

# Understanding the Role of Relational Capabilities in Buyer-Seller Relationships

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## Abstract

The study investigates the processes of relationship value creation in industrial markets from supplier perspective. Our results show that business can increase competitiveness and contribute to effective differentiation through analysis and improvement of mechanisms of relationship value creation and understanding of the role of such determinants as firm's strategic orientations, development of relational capabilities and customer specific investments and adaptations. We base our research on the theory of creation of sustainable competitive advantage and apply this theory to relationship marketing. In center of our research are relational capabilities of industrial firms as precursor of superior relationship value creation for both customer and supplier. The research hypotheses were tested using structural equation modeling. We have proved that effective relationship strategy contributes to firm's flexibility, as well as business performance, and thus has potential to create relationship-based advantage. On the base of the results of the study we propose a conceptual approach to the role of relational capabilities in coordination of customer's and supplier's strategies in managing the relationships.

**Keywords:** relational capabilities, supplier perceived relationship value, market orientation, customer specific investments

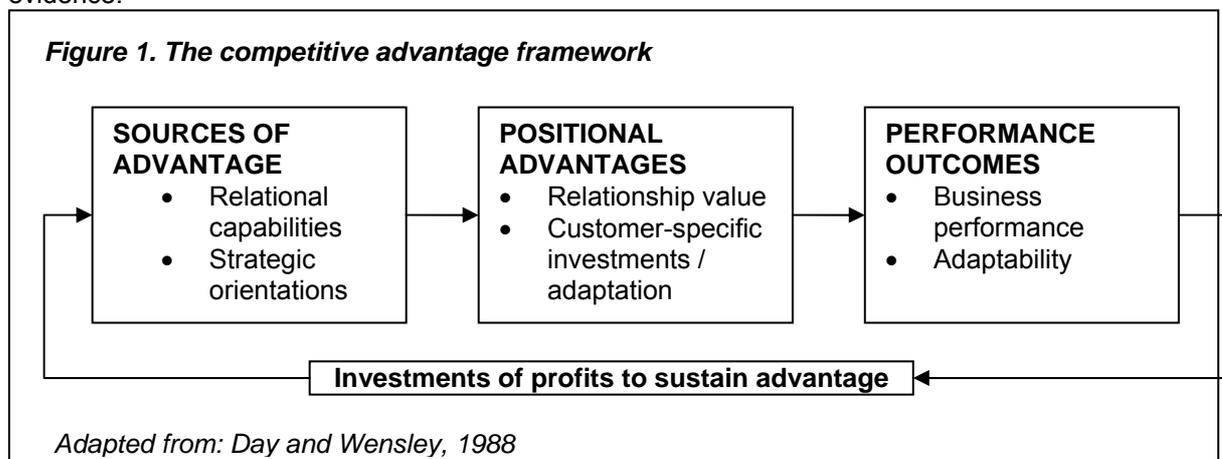
## Introduction

The idea that business relationships create value in the sense that the competitiveness of the participating partners increases because of the relationship [Wilson, 1995] has led to multiple theoretical concepts. The interest to this topic has contributed to theoretical operationalization of relationship value construct (Ravald & Grönroos 1996; Mandjak & Durrieu 2000; Walter, Ritter & Gemünden 2001; Wilson & Jantrania 1996; Lindgreen, Wynstra, 2005; Grönroos, 1997), but there is still a lack of empirical evidence on determinants and mechanisms of relationship value creation as well as on its influence on firms' performance and adaptability.

We base our study on previous results of value research, stressing the importance of understanding the mechanisms and means of relationship value creation [Walter, Ritter, Gemünden, 2001]. Taking into consideration earlier attempts to analyze relationship management in business markets from the perspective of creation of sustainable competitive advantage [Day & Van den Bulte, 2002], we look for the answer to the question "Why do firms differ, and how does it matter?" (Nelson, 1998) from the perspective of customer relationships in industrial markets. Focusing on the supplier perceived value and determinants of relationship value creation from the supplier's side, we propose to look on the possibilities to obtain advantages by turning inwardly the supplier's organization and analyzing information about the assets and relational capabilities of the firm.

