Journal of Purchasing & Supply Management 18 (2012) 68–75

Contents lists available at SciVerse ScienceDirect

Journal of Purchasing & Supply Management

journal homepage: www.elsevier.com/locate/pursup

The underlying potential of supply management in value creation

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ARTICLE INFO

Available online 2 June 2012

Keywords:
Value creation
Supply management
Value net
Collaboration

ABSTRACT

This study discusses the value-creation potential of supply management in firms, highlighting the significance of buyer–supplier collaboration, as well as resources and capabilities in the process. It is a conceptual study that builds on the theoretical basis of the resource-based view and the value net approach. Given the critical role of supply management in generating value the strategic emphasis in future should be on triple value creation. It is concluded that this cannot be achieved by focusing only on dyadic relationships or relationships in chains, and that supply relations should be viewed in a wider network context.

1. Introduction

Purchasing and supply management has traditionally been a support function in firms, characterized by transactional buying and short-term supplier relationships. Given the increasing demands of end customers, however, there have been pronounced developments in buying activities and the management of supplier relationships. Several previous studies (see Carr and Smeltzer, 1997, 1999a; Cousins and Spekman, 2003; Ellram and Carr, 1994; Kocabasoglu and Suresh, 2006; Rozemeijer, van Weele and Weggeman, 2003; Zheng et al., 2007) acknowledge the strategic function of supply management in enhancing competitiveness. Strategic supply management has been found to correlate highly with the firm's competitive advantage and business performance (Yeung, 2008). Furthermore, given that purchases comprise the largest single expenditure item in most firms, the ability to control costs is critical to their financial success (Zsidisin et al., 2003). Supply management has clearly become an increasingly influential success factor, and there have been significant improvements in performance along with the recognition of its strategic nature.

Recent studies on strategic supply management approach the discussion from the perspective of value creation in business. To the extent that supply management is responsible for finding the most valuable and appropriate suppliers as well as for supplying raw materials and products efficiently, its significance in value creation is substantial. If it is strategic and efficient, it can generate many benefits and cost savings, thereby creating more value. Value is therefore increasingly relevant as a concept from this perspective (Lindgreen and Wynstra, 2005). Moreover, the enhanced understanding of value that emanates from the supplier network (Harland et al., 2004) and the fact that unique value can be created when companies collaborate and combine their competences and capabilities (Amit and Zott, 2001; Borys and Jemison, 1989; Bovet and Martha, 2000; Harrison and Håkansson, 2006), have boosted research on the connections between supply management and value creation.

In this world of business networks the traditional view of value creation as based on value chains has changed and the focus is increasingly on value-creating networks. The value net model was developed to facilitate the analysis, description and study of value-creating systems, and takes activities rather than companies as the key elements of strategic analysis (Parolini, 1999). However, research on value nets has rarely been connected to studies on supply management even though the current business environment clearly requires companies to create value through their supply activities and supplier networks, and to create it more efficiently. As Zhang and Chen (2008) found, value co-creation with suppliers positively influences the buying firm's customization and service capability, and thus may highlight new sources of competitive advantage.

Given the increasing role of supplier networks and supply management in many firms, and the consequent search for new business models through which value can be created and high levels of success and performance achieved, this conceptual study focuses on the potential of supply management in value creation. The objective of this paper is to describe and clarify the value-creation possibilities that are inherent in supply management, and to highlight the significance of collaboration, resources and capabilities as critical parts of the process. We develop a conceptual framework that connects supply management, value creation and firm performance, and competitive advantage. First, however, we need to establish the theoretical foundation, which lies in the resource-based view and the value net approach.

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http://dx.doi.org/10.1016/j.pursup.2012.04.006

2. The resource-based view

With its origins in the work of Penrose (1959), the resource-based view of the firm (RBV) depicts firms as collections or bundles of resources, and growth depends on how these resources are exploited. It is a theoretical framework that enhances understanding of how competitive advantage within firms is achieved, and how it could be sustained over time through the acquisition and control of resources (Eisenhardt and Martin, 2000). Competitive advantage, in turn, results when a firm implements a value-creating strategy that is not simultaneously being implemented by any current or potential competitors (Barney, 1991). According to Amit and Schoemaker (1993), firm-specific resources and capabilities are crucial in explaining performance, and the type, magnitude and nature of resources and capabilities are significant determinants of the firm's profitability. As Stalk et al. (1992, p. 62) argue, "competitive success depends on transforming a company's key processes into strategic capabilities that consistently provide superior value".

