerial practices is not powerful; Finally, this point of view is based on resource-based view, and believes that value derives from products or other offering, but it does not point out the role of capabilities in creating customer value. This research believes that conceptualization of customer value should highlight the process of creating value from the perspective of capabilities, based on identifying the relationship between suppliers and customers. Therefore, this research defines the customer value as the process in which the supplier develops, shares, and uses the capabilities as well as engaging in other value activities by itself or with customers, in order to improve the value creation potential.

Customer value may be divided into different hierarchies. (Woodruff 1997) proposes that customer

value consists of three step-up levels: product attributes layer, result layer, and target layer. (Sweeney and Soutar 2001) measure statistically that customer value contains four dimensions, namely emotional value, social value, quality value and price value. In order to distinguish transactional value from relational value, (Henneberg and Pardo 2005) believe that customer value can be divided into three levels: transactional value, relational value and proprietary value. In accordance with the above standpoints, combining the perspectives of transactions and relationships, this research divides customer value into three types, namely transaction-economic value, relation-adding value and network-future value according to the interactive intensity between suppliers and customers in the process of value creation. The transaction-economic value is an exchange orientation, which means that suppliers' value creation does not require customers' participation and customers only weigh the benefits and sacrifices of the offering provided by the suppliers. Relation-adding value is a simple relationship orientation, that is to say, value creation requires simple interaction to a certain extent between both partners, and customers weigh the benefits and sacrifices of an interactive process. Network –future value is a complicated relationship orientation. Members in the network perform extensive cooperation for the future, especially cooperation of radical value innovation. Customers weigh the benefits and sacrifices of the network of relationship.

2.2 The definition and types of firm capability: customer-based perspective

Grant (1995) thought that the enterprise capability is a series of knowledge and skills that enterprises use to undertake and complete a special activity. According to the complexity of the activities, firm capabilities can be divided into the capability to fulfill a single task, professional capability, activity-based capability, capability within functions and inter-functional capability. Day (1994) regarded firm capability as a range of complicated skills and accumulated knowledge which enables enterprises to integrate activities and make full use of organizational resources through organizational processes. Similarly, in accordance with different orientations and focuses of the process, Day (1994) divided capabilities into orientation-inside processes, orientation-outside process, and processes that connect inside and outside orientation. Grant's definition emphasizes the link between capabilities and activities, and recognizes that an activity is the basic unit that constitutes value; Day's definition is based on firm process, and recognizes that capability is knowledge and skills embedded in the process. However, both definitions share a common point: capabilities are related to activities, because a process is a collection of a series of related activities. The capabilities defined by Grant reflects abilities' embeddability, which involves capability of individuals, and of teams or inter-organizations; while Day not only points out the importance of the external capabilities for nurturing and maintaining customer relationship, but also stresses the significance of integration and coordination of internal and external processes in the value creation.

However, definitions and classifications of firm capabilities by Grant and Day are from the perspective of enterprise itself, while not from the perspective of customers, thus we can not recognize the relative importance of various abilities in firm capability structure on meeting the customer needs and creating value for customers. As a result this make against managing firm capabilities according to market change. From the perspective of customers, combined with Grant and Day's definition and classification of capabilities, this research defines enterprise capability as a series of knowledge and skills that can create value for customers and are stored in both internal and external processes of organizations. According to the different characteristics of the three levels of customer value (namely, transaction-economic value, relation-adding value and network-future value) on capabilities required, enterprise capabilities can be classified into efficiency-oriented capabilities, effectiveness-oriented capabilities and value innovation-oriented capabilities from the perspective of the values of capabilities.

2.3 The role that firm capability plays in customer value

The role that firm capability plays in customer value varies from the different perspective of customers and suppliers. From the perspective of customers, the significance that firm capability plays in customer value is mainly that, firm capability becomes a key indicator to assess suppliers' potential to create value and to select the best suppliers. This is mainly because, on the one hand, if specific products provided by suppliers are made as standards of evaluating suppliers, it is very difficult for customers to find out how the suppliers' capabilities can support their business activities and whether they can support special innovation projects; On the other hand, owing to product life cycle's continuously shortening, customers seek to some factors which would not be devaluated easily to substitute products in order to evaluate their suppliers. Masella and Rangone (2000) also point out, an increasing number of management practices have showed that, products and services are core elements to evaluate current value which suppliers provide for customers, while the capability of suppliers is a key indicator to

measure their potential to create the future value for customers.