## Theoretical Background

We analyze the process of relationship value creation on the base of the conceptual model of Day and Van den Bulte [2002] and regard the relationship capabilities (*Figure 1*) as precursor of superior relationship value creation for both customer and supplier. The research field of relational capabilities of industrial companies represents just a few studies [Day and van den Bulte, 2002; Moeller and Törrönen, 2003], and the role of relational capabilities for relationship value creation has hardly received empirical evidence.



Defining relational capabilities we can use the classic definition of dynamic capabilities [Teece, 2000] as firm's ability to sense and then to seize new opportunities, to reconfigure and protect knowledge assets, competences, and complementary assets and technologies to achieve sustainable competitive advantages on the base of customer relationship management. In association with definition of marketing capabilities (Weerawardena & O'Cass, 2004) it is possible to propose alternative definition of relational capabilities as integrative processes designed to apply the collective knowledge, skills, and resources of the firm to the relationship-related needs of the business. But the main distinctive feature of relationship capabilities is that they are going outside of the marketing function and belong to cross-functional firm capabilities (Grant, 2004), since as integrated bundle of unique skills they require alignment of efforts of everyone in the company and influence firm's performance.

Despite the lack of research in the field, there have been several studies, focused on relationship-based capabilities. Thus Moeller and Törrönen [2003] investigate business suppliers' value creation potential. Due to this concept, value production includes creation of core value, value-adding relational value production and future oriented value production. The authors stress the fact, that only core value can be

created on the basis of production capabilities. The more future-oriented and innovative is the firm's strategy, the more complicated aims are defined for relationship strategy and the more complex become capabilities, underlying the value creation. *Relational capabilities* in this concept represent just one of eight types of capabilities, underlying supplier's value production.

*Customer relating capability* is the central construct for the study of Day and Van den Bulte (2002), regarded as a bundle of three interrelated components: orientation, information and configuration. This study is based on the same framework of competitive advantage and shares the view of a capability as a knowledge acquisition and application process. The configuration school of strategy has pushed capability analysis to incorporate interactions into theory: it means that when interaction is dysfunctional due to poor alignment or conflict among elements, the capability is degraded and contributes to a competitive disadvantage.

Taking into consideration, that relational capabilities are assumed to be the main determinant of relationship value creation in our study, we have addressed a recent research on *customer integration competence* [Jacob, 2003]: this approach allows more detailed and profound understanding of capability's nature and components. The construct's structure, proposed by Jacob [2003] includes three dimensions – communication competence, configuration competence, and control competence. This structure is similar to the elements of the customer relating capability [Day and Van den Bulte, 2002]: orientation, information and configuration, and considering that we have included in the study the strategic orientations of supplier's firm, we can separate the "orientation" component and make some parallel between communication and information competences. The control competence in the model of Jacob [2003] presents additional emphasis of accomplishment in capability's implementation, and can have strong impact on the value created. On the other hand, the content of the scale, measuring the relational capability in the study of Moeller and Törrönen [2003] has also many parallel items with both studies. At this point it is important to mention, that when relational capacities scale [Moeller and Törrönen, 2003] consist of 8 items to measure all the dimensions of capability, and Day and van den Bulte [2002] use single-item scales to measure the customer-relating capability, the approach of Jacob [2003] represents the most complete attempt to structure and operationalize this construct.

Defining effectiveness of firm's processes, supporting customer relationships, relational capabilities can be regarded as the main determinant having direct influence on the level of both customer and supplier perceived relationship value. When measuring relationship value we face the outcome of all the range of relationship-related activities, resulting from multidimensional understanding of value and its possible drivers. Cross-functional nature of relational capabilities forces us to go outside of single organizational functions and processes and analyze the unique combination of resources, skills, assets and technologies of each firm.

On the other side, development of relational capabilities leads not only to creation of superior relationship benefits, but also to some possible relational sacrifices in form of **customer specific investments and adaptations**. These investments and adaptations can substantially increase fit between partners in relationship and facilitate the cooperation. High level of adaptation though presents certain limitations to firm' current and future flexibility and can force dependency from partner, decreasing effectiveness of collaboration in the future. When relational capabilities in our study imply development of unique organizational capabilities supporting in the whole collaboration and interaction with customers, specific investments and adaptations are connected with substantial investments made in order to fit the needs of some specific customer. To substantial extent these investments can loose the importance to the firm in case of this relationship dissolution. Thus the meaning of these two constructs in the study is highly different. Thus we propose the hypotheses, investigating the influence of relationship capabilities development on the level of supplier-perceived relationship value on one hand, and level of customer specific investments and adaptations on the other hand.

