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Customer commitment to value creation process: Case of innovation based differentiation strategies

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Abstract— **Differentiation strategies based on innovation become one of most interesting aspect of value creation process. Considered as very efficient in firm competition advantage formation, they widely invoke the customer role. His engagement in value creation can encompass not only management architecture but also the search for concrete tools of company value proposition pre-evaluation.**

***Keywords*— *differentiation, innovation, product value cration process*, co-production, customer commitment**

I. Introduction

Describing the importance of value system related to the investment decisions J.M. English remarked that people are motivated by many things other than money, and these other values necessarily influence their decisions [4]. Often non-monetary values will dominate a decision. This point of view has been consequently developed and in fact, the conceptionalization of product or service value as the customer need satisfaction became the most important preoccupation of marketing orientation in management [5]. Particularly in mature markets, the value formulation process has been widely used as base for firms differentiation strategies strongly associated also with customer participation in market offering preparation. As consequence of differentiation strategy evolving, the marketing orientation is also considered as generation and dissemination of market intelligence with the firms responding to these challenges. This formulation of market focused learning process underlines the connection between the conceptions of value, differentiation and innovation.

II. Differentiation based strategy as the most perspective value creation concept

The concept of value in marketing orientation has still the large connotation and its concretization seems depending of specific company activities strategy process formulation based on value chain model developed by M.E. Porter [11]. This perspective on company value creation process is associated with systematic analysis of the series of activities a firm performs to provide its customer with a product. The value chain disaggregates a firm into its strategically important activities to understand the behavior of the firm's cost and firm's existing or potential source of differentiation. J.A. Pearce and R.B. Robinson underline that strategies dependent on differentiation are designed to appeal to customers with a special sensitivity for a particular product attribute, by stressing the attribute above other product qualities, the firm attempts to build customer loyalty [10]. Often such loyalty translates into a firm's ability to charge a premium price for its product. The business strategy of differentiation requires that business have sustainable advantages that allow it to provide buyers with something uniquely valuable to them. A successful differentiation strategy allows the business to provide a product or service of perceived higher value to buyers at a differentiation cost below the value premium to the buyers. Differentiation usually arises from one or more activities in the value chain that create a unique value to buyers. A business can achieve differentiation by performing its existing value activities or reconfiguring in some unique way. And the sustainability of that differentiation will depend on two things – a continuation of its high perceived value to buyers and a lack of imitation by competitors. The one of most important risk with differentiation is that the cost differential between low-cost competitors and the differentiated business becomes too great for differentiation to hold brand loyalty. Buyers thus sacrifice some of the features, services, or image possessed by the differentiated business for large cost savings. This strategy is mainly addressed to sophisticated buyers. The imitation reduces perceived differentiation particularly when occur the industry mature. The presented differentiation based strategies concept seems to be characteristic for the period of 80. and corresponds to I. Ansoff's strategy development process and also allows preparing firm's value proposition [1].

R.J. Trotta develops the strategic importance of value proposition and proposes three distinct sources for intrinsic value of company, which are revenue increase and maintenance, competitive repositioning and efficiency [13]. Firstly, the revenue increase and maintenance correspond to the economic vision of creating value and strongly expose the relationship between increasing value and the cash flow generated from increasing revenues. But in now day's market competition conditions, increasing revenue becomes more difficult in established industries, that why this is value proposition is normally associated with mergers and acquisitions. The second proposition which is competitive repositioning realized through: increasing or maintaining market share, improving competitive intelligence, differentiating the company from its competition. This way of

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increasing value still makes the strong link between the firm market share and the cash flow. But it will be not the unique action, the others two are to undertake in the same time – the company competitive advantage is obtained by acquiring knowledge about customers, suppliers, markets, and channels and at last by strong firm individualization which also may offer attractive for customer, who will appreciate it. The third value proposition – efficiency – is based on organizational process optimization which improves cash flow by performing business processes better, faster, or cheaper than the current firm operations. This value proposition can also be justified by reduction or avoidance of costs.

H. Macmillan and M. Tampoe suggest that in fact companies achieve competitive advantage either by having the lowest product cost or by having products which are different in ways which are valued by customers [9]. They also noted that differentiation implies a difference in the perception by clients of the product, whereas focus implies a difference in target market. In fact, in companies' practices, there is not such clear distinction between differentiation and cost. There are very few companies that can ignore cost however different their product. Equally, there are very few who will admit that their product is the same as all the others. That may be the reason why firms began to explore the use of intellectual property to enhance their competitiveness based on innovation and technology progress. In today's competitive business environment, operating companies need to develop products and services that provide unique differentiating value. Businesses also need to defend against potential threats to their well-being. Innovation is essential in order to maintain a competitive advantage. The value proposition derivated from the use of the new technology can help to create meaningful differentiation.

