

Hangzhou Westlake International Conference on Small and Medium Business

15 to 17 October

## **CREATING DISRUPTIVE STRATEGIES FOR SMALL AND MEDIUM BUSINESSES USING THE ‘TERMS’ TECHNIQUE**

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It is now well-recognized that in addition to the traditional industry-based view of competitive advantage (Porter 1980) and resource-based view of competitive advantage (Penrose 1959, Barney 1991, Dollinger 1999), there exists the disruption-based view of entrepreneurial strategy leading to competitive advantage (Hamel & Prahalad 1989, Hamel & Prahalad 1994, D’Aveni 1994, Eisenhardt 1989). This is based on the seminal notion of ‘creative destruction’ (Schumpeter 1939). According to this strategy, an economically-destabilising industry strategy may change the rules of the game so that a Small and Medium Business (‘SMB’) can grow to overtake the largest players.

Whilst some scholars have explored the value creation potential of entrepreneurial management of resources for firms (Barney & Arikan 2001, Barney 1991), few have developed a framework for systematic formulation. ‘Creative destruction’, inherently requires creativity. Hence, creativity enhancing techniques should assist in developing such strategy.

### **Innovation and Creativity**

Entrepreneurial strategies involve four main types of innovation Kuratko and Hodgetts (2001). These are: ‘Invention’, ‘Extension’, ‘Synthesis’ and ‘Duplication’. ‘Invention’ and ‘Extension’ involve a ‘break’ from the existing industry value proposition by creating a new business model or adding something new to a current business model. ‘Synthesis’ involves re-combining existing elements from current business models to create a new business model. Finally (the least disruptive), ‘Duplication’ involves adding a unique element to a current business model

The four types of innovation match the two main types of entrepreneurial creativity mentioned by Kirton (1987). That is, ‘Innovators’ and ‘Adaptors’. ‘Innovators’ prefer

to break the rules in order to be creative. 'Adaptors' prefer to work within the rules in order to improve things. When formulating strategy, 'Innovators' are more likely to use the 'Invention' or 'Extension' types of innovation (as well as 'Synthesis' if it breaks the rules). Conversely, 'Adaptors' are more likely to use 'Synthesis' and 'Duplication' types of innovation.

Combining Kuratko and Hodgetts' (2001) innovation types with Kirton's (1987) creativity styles, it is argued can produce Innovator heuristics to facilitate formulation of entrepreneurial strategy (Dew & Robinson, 2004)

### **Customer Value**

The ultimate goal of entrepreneurial strategy based on creative destruction is enhancing customer value. Such enhancement is not merely limited to product improvement. For example, Southwest's no-frills airline increased customer value by reorganizing the transportation process. Southwest's new strategic approach changed the rules of the game in the aviation industry. The new business model was based on value chain efficiency in performance of all Southwest's activities achieved by rapid gate turnaround, which allows frequent departures and greater use of aircraft, Turnaround productivity resulted from flexible union rules, with well-paid gate and ground crews, as well as from no meals, seat assignment, or baggage transfers, which means avoiding performing activities that slow down airlines. Southwest also utilizes airports and route (type and length) that avoid traffic. This also enables standardized aircraft (Boeing 737) thereby producing unique high-convenience and low-cost positioning (Porter 1996). Ultimately full-service airlines were adversely affected by this disruption since they could not compete on cost and convenience which Southwest offered, providing improved customer value.