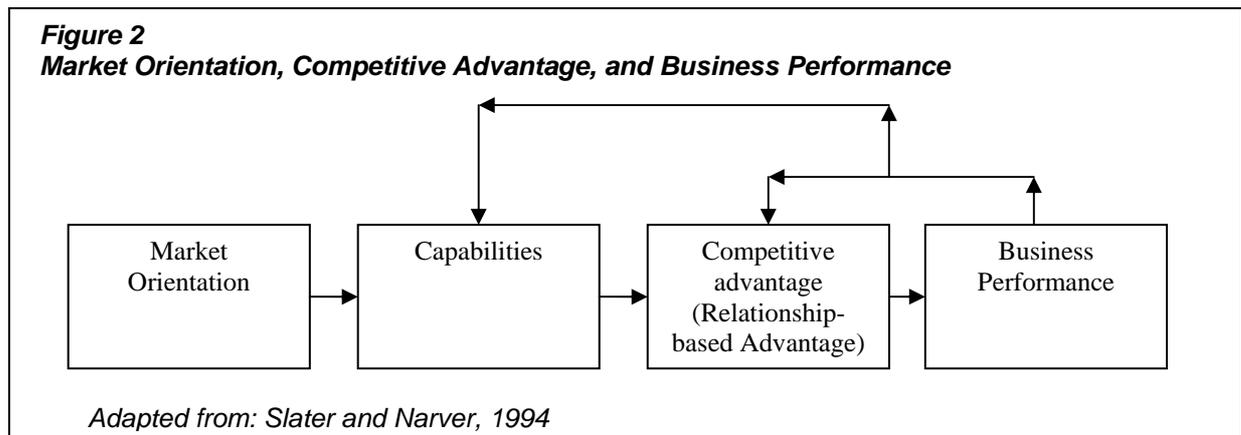
*H1: Development of supplier's relational capabilities has strong positive impact on supplier's perceived intangible relationship value.*

*H2: There is a positive relationship between supplier's relational capabilities and supplier's customer specific investments and adaptations*

Our hypotheses assume that development of relational capabilities can be positively influences from the side of the **market orientation** and **relationship orientation**. Thus we include in the analysis strategic orientations, representing important determinants for the development of firm's relational capabilities. The approach of Slater and Narver [1994] is in one line with the model of Day and Van den Bulte [2002] we draw as conceptual base of our study (*Figure 1*).

*H3: There is a positive relationship between market orientation and development of relational capabilities in industrial company.*

H4: There is a positive relationship between relationship orientation of industrial companies and development of relational capabilities.



We specify the model (see *Figure 2*) and investigate this approach basing on the supplier's relational capabilities and **relationship value** as relationship based advantage. Whether relational capabilities contribute to the firm's market success and competitiveness can be understood on the base of some indicators, whereby the main non-economic outcome and success indicator can be represented by relationship value. We have focused on the main dimensions of the relationship value construct: strategic and behavioral components of relationship value (competitive advantage, improvement of core competences and creation of market position, social bonding, trust and culture, developed by a relationship) (Wilson & Jantrania, 1994). The important feature of our model is that it puts emphasis on indirect functions of relationships with customers (Walter, Ritter and Gemünden, 2001), underlining intangible nature of relationships as company's assets (Teece, 2000).

The specific of our study is analysis of relationship value as a mediating variable – representing an outcome of the relational capabilities development on one side, and mediating these effects on the supplier's performance. Thus we imply the functions we put as base for measurement of supplier perceived value as source for differentiation, linked with the firm's ability to gain benefits from existing customer relationships. The effectiveness "market sensing" capability, for example, can be represented through the information (F1) and innovation functions (F2) of relationships in the relationship value construct. The leveraging of supplier's strategy occurs through the improvement of its competences (F4). And the level of process integration and co-production (F3) allows building the structural bonds between the companies. We also include in the analysis the reference value of relationships for supplier (F5). At the same time, we regard relationship value as trade off between benefits and sacrifices (Walter et al, 2001, Ravald and Grönroos, 1996) and take into consideration the **customer specific investments and adaptations**, supplier has to undertake in order to achieve better fit with the customer's firm and maintain the relationship.

H5: There is a positive effect of supplier's perceived relationship value on supplier's marketing results.

