

# Customer-Driven SMEs Co-Operation: A Service Dominant Logic Perspective

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**Abstract:** This paper argues that service dominant logic (SDL) can help Small and Medium-sized Enterprises (SMEs) bridge the gap between co-operation performance and customer satisfaction. We propose a customer-driven SMEs co-operation conceptual model that identifies the relationships among SMEs, customers and co-operation performance according to SDL. We also propose a set of SMEs co-operation performance evaluation criteria within SDL. A case scenario is then used to demonstrate the contributions of the model. We believe that the model and the performance criteria can inspire further research on SMEs co-operation in order to achieve the maximized customer satisfaction in terms of appropriate design of service systems.

**Keywords:** Service Dominant Logic, Small and Medium Enterprises (SMEs), Co-Operation, Service System

## 1. Introduction

Small and Medium-sized Enterprise (SME) is an important element in globe economic environment. European Union (EU) defines (European Commission, 2005) SMEs according to staff headcount, annual turnover, and annual balance sheet. An enterprise has no more than 250 employees and less than 50 million Euros of annual turnover or 43 million Euros of annual balance sheet; it can be viewed as a medium-sized Enterprise. A small-sized Enterprise then has even fewer than 50 employees and 10 million Euros of annual turnover and balance sheet. EU's definition accordingly shows that SMEs have limited financial and human resources. They can't invest as many resources as large enterprises in marketing or information technologies.

For competing with large enterprises, co-operation is an important strategy for SMEs to survive by overcoming the resources, capabilities and financial disadvantages and sharing risk with partners because SMEs have fewer assets and less market than large enterprises (Merrifield, 2007)(Lu & Beamish, 2001). Relationships between co-operation SMEs can be bilateral or multilateral, horizontal or vertical. In recent years, co-operation involving multiple partners are increasing (Varamäki & Vesalainen, 2003) because complex alliance network and cluster has better performance in resource access and operation cost reduction (Navickas & Malakauskaite, 2009). Therefore, formation of SMEs co-operation has been evolving from value-chain to value-network relationship, or even clusterization in their own locations (OECD, 2008a). In addition, SMEs have more flexibility than large enterprises in adapting themselves to accommodate the personalized needs of customers (i.e. customers can have an active role

to effect the SMEs co-operation) (OECD, 2008b). Co-operation can help SMEs discover and share complementary resources, expend economics scale to reduce transaction cost and collaborate new products or services by their own capabilities and knowledge (Das & Teng, 2000)(Koka & Prescott, 2002) (Lin et. al, 2009).

Moreover, Ireland (2002) extensively analyzed the important views that would impact the co-operation performance and identified four core views - the resource-based view, transaction-cost view, knowledge-based view and social network theory between enterprises (Ireland et. al, 2002). However, we argue this kind of performance evaluation is close to goods-dominant logic (GDL) (Vargo & Lushch, 2004) which emphasizes on the concept of value-in-exchange (i.e. units of output are products or services) and the performance of co-operation is determined by SMEs according to the aforementioned different views. For example, a coffee shop serves afternoon tea for customers. It is not necessary to bake cakes by the coffee shop. Instead, the shop can cooperate with a bakery store to acquire lower prices of cakes, but customers might not prefer the cakes going with their afternoon tea. This kind of co-operation between SMEs is formed in GDL for getting more resources such as complementary or low cost products or services. In other words, the progression of GDL co-operation has been concentrated more on activities between business and business.

With the changing role of customers in SMEs co-operation, in our opinion, the purpose of co-operation would be inevitably influenced by customers according to reports of OECD (OECD, 2008b). Hence, the performance evaluation of co-operation can not consider only SMEs

because customers participate in the value creation process during co-operation in this situation. Compared to GDL, service-dominant logic (SDL) (Vargo & Lushch, 2004) defined value based on value-in-use (i.e. value being co-created by the customers in the dynamic consumption process of the service).

