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1

Introduction

In the age of globalization, China presents a unique setting for organizations. The unprecedented growth of China's economy, which remains the fastest growing in the world, offers significant potential for both Chinese and foreign investors. Today, increased levels of competition in the wake of China's entry into the WTO have resulted in experimentation and risk-taking as ways of doing business in China. Business networking, as a form of social capital, has emerged as a growth strategy in China's emerging market economy. However, the uncertainties and ambiguities prevalent in the Chinese business environment, in particular, in the area of creating of marketing competences and strategic flexibility in the Chinese context, are neither well understood nor effectively negotiated by the international investment community. In addition, the complexities in understanding the Chinese philosophy and Chinese management style have led to the anxieties and hesitation of foreign operators. As to the international investors, China's business environment continues to present many challenges, particularly in how to manage effective business networks and ensure smooth knowledge transfer, especially in international joint venture projects. In the meantime, the Chinese investors are facing even more severe competition, both the internal and external business environment presents to them a double-edged sword with China's access into the WTO. Therefore, the ever-increasing challenging issues in the Chinese business environment have inspired the argument and the philosophy of the current study.

The nature of the study has resulted in the adoption of both the pilot study and the main study approach. Following the successful survey (both firm with 80 respondents and customer with 100 respondents) in Tianjin, a structured main study was undertaken in Beijing, Tianjin and Shenzhen. The main study has secured 187 valid responses from senior managers in companies and 367 valid responses from general

customers. Based on the data collected from China firms (the firm survey) in three big cities, Beijing, Tianjin and Shenzhen, and their customers (the customer survey), several structural equation models (including both mediated model and moderated models) are developed and empirical results show that most of the propositions are strongly supported and the key resource-based determinants such as organizational learning, technological competences, marketing competences, integrative competences and strategic flexibility do have significant impacts on different dimensions of customer-focused performance directly or indirectly. This also has implications as far as creating dynamic capabilities and the possible choices for a firm to strengthen its dynamic capabilities in turbulent environments in China for superior customer-focused performance. By taking a disaggregated approach, results of the structural equation models developed based on the data from the customer survey indicate that among the five service quality-related factors, four of them have significant but differentiated impacts on customer-perceived service quality with reliability as an exception. Furthermore, customer-perceived value has been studied as well. Not only the operationalization of customer-perceived value has been conducted and a valid measurement scale developed in the Chinese context but also results indicate that the majority of the five service-related factors have significant but differentiated effects on each dimension of customer-perceived value (functional value, social value, emotional value and perceived sacrifice) with the impact of reliability on perceived sacrifice as the only exception. In addition, the complex relationship between service quality, customer-perceived value and customer satisfaction has also been explored and tested in this study.

This chapter presents the background briefly and provides the justification of this book in aspects of theoretical significance, methodological significance and practical significance. Then the objectives and the key contributions of this book are summarized. Furthermore, the rationale for the selection of firms in China is provided.

Aims and objectives of the study

This study investigates the concept of customer-focused performance and its key determinants in the perspective of a resource-based theory of a firm. It aims at integrating service marketing literature with that of strategic management by understanding how firms build and leverage distinctive competences, capabilities of organizational learning and strategic flexibility to achieve superior customer-focused performance.

The study attempts to fill some of the gaps in the literature, and aims to define the concept of customer-focused performance, analyse the interactive relationships between its main components and identify the key determinants of customer-focused performance in perspective of a resource-based theory of a firm. Specifically, the objectives of the study are to investigate such research questions as follows:

- To define customer-focused performance, and its key dimensions and to test the interactive relationships among its key dimensions.
- To identify the key resource-based determinants of customer-focused performance and their relationships, especially the relationships among organizational learning, strategic flexibility and core competences.
- To build comprehensive structural equation models for investigating and testing the relationships between the key determinants and customer-focused performance, and uncovering how different competences interact with each other and with environment to impact the specific dimensions of customer-focused performance.
- To establish theoretic framework as to enabling firms build and leverage distinctive competences, capabilities of organizational learning and strategic flexibility to achieve superior customer-focused performance.