From the suppliers' perspective, capabilities has two main functions in creating values for customers: First of all, firm capabilities, as a major asset of the organization, indirectly create value for customers through being transformed into or stored in products, services, brands and relations. Berghman and Matthyssens (2006) thought that firm capability plays a very significant role for industrial suppliers to predict and respond to the change of customer value in advance. Second, firm capabilities, as a marketable market asset, are the direct source of customer value. Suppliers can directly create value for customers through transferring abilities to customers. For a long time, the capability-based view of firm considers that capability is of characteristics of value, scarcity, non-transferability and non-substitutability. Thus this perspective regards capabilities as an input factor of organizational process. However, Golfetto and Gibbert (2006) believe that this point of view does not comply with some current phenomena. The capability-based view of enterprises can not explain the communication and transactions of abilities on trade fairs and exhibitions. Moreover, they called this phenomenon "competence marketing" and defined it as "some tools and process that enterprises use to communicate, transfer and sell competence in commercial relationship. Moller (2006) also supported the point of view of "competence marketing", and put forward another explanation. For example, in order to strengthen core competence, enterprises often outsource some non-core abilities, then logically the appropriate contractors become capability sellers and sell the needed competence to the vendors. Therefore, the capability-based view of enterprises restricts the effects of capabilities have on industrial marketing and purchasing. The competence is not only an input element, which has indirect effects on customer value through being transformed into or stored in the products or other offering, but also an output element, which becomes a direct source of customer value through the transfer and exchange.

3 The Matching of Firm Capability to Customer Value

Different types of value production has different features in the aspects of innovation degrees, relationship needs, value assessment and so on. Therefore, the types of capability they need are too different. In the following passage, this research will analyze features of the above three value production in detail and describe further the needed types of capability.

3.1 Transaction-economic value production and efficiency-oriented capability

Transaction-economic value production is that suppliers perform solely value activities to produce offering for the customer, and then the customer carries out some activities through using his own resources and capabilities to release the benefits inserted in offering. Therefore, it needs some extra costs for customers to gain and consume benefits of the offering. According to this, a customer often makes a tradeoff between gains and loses, and also compared it with other competitive offering so as to define the value creation potential of suppliers (Moller and Torronen, 2003). Under this kind of production pattern, customers have their own capabilities to release the benefits from offering. Thus, value production and reception do not need any adjustment from the two sides and do not need any new resources. As the customers need to pay the cost to use the potential value of offering, the objective of this kind of value production is to utilize the current resources and business processes effectively and increase efficiency.

Efficiency is the primary intrinsic factor in deciding transaction-economic value. It affects customers' profits, selling scales and the competitive competence of product price. Therefore, this kind of pattern needs different efficiency-oriented capabilities to prop up. Many literatures of operational management and supply chain management indicate that suppliers, who increase productivity, improve production methods and create scale superiority, can lower production costs. Reducing some redundant processes of order management, logistics and sales, lowering uncertainty, and speeding up the payment can lower the transaction costs. Moreover, Moller and Torronen(2003) pointed out that, optimizing and improving internal processes, reorganizing operational activities, arranging exterior processes, integrating value activities of suppliers and distributors, and adjusting the business process of suppliers and customers can enhance greatly efficiency. Based on this, this research proposes the following proposition:

P1: Efficiency-oriented capabilities (such as mass production capability, Effective delivering capability, intrinsic process optimization capability, Supply chain integration ability) have positive effects on transaction-economic value.

3.2 Relation-adding value production and effectiveness-oriented capability

Relation-adding value production is a kind of value production pattern that suppliers and customers

take the maximization of mutual values as the objective and cooperatively develop a more effective product and process through common investment and adjustment. This kind of value production pattern needs both sides to carry out the incremental innovation of the existing processes and value production system. In addition, the assessment of relation-adding value is more difficult compared with transaction-economic value. Its difficulty depends on the degree of product or process adjustment, on whether it needs the important resources to input from the third party, and on the openness and trust level of bilateral relation. In view of the above features, this kind of value production needs to cultivate the combination of various capabilities that are oriented to effectiveness.

Suppliers need not only to develop incremental innovation capability so as to enable sustainable change of the existing process and production system, but also endeavor to reduce the dependence of capabilities when customers use offering. Because if suppliers add some attributes to offering that cannot be utilized by customer's capability, then it cannot bring any extra value to customers. On the contrary, customers may suspend the extra expense that has to be paid. Therefore, on the one hand, suppliers need to enhance the intellectual design ability of offering. On the other hand, it needs suppliers to provide related services on utilizing offering, such as the customer training, on-the-spot guidance, and so on. In addition, although the capability of sustaining product development and innovation is the key to increasing customer-adding value, it is difficult for this kind of incremental innovation to have effective reaction on the market if an enterprise has no market-oriented capability. Moreover, Day also believes that, the market-oriented enterprises have better market achievement than other enterprises. Based on this, this research proposes the following proposition:

P2: Effectiveness-oriented capabilities (such as incremental innovation capability, intellectual design capability, customer service capability, Market-oriented capability) have positive effects on relation-adding value.