If SMEs form co-operation from the SDL perspective, customer's needs and reactions in the process need to be regarded when forming and evaluating a co-operation. Taking the example of the coffee shop, within SDL the co-operation with a bakery store would consider whether the bakery produces the special cakes liked by the customers who can also feedback their opinions to both the coffee shop and the bakery store for future service improvement. In other words, customer satisfaction for the cakes would be included in evaluating co-operation performance given the coffee shop co-operates with the bakery store.

This study aims to propose a conceptual model for conceptualizing what SDL can help SMEs co-operation from the performance perspective. The objective of this model is: (1) to identify the relationship among SMEs, customers, co-operation performance and customer satisfaction within SDL; (2) to compare the performance differences between GDL co-operation and SDL co-operation for SMEs; (3) To imply the directions of future research on SMEs co-operation to achieve the maximized customer satisfaction (or to reduce the co-operation risk by understanding the extent to which the customer would value the co-operation).

In section 2, we introduce different aspects of co-operation performance evaluation and the possible change occurring to the co-operation performance evaluation within SDL. The conceptual model of customer-driven SME co-operation is proposed in section 3 and we also use a scenario to explain the conceptual model in section 4. Section 5 then provide some implications for the design of service systems for customer-driven SMEs co-operation. Finally, the conclusion and further research discussion are provided in section 6.

## 2. Literature Review

Co-operation is a way for enterprises that collaborate together to achieve better performance by sharing resource and capabilities (Singh, 1997)(Goerzen, 2007). The degree of performance improvement is related to co-operation success (Ireland et. al, 2002), and obtaining resources and developing capabilities for higher performance are the main purposes of co-operation. For this reason, we discuss different aspects of performance evaluation in this section including what kind of resources should be obtained in

co-operation from the resource-based view (RBV), what benefit co-operation can receive by sharing resource and capabilities from the transaction cost economics view (TCE), what type of partners can be found to acquire the desired resources and capabilities from the social network view, and how to develop the needed capabilities from the knowledge-based view.

In the resource-based view (RBV), it suggests that enterprises can choose partners with owning complementary or desired resources and alliance with them for achieving complete advantage (Das & Teng, 2000) (Mitsuhashi & Greve, 2009). Transaction cost economics (TCE), in contrast with RBV, focuses on the transaction cost and minimum production cost. Co-operation between enterprises can be viewed as a semi-internal organization structure and have lower resources exchange cost than in external environments (Das & Teng, 2000). The degree of transaction cost reduction is affected by market efficiency and trust in partnerships (Goerzen, 2007). Therefore, higher performance of co-operation based on TCE reflects from higher communication effectiveness to low communication cost among co-operation partners.

A social network describes actors and relationships among actors (Scott, 2000). It can also be applied to enterprise co-operation. Relationships in the enterprise co-operation provide social capital which can be related to co-operation success (Ireland et. al, 2002). Quantity and quality of information which social capital contains influence on enterprise performance because they are helpful in business resources network construction such as technology, knowledge or capabilities (Koka & Prescott, 2002). Besides, knowledge exchange happens in enterprise co-operation, too. Enterprises learn partners' capabilities or knowledge during co-operation and apply them to create new resources and understand customers, competitors to keep competitive advantage. Therefore, the efficiency of knowledge transfer from the knowledge-base view also relates to the co-operation performance (Ireland et. al, 2002).

The aforementioned four different views cover both tangible and intangible aspects of assets including resources, relationships, capabilities and financial cost in enterprises. Resource complementary, transaction cost reduction, social capital or partner capabilities have been used to evaluate co-operation performance.

In GDL, operand resources like material to manufacturing products are emphasized. Enterprises form a supply chain to secure resource acquisition and reduce transaction cost at the same time. Social capital from partners is used to discover or obtain more operand

resources. But better resource acquisition from better B2B relationships doesn't guarantee more customer value provision owing to customer value is regarded solely from the benefits of resource utilization (Lusch et. al, 2008). In other words, high co-operation performance within GDL might indicate that enterprise can provide high B2B value, but its relation to B2C value is weak because there is little customer involvement in co-operation formation and considerations in co-operation evaluation.