Background of the study

On the one hand, concepts such as customer orientation, staying 'close to customer', customer segmentation and niche marketing, customer as co-producer (Wikstrom, 1996), value co-production, critical co-developer of knowledge and competence (Sivula *et al.*, 1997) and co-opting customer knowledge (Gibbert *et al.*, 2001), all point to the much more significant role of customers in business success than ever before. This indicates that the arrival of a new customer-centered era and necessitates inevitably the priority of customer-focused performance. On the other hand, the increasingly dynamic and intensified nature of competition has made the improvement of organizational learning and the development of more effective methods for managing knowledge and other intangible resources a central concern of contemporary strategic management. Consequently, a new approach, the resources-based view of the firm, emphasizes the critical importance to sustainable competitive advantages and performance differentials of invaluable resources and competences such as customer relationship, marketing capabilities, learning culture, and employee skills and

knowledge (Barney, 1991; Teece *et al.*, 1997), has won increasing attention from both academic and practical circles although the traditional industrial organization economists argue that there are a rather deterministic association between market structure and profitability (Mason, 1939).

According to the resource-based view, firms are viewed as bundles of unique resources and the primary sources of performance differentials are the idiosyncratic accumulation of unique and non-imitable resources within firms. Resources are defined as those tangible or intangible assets that are tied semi-permanently to the firm (Maijoor and Witteloostuijn, 1996). Examples of such resources are: brand names, in-house knowledge of technology, skilled personnel, trade contracts, efficient procedures, organizational capabilities, marketing knowledge, etc. (Wernerfelt, 1984). However, not all kinds of resources of firms are equally important and only those that are valuable, rare, non-imitable and non-substitutable may generate sustainable performance differential (Barney, 1991). In order to test the so-called industry effects advocated by researchers in the tradition of the Mason/Bain structure-conduct-performance (SCP) paradigm that attributes differential firm performance to the structure nature of an industry, and the firm assets effects believed by resource-based theorists, several empirical studies have been conducted, and most of them have found that industry effects can only explain about 20 per cent of performance variance. Therefore, it is important for us to focus simultaneously on two things, i.e. servicing customers and leveraging resource-based sources of superior performance, and try to integrate them into an organic system with the former as a starting-point and an end-point at the same time.

In fact, in environments characterized by high-velocity change, accelerating product life cycles, narrowing customer niches, mass customization and technological discontinuities, today's product markets can appear and disappear quickly (D' Aveni, 1994), with traditional product-centered strategies providing little long-term advantage (Christensen, 1998). This has led to renewed efforts to understand how firms can develop dynamic capabilities which enable them to adapt, integrate, and reconfigure their skills and knowledge in order to adapt to a changing business environment. The dynamic process of developing resources and competences has also turned the attention of firms to collective learning (Prahalad and Hamel, 1990), a process through which organizations apply existing knowledge and develop new knowledge that shapes the development of new competences that are necessary in the changing environments (Kogut and Zander, 1992; Henderson and

Cockburn, 1994). Furthermore, this work has highlighted the need for a deeper understanding of how trajectories of knowledge and capabilities develop and how factors such as absorptive capability (Cohen and Levinthal, 1990) and 'lock in' (Dosi, 1988) influence the process of knowledge and capability development. However, up to now, there have been few systematic studies supported by empirical evidence in this field. Furthermore, there has been a strong trend for researchers and managers to try to explain the influential factors of competitive advantage and superior performance from their own perspective and ignore the rationality of views from other streams. Thus, little effort has been made to integrate knowledge management, organizational learning and competence-based competition with empirical investigations and, as a result, little research has been done to explore and examine the interactive relationship between knowledge acquisition, accumulation and sharing, organizational learning, and competence building and leveraging, and their impacts on customer satisfaction, customer-perceived service quality and other dimensions of business performance.

Furthermore, even though almost all researchers agree that firms competing in present and future situations will encounter a dynamic environment in which strategic flexibility and responsiveness will be paramount, few take strategic flexibility into account when they explore or test the links between different factors and firm performance. In addition, in today's turbulent environments, customers are playing an ever more important role in business competition, and many means have been advocated of understanding customer demands from the viewpoint of customers themselves, so that these demands can be translated into business language and actions. However, little progress has been achieved concerning customer-focused performance. Although many studies have been made of business performance, most of which are conducted with overall performance, market performance or new product performance as the focus. Therefore, drawing on a growing body of literature that distinguishes between a firm's products and its resources and capabilities (Snow and Hrebiniak 1980; Hitt and Ireland, 1985; Barney, 1991; Henderson and Cockburn, 1994; Markides and Williamson, 1996), that emphasizes organizational learning (Argyris, 1978, 1990; Senge, 1990), and that pays more attention to customer satisfaction, customer-perceived value and customer-perceived service quality (Gronroos, 1988; Zeithaml *et al.*, 1990; Parasuraman *et al.*, 1991; Anderson and Cockburn, 1994), this book will try to bridge gaps that currently exist in our understanding of business dynamics in turbulent environments and link what strategic management field argues with what service management emphasizes.