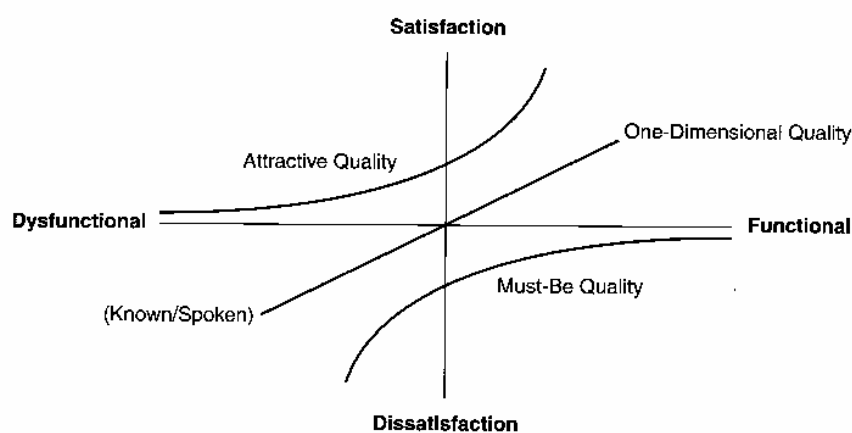
Accordingly, creating customer value requires a holistic approach. **Few techniques facilitate holism of thinking, especially when trying to envisage a future state that is vastly different from the current. It is not therefore surprising that conflict soften arise when senior members of management teams have differing views of the future. Achieving synergy at management level is important, otherwise progress toward actual disruptive strategies may be hampered by interpersonal conflict. For such**

cases, the Business Ethics Synergy Star (Robinson, Davidsson, van der Mescht and Court, 2006) is invaluable.

However, when considered from the perspective of a single function, it is less than likely that a disruptive strategy will emerge. Quality Assurance Managers may argue that creating customer value simply requires improved quality. Alternatively, Marketing Managers may argue that creating customer value simply requires marketing techniques for improved ‘actual product’ and ‘augmented product’ functions. However, neither of these approaches can produce effective entrepreneurial strategy since neither explicitly addresses disruption.

### Attractive Quality

Kano *et al*'s (1984) diagram (Figure 1, below) identifies three distinct types of quality which correlate to Quality Assurance, Marketing and Disruption perspectives.. ‘Must-Be Quality (correlating with Quality Assurance) relates to elements which fail to significantly improve customer satisfaction, but without which, customers become dissatisfied. The main purpose of Quality Assurance is to avoid such dissatisfaction. For example, the small joystick mouse located in the middle of a laptop’s keyboard was so small and close to the keys that its use was difficult. Hence laptops with such buttons were regarded as inferior and improving laptop touchpads is not considered a valuable innovation.



Source: Adapted from Kano, Noriaki, Shinichi Tsuji, Nobuhiko Seraku, and Fumio Takerhashi (1984). "Miryokuteki Hinshitsu to Atarimae Hinshitsu (Attractive Quality to Must-Be Quality)," Japanese Society for Quality Control.

Figure 1: Function vs. Satisfaction

‘One-Dimension Quality’ (correlating with Marketing) relates to the relationship between product function and satisfaction, such as actual and augmented product elements, which customers mention when asked for feedback on improvements. For example, longer battery life of laptop computers provides increased satisfaction, all other things being equal. Hence, longer life battery laptops are regarded as more satisfactory, but since they are usually available to all manufacturers, and not unique, there is little strategic advantage from enhanced functionality.

Distinguished from the above perspectives, ‘Attractive Quality’ (correlating with Disruption) relates to a quantum leap in satisfaction and customer value. For example, a wireless syncing feature enabling file transfer from PDA or mobile phone to laptop provides attractive quality for increased satisfaction since it can be proprietary and difficult to imitate for rivals. Hence this can provide competitive advantage.

However, primary market research cannot assist such strategy since customers are unable to articulate the value of a disruptive innovation before experiencing it. Therefore, one must have a means or method to systematically design creative disruptions producing novel attractive quality as well as customer value.