III. Innovation based differentiation strategy as the source of customer value

The strategic view of innovation in current marketing theory has its origins in industrial organization economics. In this view, profit comes from market power in a given market, while successful innovation makes the firm prominent in the product group level, giving rise to competitive advantage. The learning process, as the implementation of this strategy is as follows. First, a firm defines its business in terms of the market, and then by targeting and differentiation, it identifies the specific customer need within the defined market. In the third stage, the firm mobilizes its resources in innovating to satisfy the identified need. This approach emphasizes that the firm monitor customers for changing needs and competitors for changing products in order to maintain its competitive position. Since radical innovation creates its market by conceiving a discontinuity of customer perceived value, a new strategic view of innovation is required to overcome the constraint of a defined business and market. According to S.Y. Wu, the major challenge for a firm that wishes to create radically new values and develop new markets, is to make a totally, new strategic perspective basing on the strong relationship with the customers [16]. One of most interesting concept of customer value process creation was presented by J.N. De Bonis, E. Balinski, and Ph. Allen. Their model is the optimized combination of business processes, people, capabilities, resources, and capital that are focused and implemented in five continuous, dynamic steps that help to create value for the company and its customers [2]. Presented Pentadigm model is a more organizational path to transforming the business into a dynamic value creation model by transforming firm culture and processes into ones that continually scan for market insight about customers' behavior and future needs (fig.1).

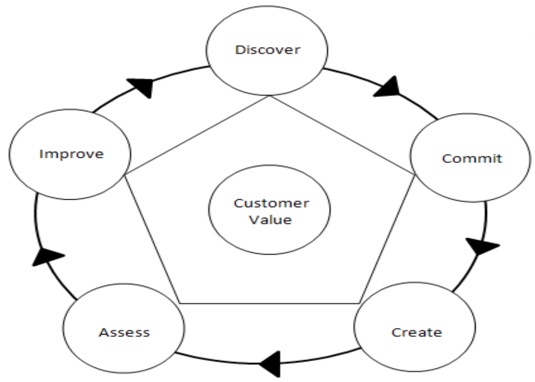

Figure 1. Pentadigm as continuous improvement process of customer value creation. Source: J.N. De Bonis, E. Balinski, Ph. Allen: Value-Based Marketing for bottom-line Success. 5 Steps to creating Customer Value, AMA, McGraw-Hill, USA 2002, p.18

This approach enables firm and its innovation efforts to offer future value that customers will be more likely to pay for because it's connected to what really matters to them. It enables also to formulate an attractive proposition for innovator customer value segment. In this case, the primary value driver is the need to maintain a leading competitive advantage in the customer's market and to be perceived as an innovator in its industry by creating value with leading products, services, technology, markets, and processes. The adequate group of customers focuses tends not to be price sensitive, but innovative sensitive, and this kind of market comportment is very similar to the circumstances of differentiation strategy use. This implies the discovering and understanding the purchasing behavior and value drivers of individual customers as the first step in value segmentation and provides a meaningful basis for targeting those customers who are most likely to firm offer value and enable to calculate whether it's possible to serve those customers profitably [6]. Presented approach signalizes also the importance of customer value commitments, which can help to define which business resources are critical to winning business in the targeted customer value segments. This enables company to focus on specific value-creating factors, and achieve the superior value position with customers. However, the nature of customer commitment in term of value perception in described approach remains rather vague and needs to be more discussed.

IV. Customer commitment as the value co-production optimization

Customer centered value creation process has to be released with conscience that in some situations, the company must evaluate the compromise between cost management and value to the customer [3]. In fact, maximization of customer value proposition can imply the diminution of value delivered to the firm. That why it will be crucial to understanding the growing gap between the two, so that the firm can deliver superior value profitably. W. Ulaga underlines the importance of this perspective - the customer is an integral part of the firm's value proposition and marketing [14]. This service-centered view proposes that the customer is always an active participant in the value creation, and is "co-producing" the service with the firm. For S. Radford and S. Sridhar, the positive assumption that greater co-production is both demanded by customers, and will ultimately lead to steadily increasing degrees of participation and customization in the market is problematic [12]. In consequence, instead of assuming that increased participation will lead to positive firm outcomes, it is suggested that firms must identify the appropriate level of customer participation and design service delivery systems that work at this level. The companies must take under consideration not only the process of creating value with co-production actions for itself, but must also be confirmed that the customer segment is satisfied with the same operation. For different co-production activities, various levels of perceived value are possible (fig. 2).

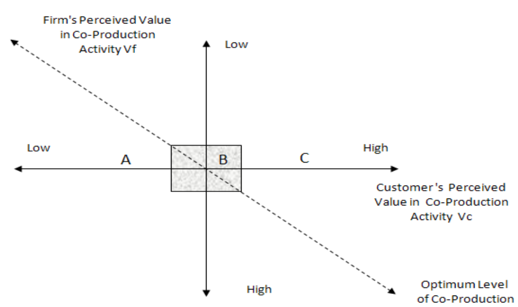

Figure 2. Multiple Co-Production Offering. Source: S. Radford, S. Sridhar: All co-production is not created equal: a value congru-ence approach for examining the degree of co-production, Enhancing Knowledge development in Marketing, 2005 AMA Educators' Proceedings, USA 2005, p.249 and p.248