How was the study conducted?

The research project aims to investigate key aspects that underpin the creation of marketing competences and strategic flexibility and addresses the crucial issues in creating core competence and strategic flexibility in the turbulent Chinese business environment. The nature of the research has decided that the design concept of the research project has been a combination of both qualitative approach and the quantitative approach. Following the literature review, both a pilot study and a structured survey were designed to be an integral part of the research project. By taking a disaggregated approach, theoretic framework and the structural equation models has developed based on the data from the customer survey through conversation with senior Chinese business executives and a well structured survey in Beijing, Tianjin and Shenzhen, in PRC.

What is the intent of the book?

First and foremost, this book is a highly practical, technically limited, presentation of principles of key resource-based determinants in creating core competences, such as organizational learning, technological competences, marketing competences, integrative competences and strategic flexibility. Furthermore, the distinctiveness of the book lies in analysing turbulent business environments and key resource-based determinants that underpin organizational learning, technological competences, marketing competences, integrative competences and strategic flexibility. This will enable business executives in both the Chinese and international business community to identify the essential ingredients in approaching the Chinese market and in making strategic decision.

To whom is this book directed?

As it is addressed previously, this book has arguably a very wide range of readers. Researchers and academics may find the book interesting and useful because the study has successfully approached a pilot study and a well-structured survey in three major cities in China.

Besides the senior students and academics in the areas of international marketing, strategic management, organizational learning, economics, business administration and international management, will also find this book of value, as it touches a subject of considerable interest to many groups, such as government policymakers, international funding

agencies, and business executives. This book not only suits the business executives in the international joint venture companies, multi-national corporations, but also that of large-middle state-owned enterprises and private operators in China.

Justification of the study

This book is timely and significant for theoretical, methodological and practical reasons as the world looks at China because of its economic expansion – in particular, the business sector, domestically and internationally, has a special sense of China's potential market.

Theoretical significance

With regard to theoretical significance, this book is important to the further development and testing of theories concerned in three ways as follows.

First, it integrates the research in the field of service marketing with that in the field of strategic management, especially those in perspective of a resource-based theory of the firm. Yet, as mentioned before, the literature on service marketing and the resource-based view in strategic management research runs in two parallel streams. Obviously, the lack of linking the resource-based view of the firm in strategic management field with service marketing has greatly limited service marketing's relevance to the growing field of strategic management. Similarly, lack of incorporating the role of service marketing in the context of strategic management studies may both limit our understanding of the roles of strategic resources and capabilities such as organizational learning, core competences and strategic flexibility in the sustaining of superior customer-focused performance and hinder the theory development of service marketing.

Given the importance of strategic resources and competences in service marketing and customer relationship management, some researchers have called for research on marketing capabilities or market-based assets. Along this line of inquiry, this book advances the literature by linking service marketing and the resource-based view of strategic management in a way of exploring the key resource-based determinants of different dimensions of customer-focused performance and investigating their interactive relationships. Thus exploring the dynamic relationships concerned provides the needed theoretical and empirical evidence for linking service-marketing theory with strategic management literature, which may greatly broaden the relevance of service-marketing theory.