### **Value Innovation**

Kim and Maugborgne’s (1997) Value Innovation assists in providing a systematic method for firms to break existing paradigms of industry competition and develop entrepreneurial strategies. Value Innovation aims to increase customer value by giving a customer more of what it wants, and less of what it doesn’t need. This process relates to elements of both the SCAMPER (Michalko (2000) and Morphological Analysis (Zwicky, 1969; Van Gundy ,1995; Michalko ,1996; and Mattimore ,1994). SCAMPER is an acronym for Substitute, Combine, Adapt or modify, Magnify or add, Put to other uses, Eliminate or reduce, and Reverse or rearrange. Value Innovation The new factors are then combined by using Morphological Analysis to form entrepreneurial strategy.

However, the utility of Value Innovation is limited by neglecting to specifically define industry factors, failing to consider other factors, or new customer wants (Dew & Robinson, 2004). Dew & Robinson (2004) postulate a method of combining the

drivers of customer wants in various ways in order to develop numerous potential strategies, called the 'TERMS' approach. The entrepreneur can then synthesise (one or more) disruptive strategies, to converge upon a superior business model.

### **TERMS Technique**

The perception of value is a combination of a many factors, with every customer weighting factors in a unique way, making it subjective. (Kotler, Armstrong, Brown and Adam,1998). The TERMS technique models customer value using five generic factors: Time, Emotion, Risk, Money and Situation. These factors enable entrepreneurs to classify rival and substitute offers in order of relative value; and to assist with changing perspective in order to create potential customer value.

#### **Time**

Time factors affecting value relate to usage time, purchase time, lead time, speed, care, durability, repeatability, maintenance, history, future, and adoption profile. For example time relates to the decision to purchase food regarding to times of the day, perishability storage, queue waiting time, store opening times, speed of eating and so on, may significantly affect customer value.

#### **Emotion**

Emotional factors affecting value relate to power, achievement, belonging, acceptance, self actualisation, self esteem, affection, halo effects, freedom, order, honour, rivalry, cognitive dissonance, involvement level, confidence, sex appeal, fashion, and morals. For example, many restaurants spend considerable sums of money on interior design of decor and layout of tables and kitchen to create a unique experience for diners. Many restaurants sacrifice seating capacity for the emotional reason of customers to value them, not simply as an increased convenience of speed and attention. In the context of the long standing disillusionment with fast food, this has the potential to be a quantum leap in value. Presumably restaurant customers value refined and elegant personal attendance by a waiter over quick service.

#### **Risk**

Risk factors affecting value relate to product performance, warranty, external changes in product relevance, internal changes in product relevance, any potential for hold up by

a supplier, adverse selection issues, moral hazard problem, liability acceptance, legal issues, failure consequences, and perceived health risks. For example, consider the purchase of a meal from a street vendor. The customer will likely factor in the cooking method of the food and the vendor's hygiene if any. However other risks that affect value include freshness of the ingredients, storage means, cooking utensils, cooking method, packaging, whether or not the vendor will be there the next day if a customer is sick, whether the vendor will admit to serving food to the customer, how sick the customer is likely to become from food poisoning. Restaurant owners that can highlight how these other risk factors are better managed in their restaurants may have a significant value advantage for customers. This is true even for customers for whom such risk management might have been unthought..

### **Money**

Money factors affecting value relate to the absolute price of a purchase, whether or not the customer perceives the purchase price as cost plus, value minus, performance based, volume based, staged with separable portions or able to be financed. The price of a purchase relative to income, budget, rivals or substitutes also affects value. For example, all other things being equal, customers tend to buy snacks from street vendors to eat alone to and from work, and eat at more expensive meals at restaurants, when dining together with others.

### **Situation**

Situational factors affecting value relate to everything else specific to the customer that can affect the value of a purchase, such as the current default technical standard for an industry and the existence of a prior specification or contract often determines value for business purchases. Customer and supplier location can influence value, as can whether or not a purchase is an investment, impulse or necessity. Trends in the external environment, competitive factors and the stage of industry development also affect value. For example, loyalty programs for repeat purchases can influence a customer to return to the same restaurant on regular occasions.