In contrast, within SDL, customers determine customer value that enterprises propose and the B2B value is subsequently decided by B2C value (Basole & Rouse, 2008). Figure 1 illustrates the relationship between B2B and B2C value. Therefore, for SMEs that have fewer resources and capital than large enterprises, it is important for them to reduce the co-operation risk by understanding how much customer value that the co-operation can provide and achieve the maximized customer satisfaction.

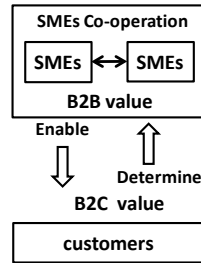


Figure1 Relationship between B2B and B2C value

Customer-driven co-operation among SMEs implies that SMEs understand customers' needs and then proposes new customer value as the goal of co-operation. After the goal is determined, partners are selected by whether their resources can be integrated or their capabilities and relationships including B2C part can help the value co-creation process within the co-operation. So does the co-operation evaluation that would be also different within SDL and they will be discussed in the next section.

### 3. Conceptual Model

In introduction section, we use the coffee shop example for describing non-customer driven and customer driven SME co-operation. In GDL, co-operation among SMEs starts in setting co-operation goals and selecting partners. The performance of co-operation can be measured from the four aspects as mentioned in Section 2 that would effect the SMEs co-operation willingness in accord with the variety of different SMEs business context. For instance, if the bakery store can steadily supply cheaper cakes which are complementary resource to the coffee shop than others and the coffee shop can also buy milk with a lower price from the supplier of the bakery store and learn how to bake cake, the co-operation performance seems wealthy to maintain. However, if the coffee shop sold another bakery store's cakes for a month and found that customers had more satisfaction with new partner's cake, should the co-operation between coffee shop and original bakery store continue because of a higher performance within GDL?

This question may be hard to determine within GDL because GDL evaluates the co-operation performance based on the exchange resources or capabilities, and has fewer considerations after the exchanges. In other words, customer satisfaction is an indicator outside the B2B relationship for evaluating the co-operation performance within GDL. This paper intends to extend this co-operation relationship in terms of relating the co-operation formation, evaluation and performance outcome to customer satisfaction, customers, customers trust based on SDL. Figure 2 then illustrates this conceptual model which identifies the required relationships among SMEs, customers, co-operation goals and its performance.

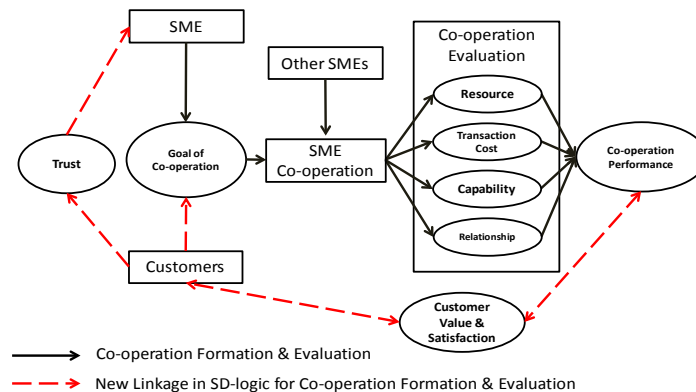


Figure 2 Conceptual model of customer-driven SMEs co-operation

In Figure 2, SMEs find their co-operation goals from customers by using their capabilities or knowledge and then select suitable partners for co-operation. Performance evaluation of co-operation would be different within SDL in comparison with that within GDL in terms of linking with customer satisfaction in order to create customer value. The customers subsequently gain customer value which would be regarded as an outcome of the co-operation performance. At last, SMEs review co-operation performance and learn new knowledge from the feedback of customer experiences. The degree of customer trust to SMEs would also be updated based on customer satisfaction that would influence the social capital of SMEs. Table 1 then shows the comparison of the co-operation performance evaluation between SDL and GDL from different aspects (represented with different focus of questions to ask).