The analysis of possible dimensions of co-production gives the possibility of formulate the strategic alternatives in aim of adjust the firm co-production offerings. Those offerings can be presented as following: B – this area denotes a segment of customers to whom the firm's offerings are appearing, A – Customers in this segment will either need a lower co production offerings than the firm currently offers, or will need to be encouraged to co-produce more, and C - customers in this segment will either need a higher co-production offerings, or will need to be encouraged to co-produce less. The most promising degree of co-production is represented by the diagonal. To reach this position, the firm has two possibilities. The first is to diminish the expectation of the amount of co-production, accepting that the customer are not interested in higher levels of co-production and try to perceive the value in offering a less co-produced alternative. The second possibility is to increase the value that customers perceive from participation. In fact, customers' engagement in co-production will vary in function of the perceived value of realized activities. As firms increase the level of co-production by offering new, more participative offerings, they must be aware of the impact on customers. Particularly, it needs to be considered in the case of firm new market segments, or in the case of innovation oriented management process. Analyzing innovation activities of German companies, S. Kinkel, G. Lay and J. Wengel confirm that innovation can be more than developing new product innovation [7]. In addition to traditional R&D - based innovation activities, they described the innovative fields of action as; technological modernization of value add processes, introduction of organizational innovations and new business models for complementing the product offer by innovative services. Their observation leads to the assumption that innovation strategy must be conceptualized not only focusing on R&D activities. In some case, technology based competitive advantage is not the key company success factor, because of its fast propagation, international competitors can easily react and offer the product imitation proposition. In this situation, some producers try to enlarge the customer value proposition originated from the new technology and work under the complete sales solutions. That appears as the one of main reasons to assign the innovative dimension not only to product but also to complementary services in way to make offer more adopted to satisfy the market needs. This kind of commercial combination can be also very interesting because it can built over the time the strong relationship with the customer and give to firm the possibility of develop the innovation based value proposition. This definition of innovation can be also hard to imitate for the competitors and leads the firm to differentiate the possessed resources not only on the technological bases. The turnover generated by such services is adequate indicator for the extent to which companies pursue this innovation path. But the needs of make the customer proposition valuable and to minimize the risk of deception suggest the use of appropriated tool to measure the potential value proposition deviation. The minimization of this deviation in case of customer and in the case of the firm will be also the condition of future efficient co-production. The possible form will reflect the way that the firm developed innovation based values are converted into customer perceived values. The confrontation of those two perspectives will be useful for the firm when analyzing the innovations initiatives, particularly in the case of formulating technology strategy of the company as the innovation based differentiation marketing strategy. An example of value perception perspective grid use is given for the case of two different sales solutions (fig.3). Project A – a innovative product service combination is estimated by the firm as high value for customers (A1), but its customer evaluation is low (A2), the circle diameter is its sale amount forecasts established respectively on firm and on customer based sources.

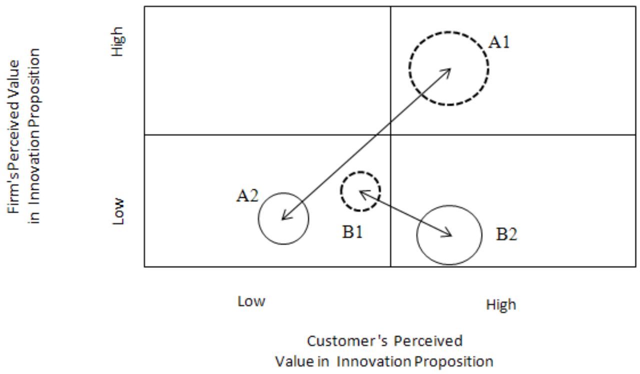

Figure 3. Value perception perspective grid as the value proposition evaluation tool. Source: Own

The Project B can be considered as organization process innovation with firm low value estimation (B1), but its customer notation is quiet different and assigns to it some higher value (B2). The first applications of this tool signalize also the different way of innovation based commercial offer perception - the firm innovation high value propositions in some cases, were perceived by the customer in different way, confirming the importance of customer engagement in very early stage of value proposition formulation process. The Use of presented grid gives to firm the possibility of customer commitment adaptation as the tool of visualization the deviation in value perceptions, significant for the conceptualization of new innovation based sale solution commercialization process. The proposed approach is also giving important indications about the possible dimensions of co-production.

V. Conclusions

The satisfaction of customer need based on innovation based differentiation strategy is one of most promising way to create the value on competitive market. The conceptualization of efficient strategy aiming the investment risk minimization must be funded on customer commitment. The degree of this involvement varies and firstly the customer was widely perceived as the important part of company management process architecture. Than the customer commitment operationalized through the co-production is considered as source of value, becoming important stage of firm value proposition evaluation process with potential value perception contradiction between firm and customer. This potential divergence becoming crucial for innovation based differentiation strategies due to its market uncertainty, becomes an interesting object of analysis resulting in research of unconventional management tools.

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