H6: There is a positive effect of supplier's perceived intangible relationship value on supplier's overall business results.

H7: There is a positive effect of supplier's perceived intangible relationship value on supplier's adaptability.

Relationship value indicates the non-economic, intangible outcomes of development of relational capabilities and thus relationship strategy of a firm. But we trace also the business results of a firm to adjust created relationship value to tangible, economic outcomes. Organizational performance is a multidimensional construct, tapping financial, operational and customer-related performance domains. For measurement of business results we use two constructs: **performance** measurement is based on such indicators as changes in general cost and profitability level in comparison with company's main competitors. We have included in our study a construct, measuring company's **adaptability** as readiness to face future market challenges.

H8: There is a positive relationship between customer specific investments and adaptations of industrial company and its performance.

H9: There is a positive relationship between customer specific investments and adaptations of industrial company and its adaptability.

H10: There is a positive relationship between supplier's perceived relationship value and its adaptability.

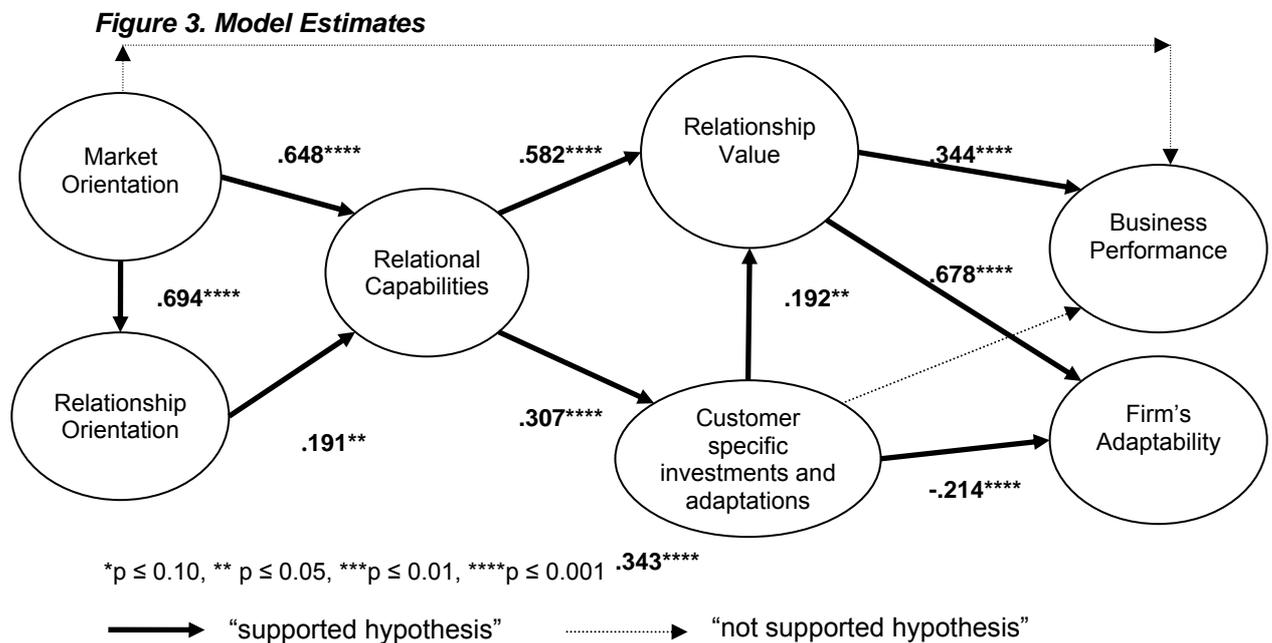
H11: There is a positive relationship between supplier's perceived relationship value and supplier's performance.

## Research Method

Data were collected on the base of the self-administered questionnaire sent to representatives of top-management in German industrial companies (mainly from such industries as machinery construction, metallurgy, etc.) in two phases. The total return rate proved to be 18,9% (185/974), so the final sample consisted of 185 industrial firms. The research hypotheses were tested using structural equation modeling on the base of the software package AMOS 4 (Analysis of Moment Structures). The resulting measurement model  $\chi^2_{(94)} = 1.782$  ( $p = .000$ ). The other overall fit indices obtained for the model were as follows: GFI = .902, CFI = .954, TLI = .941, IFI = .954, RMSEA = .065, RMR = 0.97. Taking into consideration the complexity of the model these goodness-of-fit statistics suggest that the overall model is acceptable (Anderson & Gerbing 1984). In the scales we have used a seven point Likert-type scale was used (1 = strongly disagree; 7 = strongly agree). For further details see *Table 1 and Table 2*.