Table 1 Comparing SMEs co-operation performance evaluation between GDL and SDL

Aspect	Performance evaluation	
	GDL	SDL
Goal	From SMEs	From customers and SMEs
Resource Exchange	Can the co-operation get more complementary resource for competitive advantage?	Can the co-operation get more complementary resource for achieving the co-operation goals?
Transaction Cost reduction	Can the co-operation extend the economics scale to lower transaction between B2B?	Can the co-operation : -Lower transaction between B2B -Reduce communication cost for customers to facilitate customer feedback
Relationship	Can the co-operation gain more social capital from partners' business relationship?	Can the co-operation gain more social capital from both partners' business and customer relationship?
Capabilities	Can the co-operation extend our	Can the co-operation extend capability for

	capability for competitive advantage?	providing more choices to achieve maximized customer satisfaction?
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From the previous studies as mentioned in the literature review, co-operation success is influenced by co-operation performance. Based on our conceptual model, we propose the change of the performance evaluation criteria required within SDL as specified in Table 1. First, from the resources aspect, complementary resources are used for achieving goals from customers instead of for business competitive advantage. This is because the usage of resources should result in benefits to SMEs, and the end benefits are determined by customers within SDL. Secondly, for transaction cost reduction, we focus on not only extending economics scale to lower the transaction costs between B2B, but also lowering the communication cost to encourage feedback from customers within the value co-creation dynamic consumption process of the service (i.e. the SDL context). Thirdly, partners' customer relationships are also considered for understanding partners' knowledge and reputation in customers. Finally, similar to the reason of resource aspect, the purpose of obtaining new capabilities for SMEs is to create more services for customers. The evaluation from the capability aspect can be extended to provide more choices for increasing customer satisfaction.

In sum, a sustainable SMEs co-operation based on high co-operation performance can be characterized as: (1) having knowledge or capabilities to design co-operation goal for customers, (2) sharing resources and capabilities for achieving the goal and creating a diversity of new choices for customers (3) establishing effective channels to communicate with customers, and gathering customer feedback.

#### 4. Case Scenario

□ Tourism is a growing industry since 1996. Among all Travel & Tourism consumption, personal Travel & Tourism such as lodging, traffic, and other entertainment services has been the largest part of total business demand (WTTC, 2009). Issues on tourism innovation, economic measurement of service, internationalization of SMEs and culture in making regions/areas more attractive was pointed out by OECD Tourism Committee (OECD, 2008). The reports from OECD have demonstrated that SMEs demand the cooperation between tourism SMEs in the particular context of local clusters. SMEs may not be benefiting from the trend of globalization due to lack of abilities on service innovation and ICT adoption, although they have great

advantage on satisfying the specific needs of customers than Multinational Enterprise (MNEs) in the experience economy era.

In tourism ecosystem nowadays, tourism SMEs which co-operate with travel agencies and MNEs serve customers in the frontline, but they do not have enough bargaining power on profit distribution. However, apart from providing unique customer experience, low cost, high flexibility, high local knowledge and culture make tourism SMEs become an important role in tourism value network especially for personal tourism. Therefore, the potential niches for tourism SMEs in regional tourism appear high.

Here is a scenario about co-operation of regional tourism SMEs. For an owner of farmstead co-operated with a travel agency in the past, although the travel agency provided a stably customer source and had good marketing abilities, the farm village could only earn limited profit. Therefore, he (Farmstead SME) decided to engage co-operation with other regional tourism SMEs on his own. In the beginning, he made his first co-operation with a small restaurant and hoped to cut food cost from its low-price resource and capabilities. However, foods that the restaurant provided were all fried foods like instant foods in big cities. Customer didn't like them and the total income from selling foods was down, although they were cheaper than before. After the first co-operation failure, he found that customers came to their village to get the feeling of the country life. Based on this needs observed from customers, he designed the second co-operation goal as "a tour for customers feeling like "grandmother's farmstead" according to his experiences. In this time, he selected partners who retained the traditional culture and service activities which corresponded to the co-operation goal from customers, such as a farmer providing a cattle car service when farm fallow and a small restaurant provided customers with the experiences of the traditional kiln BBQ. This co-operation empowered the farmstead to provide more diversity of services than before. Most of elder customers could recall their nostalgic memory when living in a village in the past and younger customers had a novelty experience for the grandmother's farmstead-like tour. The resource combination successfully achieved the goal and the co-operation reduced customers' cost for searching ideal services. The co-operation could also lead to the sharing of customers' complaints and the integration of their capabilities for improving the services. Customer satisfaction was accordingly increased. In addition, the owner of farmstead was also suggested by customers to provide traditional Chinese tea which led to collaboration with his friend of a small restaurant owner,