### **Using TERMS for Small & Medium Business Disruption Strategy**

The TERMS process consists of eight steps (Dew & Robinson, 2004):

1. Determine the value curve in TERMS for the industry
2. Imagine a specific customer from a potential target segment
3. Empathise with the customer's TERMS
4. List qualitative TERMS factors that affect value
5. Determine the most important qualitative factors
6. Synthesise a business model based on the most important factors
7. Repeat with different specific customers
8. Select the best business models on the basis of inimitability and segment attractiveness.

The following case study illustrates how TERMS could be used to duplicate the entrepreneurial strategy developed by the founders of Alibaba.com when developing strategy for their website of the same name.

Alibaba was formed around a new online business directory enabling business-to-business (B2B) interactions. The basic website enables suppliers to upload their contact details together with product information such as specifications and photographs to [www.alibaba.com](http://www.alibaba.com). This website is free to access and browse for potential trade buyers, both domestically in other provinces, as well as internationally in other countries.. Alibaba was founded in 1999 with only USD\$60,000 from an apartment in Hangzhou<sup>1</sup>. Historically, information on Chinese manufacturers was difficult to obtain due to the absence of 'Yellow Pages' business directories commonly found in Western countries. Converting American hardcopy telephone directories onto softcopy gave rise to the idea for an online yellow pages for the Chinese market by the firm's founder Jack Ma..

Despite the annual subscription charge of USD\$5,000 to \$8,000.for access to Alibaba international website '[www.alibaba.com](http://www.alibaba.com)' compared with USD\$300 for using [www.china.alibaba.com](http://www.china.alibaba.com), Alibaba's users turnedover USD\$5,000,000 in 2004, with the company earning \$68million in cash revenues in 2004.<sup>2</sup> Alibaba employs 2,000 people in China, Europe and the US, and is the only import-export marketplace being awarded five years in a row "Best of the Web" by *Forbes* magazine.<sup>3</sup> In analysing

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<sup>1</sup> <http://knowledge.wharton.upenn.edu/article.cfm?articleid=1221>

<sup>2</sup> <http://knowledge.wharton.upenn.edu/article.cfm?articleid=1221>

<sup>3</sup> <http://knowledge.wharton.upenn.edu/article.cfm?articleid=1221>

Alibaba’s business model, TERMS provides insight to the disruptive strategies developed by Alibaba’s founders (see Table 1).

Table 1: Analysing Alibaba’s Business Model for Business Directories Using TERMS

TERMS Factors	Incumbents	Alibaba
Time	Long lead time (months) to arrange & schedule Company visit.	Online contact details enable instant communication via email and instant messaging
	Long lead time (weeks) to organise Product catalogues / samples	Online product catalogues enable access to photos and specifications.
	Limited duration (days) of trade fairs.	Online access available 24/7/365
Emotion	Word of mouth referalls of buyers/suppliers	Complete & continually updated list of buyers and suppliers
	MNC hosted website access to global marketplace	SMB convenient access to global marketplace
Risk	Personally recommended buyers / suppliers	Independent Thrid Party authentication and verification reducing risk of fraudulent buyers or sellers
Money	Company visits expensive to travel between provinces/countries organise/arrange/schedule(months)	Free of charge to use
	Participation in international trade fairs expensive transportation / accommodation	Subscription fee ‘premium’ benefit of enhanced site positioning, storage,, and transaction processing,
Situation	Industry specific sales networks	Global scale of electronic marketplace
	Limited information on Asian suppliers	Asian focus & dominance
	Limited Business Intelligence	Comprehensive catalog for competitor intelligence

Key differences in the Alibaba business model include:

- Instant access to product ranges and contact details of suppliers available free of charge to potential purchasers rather than requiring subscription to access such extensive business directory.,

- Access to global marketplace for ‘mom and pop’ SMBs without internet experience to showcase their products and businesses. Such access was previously only available to MNCs or larger companies which could afford a costly and dedicated webmaster to develop their own website.
- Market awareness based on buyers and suppliers both listing their businesses products and contact details online as their ‘webportal’, hence creating easily communicated ‘word of mouth’ promotion without the need for expensive advertising by Alibaba.
- Risk reduction for traders based on third party authentication and verification of business identity.