Secondly, the book clearly defines the dimensions of customer-focused performance and constituents of the key resource-based determinants, especially the constituents of core competences. On the one hand, in spite of the extensive studies of resources and competences, much of the work has been descriptive in nature and relatively few empirical studies have been conducted. More specifically, strategy researchers have not succeeded in establishing more stable, immutable conceptualizations of core competences, organizational learning and strategic flexibility because of the lack of conceptual refinement and empirical tests. The lack of conceptual refinement has also lowered the ability of strategic resources and competences variables to explain variations in firm performance, especially in customer-focused performance. On the other hand, although extant studies in service marketing on customer-perceived service quality, customer-perceived value, customer-perceived sacrifice or customer satisfaction have been becoming more and more fruitful, less has been done systematically about the interrelationships between them, no general agreements have been arrived at about the conceptualizations and measurements except customer-perceived service quality, and few have taken them together and tried to integrate them into one comprehensive mode to reflect the superiority of customer-focused performance. For example, extant studies have never articulated well on which kinds of competences firms should focus to achieve superiority in some dimensions of customer-focused performance, and how different competences effectively impact different dimensions of customer-focused performance. Therefore, attempts to investigate customer-focused performance and its key resource-based determinants may not only broaden the focus of studies of service marketing and customer relationship management but also enhance our understanding of firm development and competitiveness building and leveraging, and thus enrich the strategic management theory.

Thirdly, previous studies on either the resource-based view of the firm or service marketing have been conducted mainly within the context of the well-established market economies and some highly related research findings have been achieved. In theory development and testing, however, these findings cannot be taken for granted excluding decisive influences of the context to which they may be applied. Firms in a transitional economy may differ from their western counterparts in many dimensions. A transitional economy refers to an economic situation where the economy is transiting from a planning oriented to a market oriented and both market power and non-market power play roles simultaneously in coordinating resources allocation. The context of this book will reinforce attempts to generalize the literature on service

marketing and the resource-based view of strategic management to a transitional economy. As indicated above, environmental characteristics in a transitional economy may lead the firms there to adopt different strategies and take different actions from their counterparts in a market economy. Yet, empirical studies in this stream are particularly scarce. This book represents an initiation to investigate the customer-focused performance and its key resource-based determinants in a transitional economy.

The methodological significance

The methodological significance of this book is related to the structural equation model building and the moderating effect testing by using Partial Least Square method. On the one hand, according to Hair *et al.* (1998), SEM is characterized by its ability to estimate multiple and inter-related dependent relationships simultaneously, and measure unobservable concepts in these relationships uncontaminated by measurement error. On the other hand, as one of the estimation techniques for structural equation model (SEM), although the PLS method is not as popular as the maximum likelihood (ML) based covariance structure analysis method, it does provide 'a way to avoid problems of improper solutions and factor indeterminacy as well as the violations of distributional assumptions' (Fornell and Cha, 1994). Furthermore, as for the testing of moderator effects, although traditional techniques such as analysis of variance (ANOVA, MANOVA, MANCOVA, ANCOVA) or moderated multiple regression (MMR) are frequently used, however, they may not be able to detect such interaction effects under conditions of measurement errors. For example, according to what has been concluded by Chin, *et al.* (1996, 2003), studies using analysis of variance approaches fail to report effect size estimates on the one hand while the regression and path analysis techniques, which do provide beta path coefficients, have few significant terms, small effect sizes and low statistical power, which can be overcome by the PLS method. Moreover, the usage of two different sources of data and making useful comparisons are also of methodological significance.

The practical significance

The book is also of practical significance. Both strategy and service marketing practitioners working in firms are at a disadvantage due to the lack of research and theory to support their contributions to their firms. This book provides empirical understanding of what kinds

of strategic resources and competences firms actually accumulate, and how these valuable resources help firms effectively adapt to external environments and achieve superior customer-focused performance and distinctive advantages. For those foreign firms that attempt to enter the China market, this book provides them much-needed evidence for learning how the Chinese firms compete and achieve success in a transitional economy, and results of the book also provide guidelines for foreign firms to enter this market. Finally, this book will benefit public policymaking and contribute to the national economic development in the long run.

Contributions to research

As described above, the book not only tries to identify the significance of customer-focused performance and its key determinants but also aims to find and test the dynamic relationships between them. Accordingly, the major contributions can be summarized as follows.

First, it connects the latest research findings in two different fields of management: service management and strategic management. Up to now, even though important conclusions have been made in each field, less efforts have been paid to connect them together empirically with the study of Aung and Heeler (2001) as an exception. Although some empirical research exists trying to establish the relationship between competences and performance, they mainly focus on the overall performance, market performance or new product development performance. In fact, the resource-based view in strategic management lays solid and sustainable foundations as well for achieving superior customer-focused performance. Thus in this research, it is expected that a linkage between such strategic resources as competences and strategic flexibility, and customer-focused performance will be built conceptually and empirically. For example, the mechanisms for organizational learning, technological competences, marketing competences, integrative competences and strategic flexibility to contribute to different dimensions of superior customer-focused performance, i.e. customer-perceived service quality, customer satisfaction and customer-perceived value, will be discussed and tested in this study.