and this cooperation further expanded his customer segment to retired people and won more trust from customers. With the high customer satisfaction from the second co-operation, more regional SMEs would like to join another co-operation program initiated by the farmstead. Also, it has been more tourism SMEs in the village that were willing to cooperate to create a diversity of services through their co-operation. In the end, the farmstead and the whole village developed their unique region features, and the features would keep changing to satisfy customer needs.

## **5. Implementation of Service Systems for Customer-Driven SMEs Co-Operation**

To realize customer-driven SMEs co-operation, service systems can be appropriately designed so as to facilitate SMEs co-operation based on the understanding of the customer-driven co-operation performance evaluation criteria.

Taking the tourism service system example of the case scenario, the service system design for customer-driven SMEs co-operation can involve customer needs discovery and modeling, partners selection for SMEs co-operation, SMEs co-operation feasibility assessment and SMEs co-operation performance evaluation based on the four performance views. For instance, to facilitate customers to search for tourism service providers they emotionally aspire for and then express their needs, the modeling of the customers' needs and wants in terms of some imaging services capable of representing and processing the emotional desire can be developed. E.g., customers can discover "exciting trips" that appropriate tourism service providers can offer the emotionally exciting elements in destinations based on the analytically computed images (i.e., content, context, events, stories, *etc.*) instead of merely using the traditional way of keywords to do the search. SMEs which join the service system (i.e., a service platform) can also understand the trends of customer needs according to customers' search activities (i.e., wanted image changes for service providers) besides their own resources/capabilities before setting up their SMEs co-operation goals. After SMEs identify the co-operation goals, the partner search and selection mechanism could be designed to suggest the unique partners required to build the niche images for SMEs. Decision support for partner selection covers the resource/capability issues for achieving co-operation goals and high customer satisfaction, transaction cost reduction among the partners and customers, and improved relationships based on the past reputation from partner businesses and customers. The co-operation feasibility with the selected partners results in

the rating of these four aspects. SMEs can choose most suitable partners to cooperate. Finally, based on the feedback mechanism from both customers and SMEs cooperators, the co-operation performance improvement can be identified and the co-operation willingness tailored to high or low performance SMEs cooperators can also be provided. In short, this example showcases how a service system can be possibly designed in order to support the customer-driven SMEs cooperation. We hope this example can inspire a slew of new designs of service systems aiming at helping SMEs achieve the maximized customer satisfaction through the concepts of customer-driven SMEs co-operation.

## 6. Conclusion

In this paper, we present a conceptual model to discuss the customer-driven SMEs co-operation within SDL and extend the co-operation processes from merely B2B relations to considering both B2B and B2C relations. The conceptual model relates SMEs co-operation performance to customers and their customer satisfaction in order to ensure the delivery of values appreciated by customers. We also propose the co-operation performance evaluation criteria based on SDL. Besides obtaining the complementary resources or transaction cost reduction, SMEs should understand who need their co-operation and what kind of co-operation services should be provided. By delivering B2C value which customers need, the B2B value in SMEs co-operation would grow accordingly. As a result, SMEs and customers can establish a value co-creation ecosystem for maintaining competitive advantage.

It is important for SMEs to understand the mindset change from GDL to SDL in their co-operation. SMEs need to consider the benefit customers will receive instead of themselves in the co-operation formation. Therefore, how to identify customer needs before co-operation and maximize customer satisfaction during co-operation would be the key purposes to select partners and reduce co-operation risk. We suggest that SMEs can sense customer needs and interpret them from own knowledge and then embody the focus of co-operation performance evaluation criteria based on the B2C values besides the B2B values. The true values of SMEs co-operation would then be more accurately estimated and delivered to customers. Moreover, our proposed framework and evaluation criteria are believed to provide the directions for the design of future service systems that can assist SMEs to achieve service innovation, growth and productivity through co-operation within their service sectors.

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