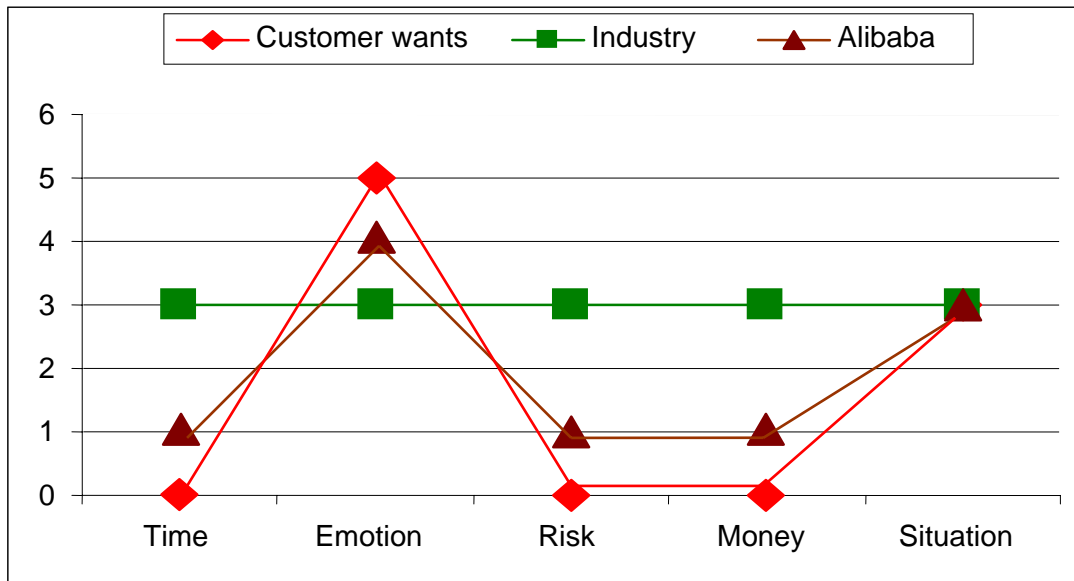
These differences could have been developed using the TERMS methodology. The process could have proceeded as follows. Firstly using TERMS all the existing business directories could be categorised with some common factors as listed in Table 1. Then the entrepreneur could have created a list for each TERMS factor of qualitative value factors for import/export customers. Then these factors may have been reduced to the following most important factors:

1. It would be nice to be able to look up a company’s products whenever one wants, and wherever that company is located., one need not travel to a trade fair or wait for weeks or months to obtain product catalogues and samples.
2. Having independent third party verification of buyers and suppliers reduces the risk of fraudulent enquirers
3. Being able to access product catalogues featuring product specifications and photographs online, instantly, at any time of day, free of charge, rather than paying for such privilege enabled the rapid build up of a large user base, hence increasing the value of the website to all users.

The above list would then serve as the design template for the disruptive strategy. Thus it is evident how the current Alibaba business model could be created by synthesising the factors into a business model. The business model does not require the control of a suitable set of starting resources and covers both actual and augmented product elements as well as marketing and strategy elements.

Figure 2 depicts how a TERMS based value curve can be used to compare Alibaba against traditional business directory incumbents. The graph shows that overall Alibaba is a closer match to the value curve empathically designed around an imagined import/export business customer.

Figure 2 : Business Directory Market TERMS Analysis



### Conclusion

The above strategy using TERMS can be adopted by SMBs to create novel, unique, non-generic and 'disruptive' business models, by ensuring that their strategies are closely aligned with their target market's needs and preferences. TERMS is also an ideal way to take stock of existing strategies and to upgrade SMB strategies on regular, eg. Annual basis.

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