Secondly, defining and identifying the key components and dynamics of customer-focused performance and its key determinants is one of the most innovative exploratory studies in related fields. Even though more and more agreements have been made about the important role of customers in business competition, little has been done systematically about customer-focused performance, especially the performance

evaluated by customers in the eyes of themselves, not the firm. In this book, the connotation of customer-focused performance, a performance system directly evaluated by customers outside the firms, will be analysed and its key dimensions will be identified. Based on the extensive literature review and in-depth focus group discussions, the measurement system will be developed and then the interactive relationships among the key dimensions will be discussed and tested systematically. Furthermore, in this research, much attention will be paid to the key dimensions of customer-perceived value as well so as to deepen our understanding of customer-perceived value and leverage it to build sustainable competitive advantages.

Thirdly, identifying and testing the different roles of marketing competences, technological competences and integrative competences in enhancing strategic flexibility and achieving superior performance is still a direction to be studied further. A number of studies have been undertaken of resources and competences in different perspectives up to now, some of which are empirical, however, it is too difficult to find any empirical findings specifying and testing the different roles and unique significance of these three broad constituents of core competences. In this research, it is expected that reliable and valid scales will be developed based on extant research work and in-depth interviews with senior managers in China. And then their proposed roles in core competences and unique contributions to superior customer-focused performance will be tested based on evidence from China.

Furthermore, analysing and discussing the special contribution of organizational learning to core competences and customer-focused performance is another point worthy of empirical investigations. It is easy for us to find many qualitative studies for organizational learning, however, more empirical studies are needed to propel its development further. Thus the impacts of the three dimensions of learning orientation, i.e. commitment, shared vision and open-mindedness, on core competences will be examined and tested conceptually and empirically in this book.

Finally, discussing the value of strategic flexibility to different dimensions of superior customer-focused performance is very helpful to enrich studies on strategic flexibility and useful for senior managers to understand strategic flexibility and leverage it more effectively in today's turbulent environments. Nowadays, although strategic flexibility has become one of the focal point for both academics and practitioners and some qualitative researches have been emerging rapidly, few empirical studies can be found and no research up to now has been done to link strategic flexibility to different dimensions

of customer-focused performance such as customer-perceived quality, customer-perceived value and customer satisfaction.

Rationale for the selection of firms in China

In this book, data are collected from firms in China, a country that is undergoing reforms from a centrally planning to a market economy. There are several reasons for this selection. The first is that investigating customer-focused performance and its key resource-based determinants within the context of a transitional economy is more critical than doing that within a market economy. The rationale for this proposition is that, on the one hand, market power is growing but the market infrastructure has not been well developed in a transitional economy (Nee, 1992; Peng and Health, 1996). Hence, application of marketing knowledge and emphasis on strategic resources and competences are rather limited. However, in a transitional economy, where marketing skills/resources are less available, firms that have such strategic resources and deploy them effectively are more likely to build up sustained differential advantages to achieve superior customer-focused performance and accordingly, superior financial performance. In fact, researchers have found that strategic resources and competences such as marketing skills/resources are more critical for a firm's performance in a transitional economy than in a market economy (Calantone *et al.*, 1996). Thus, it is important to understand the mechanisms through which a firm build and leverage competences and resources to deal with environmental situations resulting from market transition. On the other hand, comparatively speaking, less related knowledge has been accumulated to provide special guidance for the developing worlds than that for developed countries although more people belong to the former. So it is of significance to make studies of the specific phenomenon in developing countries and develop more knowledge for this majority of population in the world (Aung and Heeler, 2001). In addition, this book conducted within a context of the transitional economy in China can help to redress the balance of empirical work that is largely based on the North American and European data sets. As Shenkar and von Glinow (1994) point out, China is an ideal site for testing the generalizability of western organizational and management theories. Given China's distinctive culture, economic and political systems, particularly the size of its population, social and managerial theories must explore their implications in China to be complete. Compared with other transitional economies in Eastern Europe and their Post-Soviet republics, China's transitional process is more successful as far as the stable and incremental nature of reforms are concerned.

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