3.3 Network-future value production and value innovation-oriented capability

Network-future value production is a kind of value production pattern that suppliers and customers set future value creation as a goal, and then both commonly develop new technology, create new product or business concept and new business pattern. This kind of value production pattern has following several features: Firstly, it needs to carry on radical change of the existing value production system and create completely different value activities. Secondly, it needs to construct well a relation network and design dynamic and complicated learning process. Thirdly, it is difficult to evaluate exactly different value activities and products beforehand under this kind of production pattern because it relies on the development and the evolution of the service field or other related field and even the whole society. Finally, although this kind of value production has great risks, it also has great potential incomes. This kind of challenge will motivate many investors and managers to hold a more and more optimistic attitude towards the development of network future value.

As network-future value production needs to have radical transformation on the existing business thinking mode and business pattern, it needs the combination of different capabilities that is oriented to value innovation. On the one hand, it needs the radical innovation capability of industrial development pattern, industrial production logics, industrial rules and technologies. It needs the capability to re-position the existing value function, re-construct value production process and to transform the intrinsic business pattern. On the other hand, radical value innovation usually needs to mobilize some other participants as well as "customers" and "suppliers". Therefore, it needs to develop dynamic capability of relationship network management. First, the supplier should be able to fully understand the development status of the business field, set attractive network construction agenda and mobilize other enterprise to participate in the network. The network mobilization needs enterprises to be in the core status of the field. It should have special resources and knowledge to attract other enterprises to participate in the network. Only this can they select excellent cooperators and affect the formation of strategic network. Next, it should develop a network cooperation culture, such as mutual trust, studying, and knowledge sharing, in order to guarantee the justness and fairness of cooperation among member enterprises, especially small enterprises. Finally, it should increase the network leading capability. A network leader means to be able to affect the developing direction of new business network, and can realize and identify the changing tendency and track of new business field. But it is not any participants that can become the network leader. This role needs to have fertile imagination and strong communication ability, to deeply understand the development of business field, and to gain stronger business position. Based on this, this article proposes the following proposition:

P3: Value innovation-oriented capabilities (such as radical innovation capability, value reconstruction capability, business pattern transformation capability, network mobilization capability,

network cooperation capability, and network leading capability) have positive effects on network-future value.

Finally, although above three capabilities that value production needs have different functions and different contents, they are mutually related and supplemented. Although efficiency-oriented capability is the basis of transaction-economic value, it is also the requirement of value-adding production and provides the conditions for network-future value production. Similarly, for effectiveness-oriented capability, the capability of dealing with business relationship is not only the premise of reducing transactional costs and increasing economic value, but also an important method of handling more complicated network relationship and creating network future value. The enhancement of enterprise value innovation capability is not only the basic of future value creation, but also the new source of the creation of economic and additional value. Therefore, we believe that each type of value production is established on different value production systems and it needs different types of capability to maintain. Based on this, this paper proposes the following proposition:

P4: Efficiency-oriented capabilities have positive effects on relation-adding value and network-future value.

P5: Effectiveness-oriented capabilities have positive effects on transaction-economic value and network-future value.

P6: Value innovation-oriented capabilities have positive effects on transaction-economic value and relation-adding value.

3.4 The matching framework of different capabilities to different types of value production

As described in the above, efficiency is the core of transaction-economic value production. It decides sales sizes and market competitive competence of customers' products, and finally affects profits gained by customers. Therefore, the improvement of efficiency-oriented capabilities for suppliers is a competitive focus of economic value production. Only those suppliers, that have the capabilities of scale-production, rapid delivering, and of process optimizing and improving, can gain lower production costs, less transaction costs, and more competitive advantages from more efficient processes. Effectiveness is the core of relation-adding value production. It relates directly to offering quality, brand reputation, and social image, therefore, the improvement of effectiveness-oriented capabilities for suppliers is a competitive focus of relation-adding value production. Only those suppliers, that have strong capabilities of value innovation, market orientation, and of customer relationship management, can gain more advantages in effectiveness. The capability of network-future value production of suppliers decides leading position and market leader role of customers in emerging industries. Only those suppliers, that have the capabilities of radical innovation, reconstructing value, strong network relationship management, and changing business patterns, can become optimum partners that customers choose and cooperate with.

Based on the above discusses, this research constructs a conceptual matching framework (e.g. Figure 1) of relationship between different types of value production and of capabilities.

