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Organizing for value appropriation: Configurations and performance outcomes of price management

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ABSTRACT

Value creation and value appropriation are fundamental strategic processes. Both can be analyzed at the level of the individual manager, an organization or at the systemic level. On the organizational level, empirical research so far has put strong emphasis on aspects of value creation, while value appropriation has received less attention. We analyze value appropriation through the organizational implementation of pricing processes in the context of formalization, specialization, centralization, dispersion of influence, and top-management involvement in firms' pricing organization. Through a large-scale exploratory study of 419 European companies in the B2B area, we identify five empirical organizational configurations of pricing organization for value appropriation. Testing the effects of pricing configurations relating to pricing performance as well as overall firm performance reveals that more systematic approaches to pricing organization significantly improve value appropriation outcomes.

1. Introduction

Value creation and value appropriation are fundamental strategic processes (Ghemawat, 1991; Obloj & Capron, 2011; Reitzig & Puranam, 2009). They can be analyzed at the level of the individual manager, at an organizational level, or more generally related to systems such as business relationships, networks or society (Lepak, Smith, & Taylor, 2007). Strategic management focuses primarily on the organizational level of value-related aspects and studies value creation and appropriation in different contexts, such as entrepreneurial opportunity recognition (e.g. Mahnke, Venzin, & Zahra, 2007), alliance management (Ness, 2009), or framing of innovation (Van Burg, Berends & van Raaij, 2014).

Value creation and value appropriation have been researched with regard to their effects and determinants (e.g. Blocker, Cannon, Panagopoulos, & Sager, 2012; Obloj & Capron, 2011; Priem, 2007), or their interactions and trade-offs (e.g. Bowman & Ambrosini, 2000; Mizik & Jacobsen, 2003). However, it has been argued that "*these developments have been curiously one-sided, with the emphasis on […] value creation rather than value appropriation*" (Reitzig & Puranam, 2009, p. 765). This asymmetry in scholarly interest is all the more surprising given that value appropriation "*is arguably the main objective of firms*" (Pitelis, 2009, p. 1124).

While *value creation* is important as a determinant of a firm's competitive advantage, *value appropriation* refers to the degree to which a firm can capitalize on this advantage, i.e. to what extent it can extract value based on its competitive position (Mizik & Jacobsen, 2003). MacDonald and Ryall (2004) argue that competition determines whether a company can capture (i.e. appropriate) value. The more effective a company is in value appropriation, the better it is able to avoid *value slippage*, i.e. a situation where the firm creating a substantial part of value in a value network does not retain a corresponding share of the value it creates (Lepak et al., 2007; Parolini, 1999). Hence, extracting value from customers (i.e. monetary sacrifices) in exchange for value created by an offering, and retaining a maximum of this value in vertical competition within a value system (i.e. *vis-à-vis* suppliers) is a key challenge for firms. Consequently, value appropriation is seen as a core *organizational capability* (Reitzig & Puranam, 2009).

In the context of value appropriation the general management literature has consistently stressed the importance of price (Hinterhuber, 2004; Monroe & Della Bitta, 1978; Rao, 1984). Pricing decisions affect firm profitability arguably more, and more directly, than any other business decision, and sound pricing has been regarded as a source of competitive advantage (Dutta, Zbaracki, & Bergen, 2003). Although firms' awareness of the critical role of pricing has been increasing over the last two decades, there still exists some lack of knowledge about certain pricing aspects in managerial practice as well as in scholarly research (Baker, Marn, & Zawada, 2010a). Some issues of pricing as an organizational value appropriation capability are well researched, for

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example pricing strategy (e.g. Forman & Hunt, 2005; Morris & Calantone, 1990), partly because of the immediate impact of getting pricing decisions wrong: Netflix's pricing fiasco in the U.S. in 2011 represents such a case. Netflix raised the price of its DVD-streaming bundle by almost 50%, resulting in a severe customer backlash, with the loss of almost 30% of its subscriber base of about 25mio. customers, and a 50% reduced share price. However, the same emphasis has not yet been given to issues about how to *organize for pricing*, although extant surveys of pricing professionals show that such organizational aspects are top-of-mind in practical value appropriation management (Homburg, Jensen, & Hahn, 2012; Noble & Gruca, 1999; Roll, 2009).

Dutta et al. (2003) have argued that pricing is an organizational capability, which is linked to firm's organizational design choices. Such choices are important aspects of practical pricing management: in the automotive supply industry with its oligopolistic demand structure, supplier companies had to find optimal pricing organization designs by organizing 'near to the customer'. Thus, sales teams linked to project structures are responsible for pricing (in coordination with the controlling function), with the marketing department being side-lined. Other companies, such as a German tool manufacturer, developed new organizational structures around 'in-house pricing consultants' who are assigned to bidding teams for project acquisition activities (Batten, 2011).

