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Environmental factors affecting innovation strategies of companies: Customers and suppliers effect

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Abstract

We aim to identify the effect of customer characteristics, the effect of supplier characteristics and the effect of firm specific features on innovation level of firms. As the dependent variable has binary values, whether the firm makes innovation or not, the effects of independent variables on innovation activities are analysed by using binary logistic regression model. We have the following results from the earlier analysis of the data. The firms' motivation for innovation is mainly affected by their customer's and supplier's characteristics. Specifically, we found that if the spans of the customer and supplier increase, firms are more likely to innovate. Furthermore, if the turnover is generated by few companies, firms are less likely to make product innovation. Likewise, if the firms have higher number of customers and suppliers, the innovativeness levels of the firms become higher.

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Keywords: Innovation; process and product innovation; customers; suppliers

Introduction

Many low and medium added value product producers have lost their competitive advantages in the markets recently. Some of the reasons for firms' failure for losing their competitive advantage are globalization, access to cheap labour forces and rapid dissemination of know how through Internet and IT Technologies. It has been witnessed that economic growth and development in the developed and developing countries are mostly determined by innovation level rather than efficiencies of the firms as

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innovation enables companies to produce high added value products. Thus, innovations and ability to innovate become vital for firms in order to sustain their competitive advantage. Innovation strategy of a company is not only determined by company's workforce, capital and technological ability but also by how environmental factors force R&D activities and innovation level. Firms operating in the same sector have different innovation levels. Thus, the effect of environmental factors on innovation level and different innovation strategies also become important for sustaining competitive advantage of the firms.

In recent studies, innovation abilities of companies have been analyzed extensively through organization factors or through customer and supplier relations of companies. However, the effects of external environmental factors on organizational innovation capability have not been thoroughly analyzed. The characteristics of suppliers and customers are the most vital factors affecting innovation level of a company. The variety of customer demands lead companies to serve in a more competitive environment and this force firms to become more innovative. The high numbers of competitive suppliers enable companies to learn new ideas from them, thus enable the possibility of accelerating innovation trends in the company.

This paper focuses on two main questions: 1) How does customer characteristics affect firms' innovation level? 2) How does supplier characteristic affect firms' innovation level? In order to answer these two questions, dataset from European e-Business Market Watch survey is analyzed.

The dataset used in this project is more comprehensive; thus it will enable several original contributions to the literature. We analyze how customers' and suppliers' competitiveness and their changes in market share affect firm's innovation level. Our findings reveal that the competitiveness of suppliers and customers greatly affect the innovation level of the companies.

Literature Review

Relations with customers and suppliers are the most important factors affecting innovation strategy of a company. The recent studies in the literature emphasize the effect of customers and suppliers on innovation level of the organizations. The suppliers' impact on new product management has been analyzed in terms of innovation by Hakanson et.al. (1993). The close relations with suppliers result cost reduction, quality increase and faster release of new product in the markets (Wynstra et.al, 1999; Handfield et al. 1999; LaBahn et al. 2000; Takeishi, 2001). The effect of customers on innovation level has been studied by Von Hippel (1986), Lundwall (1986) and Biemans (1989) and results have shown that the feedback from customers lead to unique innovations. Johnsen et al. (2006) have analyzed the level of customer and suppliers' effect on innovation process. The results have shown that the customers affect the innovation in the early phases and the suppliers affect the innovation in the later phases. Salomo et al. (2003) showed that customer orientation in innovation projects has a positive influence on new product development success and the degree of product innovativeness increases in due course. Atuahene-Gima (2005) argued that customer orientations support product innovation. Lukas and Ferrell (2000) analysed the customer orientation's effect on products. Chen and Tsou (2012) have emphasized the IT abilities of customers and the fact that the process innovation is led through organization's performance. Romero et al. (2012) have supported the thesis that the factors affecting process and product innovation should be analyzed separately. Romero et al. (2012) stated that the personal motivations have a certain effect on process innovation, however has no considerable effect on product

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