4 Conclusions

This paper discusses the matching of different types of value production and different types of capabilities. Main conclusions of this research include: (1) to propose another definition of customer value from the perspective of capability. This definition considers the relationship between suppliers and customers, gives prominence to the process of value creation, emphasizes the role of capabilities in value creation, and so overcomes the defects of traditional definition. The definition is of significant implication to understand systematically customer value, and of more powerful guidance to value creation activities by suppliers and customers. (2) to discuss the role of capabilities in the value creation for customers separately from the perspective of suppliers and customers. This paper thinks suppliers' capability is a key factor and a decisive indicator that customers assess suppliers' value creation potential and choose optimum suppliers. Firm capability, as a marketable asset, is a direct source of customer value. Suppliers can create directly value for customers through transferring capabilities needed by customers. Traditional capability-based view, which believes firm capability, only as an input of organizational process, indirectly affects customer value, and so restricts the effects of capability on industrial marketing and purchasing. (3) to create different types of value needs different kinds of firm capabilities. Transaction-economic value production needs efficiency-oriented capabilities, relation-adding value production requires effectiveness-oriented capabilities, and network-future value production needs value innovation-oriented capabilities. This is of great implication for suppliers to

make a capability development strategy according to the requirement to capability of creating customer value.

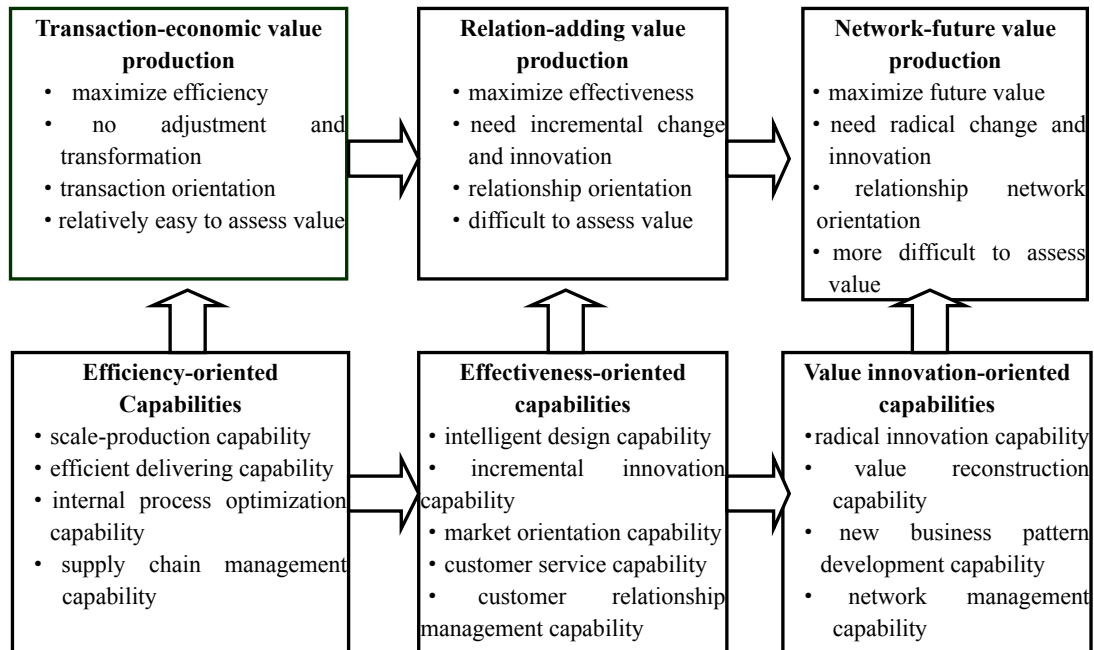


Figure 1 The Matching Framework of Three Types of Value Production and Capabilities

This paper, otherwise, needs to further study in the following: (1) Traditional capability-based view thinks that firm capability, as an input of organizational process, can not be transferred. However, some scholars have recently proposed the concept of “competence marketing”, “competence communication”, and “a marketable asset”, and have thought capability, as an output of organizational process, can be transferred. Obviously, this has greatly challenged traditional view. Therefore, future research needs to further discuss and disclose the essence issue of capability, and to explain theoretically these phenomena of competence marketing. (2) Future research needs to further validate empirically the conceptual matching framework between different types of customer value and of firm capabilities. (3) This paper thinks that suppliers’ capability is a key factor and a decisive indicator that customers assess suppliers’ value creation potential and choose optimum suppliers. In marketing practices, however, it needs to deeply study how customers assess suppliers’ value creation potential according to capabilities.

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