We have undertaken sequentially confirmatory factor analysis to check our constructs for unidimensionality. On the base of conducted test for unidimensionality we have decided to use item parceling technique in order to decrease bias in structural parameters. The items for the measurement of study constructs were in most part taken from previous studies to relevant research directions: market orientation - MARKTOR scale (Narver and Slater, 1990), relationship orientation (Ivens, 2002), relational capabilities (Jacob, 2003), customer specific investments and adaptations (Ivens, 2002), marketing results and business results (Hildebrand, 1997). The scale for measurement of supplier perceived relationship value and the scale for adaptability are new ones.

## Research Findings



We have tested 11 hypotheses, 9 of 11 hypotheses were supported. **Figure 3** presents the diagram of relations of the estimated model.

In the first place, the results have proved that relationship capabilities have a highly strong positive impact on the supplier perceived intangible relationship value. At the same time, development of relational capabilities indeed affects also customer specific investments and adaptations of the firm. The level of customer specific investments and adaptations is proved to be also determinants of the relationship value perceived.

Our results support that both market orientation and relationship orientation are determinants for the level of development of supplier's relational capabilities. The impact of market orientation is substantially

stronger. We analyze whether market orientation influences relationship orientation, and support this hypothesis. We have also undertaken several steps to analyze mediating effects of some variables in the model, and have proved that relational capabilities mediate the effect of market orientation on creation of relationship value. At the same time, both relational capabilities and relationship value are key mediating variables between market orientation and business performance that has been supported by our tests. These results give us an opportunity to imply that development of relational capabilities indeed leads to creation of superior relationship value; this value creation chain influences firm's business performance and firm's adaptability and at the same time represents a possible way to implement market orientation in the firm – through creation of stable mechanism, directed at effective management of customer relationships and relationship value creation.

Finally, we have received evidence of the link between the level of supplier perceived relationship value and supplier's business performance. This is the verification of the whole value creation chain within supplier's firm – starting on the firm's strategic orientations and being based on the development of relational capabilities. Relational value mediates these effects, since the influence from customer specific investments and adaptations has been not proved. Both relationship value and level of specific investments have impact on firm's adaptability, signifying not only impact on firm's current results, but also on it's possible future results. It is important, that the link between customer specific investments and adaptations and firm's adaptability is negative, limiting firm's flexibility in future. But considering substantially higher impact on adaptability from the side of relationship value leads to positive influence in the whole.

## **Theoretical and Managerial Implications**

The main aim of our study has been to investigate the relationship value creation mechanisms in terms of the development of relational capabilities and assessments of their effectiveness. We have followed current existing interest to contribution of marketing discipline to the achievement of sustained competitive advantage (Day & Van den Bulte, 2002; Santos-Vande *et al.*, 2005) and analyzed customer relationships as firm's resources in combination with relational capabilities in order to explore practical effects of development of these resources and capabilities on organizational results and firm's effective differentiation. Our study has accepted propositions for further research and necessity to understand the preconditions for the development of relationship value functions (Walter *et al.*, 2001).

The findings of our study demonstrate that firms can really enhance their relationship value through development of relationship capabilities. The effectiveness of firm's processes of managing customer relationships do not only contribute to the creation of relationship value as a "soft" variable in our study, but also influence the "hard" performance variables as overall business results and firm's adaptability.

The main hypothesis of our study has been based on the understanding of firm's relational capabilities as active approach to relationship marketing, and supplier-perceived relationship value as outcome of this approach. Our theoretical model and results of the analysis allow us to propose an integrated concept, based on the framework of competitive advantage "sources of advantage – positional advantages – performance outcomes" [Day and Wensley, 1988] (Fig. 1). The analysis of the role of market orientation on relationship value creation (Fig. 2) expands our approach and allows to understand the potential of relational activities of firm's performance influence.