Amit and Schoemaker (1993, p. 35) define resources as "stocks of available factors that are owned or controlled by the firm", and according to Grant (1991, p. 118), "resources are inputs into the production process". Teece et al. (1997, p. 516) add that "resources are firm-specific assets that are difficult if not impossible to imitate", and use the term firm-specific asset as a synonym for resource. Furthermore, Wernerfelt (1984, p. 172) argues that a resource refers to "anything that could be thought of as a strength or weakness of a firm". Thus, resources comprise know-how that can be traded, financial and physical assets, and human capital (Amit and Schoemaker, 1993). Barney (1991) similarly distinguishes between physical capital (the physical technology used, plant and equipment, geographical location, access to raw materials), human capital (the training, experience, judgment, intelligence, relationships and insight of individuals in the firm) and organizational capital (the formal reporting structure, formal and informal planning, controlling and coordinating systems, and informal relations), all of which can be used to implement value-creating strategies.

The basic premise of the RBV is that competitive advantage comes from having resources that create value and are unique. Value is generated from the productive usage and combination of complementary and specialized resources and capabilities (Amit and Zott, 2001). Hence, the internal intangible and tangible assets of a firm are the main enablers of value creation and may be sources of value. Capability and knowing how to utilize external resources may also be enablers of value creation (Medcof, 2001). As Gulati et al. (2000) state, from the perspective of the RBV, a major source of value-generating resources lies in networks of relationships.

3. Value and value creation

The concept of value can be understood in various ways. Walter et al. (2001), for example, describe it as a trade-off between benefits and sacrifices. Forsström (2005), in turn, stresses the importance of distinguishing between value and value creation: whereas perceived value is a subjective assessment of the trade-off between benefits and sacrifices, value creation is the process through which the participants make use of each other's resources in order to generate value. In other words, value creation could be defined as "the process by which the capabilities of the partners are combined so that the competitive advantage of either the hybrid or one or more of the parties is improved" (Borys and Jemison, 1989, p. 241). Forsström (2005) further argues that there are three different perspectives from which value can be analysed: (i) the value of an offering (measured in monetary units), (ii) the value of a relationship (not only monetary value but also intangible issues), and (iii) the value created in a relationship. According to Allee (2003), one of the major shifts on the strategic level involves rethinking value to include both monetary and intangible aspects.

Value creation could also be considered from several perspectives. Value capture refers to the allocation of customer payments to a firm (Priem, 2007), which is in line with the Porterian view of competitive forces (Porter, 1985). In other words, the company is struggling against environmental forces and is positioning its competitiveness in relation to other players in the industry. Secondly, value may be co-created by the customer and the firm (buyer and supplier) (Prahalad and Ramaswamy, 2004), and firms should move away from firm- and product-centric thinking towards the provision of individualized goods and services to interconnected customers (Johannessen and Olsen, 2010). Thirdly, from the consumer's perspective it could be said that value is established by the end customer's valuation (Priem, 2007; Johannessen and Olsen, 2010). In sum, therefore, value is generated from three different perspectives: the ability to compete and respond to environmental challenges in the industry, the ability to exploit relational capabilities, and the ability to understand and respond to customer.

The concept of value creation has its origins in several streams of business research. The value-creation ability of networks of firms has been under scrutiny for decades, and thus is not a new phenomenon. The notion of value arising from networks can be traced back to the ideas of Marshall, who observed that "access to external economies depends partly on situation" (Marshall (1997), p. 257), meaning that firms in the same industry located close together in the same area could generate economies of scale that are external to the firm through co-location. Studies from the 1950s raised this issue in the context of industrial districts and centralized industries: it was found that innovative firms had above-average rates of productivity growth, or an increasing market share. Combined, these growth poles (Perroux (1955)) formed networks in which learning and collaboration were distributed in order to generate knowledge among the members. Network growth expands the pool of skilled labor, facilitates the development of vertically linked activities in a supply chain, and enables knowledge transfer to other firms (Salmi et al., 2001). However, the agglomeration of firms creating today's value network is based on collaboration and knowledge, and the location factor is less significant. Furthermore, agglomerations of knowledge and industrial districts are changing into service clusters in which the value comprises experiences that engage customers or consumers in a personal way (Hsieh et al., 2011).

According to comprehensive reviews of the literature on value in business markets conducted by Lindgreen and Wynstra (2005) and Lindgreen et al. (2012), there are two different levels of analysis, the value of goods and services and the value of buyer–supplier relationships. The marketing literature in particular emphasizes that value accumulates through relational more than transactional exchange (Lindgreen et al., 2012). In sum, it seems that research on value creation has been following at least three main streams for decades. Fig. 1 identifies these streams and gives some basic points of reference for each one.

4. From value chains to value nets

According to Parolini (1999), a value-creating system (VCS) is a set of activities that create value for consumers. Various resources are used in carrying out these activities, linked by different kinds of flows. Value-creating systems contain economic players who may be involved in more than one VCS. The traditional approach