Despite increasing attention regarding the importance of pricing, challenges to organizationally implementing pricing activities persist, resulting in many companies failing to take advantage of value appropriation opportunities (Hinterhuber, 2008; Ingenbleek, 2007). Contrary to assumptions of prior research, pricing is neither easy nor costless (e.g. Dutta, Bergen, Levy, & Venable, 1999; Bergen, Ritson, Dutta, Levy, & Zbaracki, 2003). Profitable pricing as part of successful value appropriation involves considerable process costs (Dutta et al., 2003; Zbaracki, Ritson, Levy, Dutta, & Bergen, 2004) and can arouse intense intra-organizational controversy (Lancioni, Schau, & Smith, 2005), making a firm's lack of enthusiasm for dealing with organizational pricing challenges more understandable: "*Few challenges cause more anxiety for senior executives than the implementation of pricing strategies*" (Nagle, Hogan, & Zale, 2011, p. 174).

In an attempt to better understand value appropriation issues, recent academic work has paid greater attention to the *organizational context of pricing*. Several authors note that prior studies have neglected such organizational aspects of pricing (Carricano, Trinquecoste, & Mondejar, 2010; Ingenbleek, 2007), and conceptual articles argued that failure to use advanced pricing approaches might be ascribed to the organizational context of pricing (Ingenbleek, 2007). Practical concerns by managers underline the relevance of a systematic pricing organization to make a difference: "*Successful companies deliberately build a strong pricing infrastructure that underpins and sustains pricing excellence*" (Baker et al., 2010a, p. 2).

Recent value appropriation research most frequently studies selected and traditional bureaucratic organizational dimensions. For instance, some researchers have examined specialized pricing functions (Baker, Marn, & Zawada, 2010b; Carricano et al., 2010; Nagle et al., 2011), as well as issues around formalization (Argouslidis & Indounas, 2010; Ingenbleek, 2007), and centralization (Cavusgil, Chan, & Zhang, 2003; Frenzen, Hansen, Krafft, Mantrala, & Schmidt, 2010; Homburg et al., 2012). They found that pricing organization may vary considerably among firms (Smith, 1995).

However, the variety of approaches to pricing organization across companies has not been investigated on the basis of large-scale empirical evidence. Often, uni-dimensional concepts are used. The result is not only a dearth of empirical research that systematically explores pricing organization but also the absence of a conceptual framework that includes a variety of relevant dimensions of pricing organization. To rectify this important gap, this paper builds on prior conceptual groundwork that discusses prototypes of pricing organization both conceptually and anecdotally (Baker et al., 2010b; Carricano et al., 2010; Nagle et al., 2011; Smith, 1995). From this starting point, we develop an integrative conceptual framework for pricing organization and use data from 419 business units in the B2B sector that allow for the exploratory analysis of different configurations of pricing organizations and their performance implications.

Doing so, our study contributes to existing research by deriving the core characteristics of pricing organizations as part of an integrative conceptualization; by validating measurement instruments for these core characteristics; by identifying different configurational approaches to pricing organization in practice on the basis of a large-scale taxonomy, and by testing the relationship between different pricing organization approaches and organizational outcome variables.

The remainder of this article has the following structure. We review the literature on pricing organization and related research, and identify and introduce fundamental dimensions of pricing organization. We then outline our data collection and measurement approach and describe the taxonomical procedures. We present the taxonomy and the performance implications of configurations, and finally we discuss implications for academic research and managerial practice.

2. Literature review

2.1. Research on pricing organization

During the last two decades, the management literature has increasingly considered pricing to be not just a one-time decision but a continuing organizational process (Baker et al., 2010b; Dutta et al., 2003; Shipley & Jobber, 2001; Smith, 1995), requiring therefore the management of a set of interdependent activities (Shipley & Jobber, 2001). Building on previous frameworks, four critical decision fields can be identified: strategic pricing decisions, list or target price decisions, transactional pricing decisions, and price controlling (Baker et al., 2010b; Dutta et al., 2003; Farley, Hulbert, & Weinstein, 1980; Hinterhuber, 2004; Lancioni, 2005; Shipley & Jobber, 2001).

Activity-based research tends to focus on the activities related to such decision fields. So far, structural organizational issues play a minor role in this context, despite the findings of research on comparable marketing and management processes showing that such organizational aspects are a major concern (Cadogan, Sundqvist, Salminen, & Puumalainen, 2005; Homburg, Workman, & Jensen, 2002; Menon, Bharadwaj, Adidam, & Edison, 1999). While our study draws on an activity-based perspective of pricing, it takes the position that pricing organization is the structure that buttresses the pricing process, and therefore needs to be considered especially.

A review of the literature shows that few authors have addressed pricing organization either in a holistic manner, or related to specific organizational dimensions. Prior research can be divided into three categories (Appendix 1): (1) studies that focus explicitly on pricing organization, (2) investigations that draw implicitly on the notion of pricing organization, and (3) examinations of single dimensions of pricing organization in a narrow context. Based on the analyzed literature, five main dimensions of pricing organization are identified: formalization, centralization, specialization, dispersion of influence, and top-management involvement.

Studies in category 1 consider pricing organization within a cross-functional decision-making process, with the most comprehensive conceptual framework being provided by Smith (1995). This view comes closest to our understanding of pricing organization, as it regards organizational dimensions as characteristics of decision-making processes in pricing. This line of research is largely conceptual (Baker et al., 2010b; Nagle et al., 2011; Smith, 1995), with some contributions being based on anecdotal evidence (Baker et al., 2010a; Shapiro, 1983). The one empirical study in this category is based on qualitative interview data (Carricano et al., 2010). Some studies in this category suggest typologies describing several stages of the development of