The sources of advantage are in our study are seen as two-level construct, presented by relational capabilities as the central determinant [Day & Van den Bulte, 2002; Moeller and Törrönen, 2003], determined itself through the supplier's system of strategic orientations. Indeed, the previous research assumes that divergence in goal systems between companies may differ tremendously from company to another [Mayo, 1945, Barnard, 1968, Ivens, 2002], having impact on the effectiveness of the whole management system and strategy of the company. Thus we provide empirical evidence, supporting the potential of creation of competitive advantages on the base of improvement of relationship management.

Firstly, our results show that effective relationship strategy contributes to better performance and superior flexibility of a firm, what has a really strategic meaning and indicates the effectiveness of the firm's strategy (the block "performance outcomes"). Secondly, the optimized combination of customer specific investments and adaptations and superior supplier perceived relationship value represents the unique position of the firm, based on the harmonized interaction with customers ("positional advantages"). And finally, the creation and promotion throughout of organization of strategic orientations (as marketing and

relationship orientations) together with the development of relational capabilities symbolize really unique resources of the firm. According to the concept of value innovation (or strategic innovation) (Matthyssens and Vandembemt, 2003). The aim of value innovation can be described as creation of new market space, enabling companies “out-competencing” rather than “out-performing” competitors [Pitt and Clarke, 1999]. Without decreasing attention to efficiency and cost control, in focus of strategy development have to be flexibility, creativity and timing [Galunic and Eisenhardt, 2001]. New value concepts and re-invention the way the value is created and delivered is one of the ways to create long-term competitive advantages [Matthyssens and Vandembemt, 2003]. Customer relationships underpin the base of intellectual assets of a firm and imply potential resources and drivers to improve firm’s capabilities and competences when managed effectively.

Analyzing the results of the model testing, we may conclude that the supplier perceived relationship value, is often regarded as the very “outcome” of the relationship strategy [Payne, Holt, 2001], represents at the same time the outcome of the customer’s relationship strategy – as customer’s level of involvement in the development of several directions of collaboration within overall customer-supplier interaction. This level of customer’s involvement into relationship development can be categorized as the customer’s relational mode [Groenroos, 1997]. Analyzing the customer’s relational mode, Groenroos [1997] investigates, what type of marketing strategy seems to be most appropriate for the supplier. The other factor for the strategy definition is the type of supplier’s efforts, based on relational or non-relational intent. This conceptual model allows us to present our results in the following matrix as combination of customer’s and supplier’s relationship approaches (Table 1). We base this model on our study supporting importance of supplier’s capabilities in relationship value creation as determinants, and as outcome itself – mediating the effect of firm’s market orientation and relationship orientation. We imply that the same many-dimensional and many-level structure affects relationships’ success and potential for value creation from the side of customer’s firm.

**Table 1. The Analysis of Partner’s Relationship Strategies in Industrial Markets**

		Customer’s relational mode		
		Active	Intermediate	Passive
Supplier’s relational capabilities	Superior	<b>(1) “pure collaboration”</b> <i>-buyer-supplier strategy-fit;</i> <i>- high-potential value co-creation;</i> <i>- high customer involvement</i>	<b>(2) supplier-forced relationship</b> <i>-supplier’s driven of value co-creation;</i> <i>-limited customer involvement</i>	<b>(3) “doubtful” relationship</b> <i>-doubtful potential of value co-creation;</i> <i>-low customer involvement</i>
	Limited	<b>(4) customer-forced relationship</b> <i>-customer’s driven of value co-creation;</i> <i>-high customer involvement</i>	<b>(5) indeterminate position</b> <i>-buyer-supplier strategy-fit;</i> <i>- limited potential of value co-creation;</i> <i>- limited parties involvement</i>	<b>(6) supplier’s maintained relationship</b> <i>-low potential of value co-creation;</i> <i>-low customer involvement;</i>
	Low	<b>(7) “doubtful” relationship</b> <i>-doubtful potential of value co-creation;</i> <i>- low supplier’s involvement</i>	<b>(8) “potentially non-viable relationship”</b> <i>-low-potential of value co-creation;</i> <i>-low supplier’s involvement</i>	<b>(9) “pure transactional exchange”</b> <i>-buyer-supplier strategy-fit;</i> <i>-transactional focus: no value co-creation;</i> <i>-no parties involvement</i>

In this table we can analyze three equilibrium situations of strategy fit between buyer and supplier (1, 5, 9), proposing pure collaborative, intermediate and pure transactional situations. The most promising

situations (1, 2, 4) represent potential for relationship value co-creation, and differ just on the level of parties involvement and motivation to develop the relationship and to invest in the collaboration. The three further similar situations (5, 6, 8) represent the much lower potential of effective collaboration, and signal the failure in the companies strategic orientation system and market sensing. The most polar differences in sides' strategies are shown by situations (3) and (7), and are called "doubtful" relationships. We assume that these cases represent false partner selection, and can be regarded as hardly viable relationships. On the other hand, though, considering very high involvement of one of the partners, these situations allow to suppose possibilities for forcing the "right" type of relationship and development, "education" and strengthening of the partner's strategy in course of interaction by the relationship leader.

Taking into consideration the strong impact of supplier's relational capabilities development on the level of supplier perceived relationship value in our study, we may conclude, that intense supplier's investments in the development of relational capabilities mostly correspond with the character of customer's relational mode – active or intermediate. This can mean that these are mostly *mutual* investments, occurring in the concurrent adaptation and adjustment of processes, skills, and capabilities leading to better strategy fit. We have also to take into consideration that we asked to answer to the questionnaire according to the "main, most important" customers to the company. Thus we speak on the results on the key customers relationships, which is the supplier's strategy really oriented at. Therefore our results do not exclude all the other fields of the matrix, and provide just a better picture on the relationship oriented situations.

We imply that our results on the mechanism of value creation from supplier's perspective provides us with many potential points of value creation in frames of buyer-supplier collaboration in industrial markets. This many facets of possibilities for coordination of buyer and seller's strategies' coordination, supposed by our model, may become the basis for better understanding of interactions in industrial markets, firm's analysis and self-assessment. The supplier perspective in the study is its both advantage and main limitation. The advantage consists of the possibility to have an in-depth view on the value creation processes and the role of relational capabilities in supplier's firm. But at the same time, the Table 1 represents our concern for understanding of both sides' strategies and impact on value creation. There is a general lack of both-sided studies, taking into consideration an extended view on the value creation determinants, its impact of performance and possibilities of finding the best "fit" combinations among partners.

We are convinced that the capabilities based approach allows the researchers to investigate more the mechanisms, supporting effective buyer-seller relationships in industrial markets, and to combine the knowledge from this sphere of management with the knowledge from other spheres, providing thus value both for academics and practitioners. We understand the limitations of our study and would like to propose several aspects of the study for further research. The dynamic aspect of the strategy development was not assumed by the aim of our study, but the results achieved allow us to propose these issued for the investigation by the future research. The other intriguing research direction could be analysis of these mutual strategies adjustment from the customer's side. We would also propose for the future research to investigate the mechanisms of coordination between the customer and supplier relationship management in industrial firms, and thus the relationships between the development of the interrelated organizational capabilities in these fields.

## Appendices

**Table 1. Summary Statistics of the Measurement Analyses (N=185)**

	Mean	Cronbach's alpha	Variance Extracted	Composite Reliability	Factor Loadings*
Relationship orientation	5.63	.70	.55	.71	.70-.79
Market orientation	5.22	.78	.56	.79	.64-.85
Relational capabilities	4.84	.81	.83	.94	.87-.95
Relationship value	4.96	.79	.83	.91	.91-.92
Customer specific investments/adaptations	4.87	.78	.67	.80	.70-.93
Business performance	4.24	.74	.60	.75	.72-.82
Adaptability	4.92	.70	.55	.71	.69-.78
Fit Statistics: $\chi^2_{(94)}=174.725$ (p=0.000), df = 1.782, CFI=.954, NFI=.902, IFI =.954, TLI=.941, GFI=.902, RMSEA=.064, RMR=0.97					

**Table 2. Correlation/Covariance Matrix**

	RO	MO	RC	RV	BR	A	IA
Relationship Orientation (RO)		.697	.632	.572	.157	.509	.169
Market Orientation (MO)	.206		.779	.644	.281	.702	.303
Relational Capabilities (RC)	.267	.359		.615	.285	.502	.362
Relationship Value (RV)	.257	.328	.437		.399	.567	.364
Business Performance (BP)	.057	.111	.146	.213		.554	.090
Investments/Adaptations (I/A)	.110	.213	.332	.345	.078	.024	
The correlations are shown above the diagonal, and the covariances – below the diagonal.							

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