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Towards a further understanding of the development of market orientation in the firm: a conceptual framework based on the market-sensing capability

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While the relationship between market orientation and performance has been examined extensively in the literature, relatively little attention has been given to the antecedents of market orientation. So the basic question of how to develop a market-driven organisation remains to a large extent unanswered. The capabilities framework provides a useful conduit through which this issue can be approached, since it recognises that firms are innately heterogeneous because the different resources or capabilities they possess. However, this area has been accused of being tautological in nature, and requires further extensive empirical analysis. This paper presents a theoretical framework that uses the decomposition of the market-sensing capability as a way to facilitate understanding of the creation of market orientation. Thus it will not only add to the literature on the antecedents of market orientation, but also offers an empirical analysis of a significant capability. Furthermore, this model addresses the question of the relationship between market orientation and learning orientation, and proposes that a learning orientation precedes a market orientation.

KEYWORDS: Market orientation; learning orientation; market-sensing capability

INTRODUCTION

If a date can be attached to the operationalisation of the marketing concept, it must be 1990, when a study by Kohli and Jaworski defined market orientation as being essentially an informational construct:

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> Market orientation is the organisationwide generation of market intelligence pertaining to current and future customer needs, dissemination of the intelligence across departments, and organisationwide responsiveness to it. (p.9)

The parallel study of Narver and Slater (1990) also preceded a considerable body of research on the implementation of the marketing concept through a market orientation (e.g. Greenley, 1995; Gray *et al.*, 1998; Deshpande and Farley, 1998). A number of studies have found a positive association between market orientation and performance, albeit using different performance measures (Narver and Slater, 1990; Kohli and Jaworski, 1991; Slater and Narver, 1995; Gray *et al.*, 1999). However, the literature on the antecedents of market orientation has been neglected according to Avlonitis and Gounaris (1999), whose study of the antecedents of market orientation is one of the few following the original analysis by Jaworski and Kohli (1993). Thus, while the market orientation literature has contributed by operationalising the marketing concept, relatively little has been achieved that is usefully prescriptive to managers seeking to develop a marketing focus.

The resource-based view of the firm (RBV), which originated in the strategy literature (Wernefelt 1984), may provide a useful framework for examining the development of market orientation. The resource-based view of the firm rests on a simple premise (Fahy and Smithee, 1999): that the desired outcome for organisations is to achieve a sustainable competitive advantage (SCA) that allows them to earn economic rents or above-average returns. The key to earning this reward is the possession of critical resources that are firm-specific, valuable to customers, non-substitutable and difficult to imitate (Rugman and Verbeke, 2002), and that lead (if deployed effectively) to an SCA (Fahy and Smithee, 1999).

This perspective emphasises firm-specific capabilities and assets and the existence of isolating mechanisms as the fundamental determinants of firm performance. However, the RBV literature has failed to explain the nature of these isolating mechanisms (Teece, Pisano and Shuen, 1997) – specifically, how the capabilities can be identified and how they work to give a differential advantage. Taking this dynamic capabilities approach, we can identify the market-sensing capability – which is essentially the ability of the organisation to be aware of changes in its market, and to forecast accurately responses to marketing actions (Day 1994) – as being potentially critical in developing market focus and thus, ultimately, company performance.

This paper proposes a conceptual model that diagnoses market-sensing capability and its relationship to market orientation. Thus it will illuminate the rather opaque issue of the antecedents of market orientation. It also satisfies the crucial research imperatives that RBV and marketing researchers must carefully and systematically identify how particular market-based assets and capabilities contribute to customer value (Srivastava, Fahey and Christensen, 2001), and must also examine the relationship between market orientation and other capabilities (Hult and Ketchen 2001). The proposed model also addresses the causal relationship between market orientation and learning orientation (Bell, Whitwell and Lukas, 2002), and proposes that learning orientation precedes market orientation.

MARKET ORIENTATION

Two important papers published in the *Journal of Marketing* established the beginning of the body of literature that distinguished itself from the historical examination of the marketing concept by terming itself 'market orientation' literature: Kohli and Jaworski (1990) and Narver and Slater (1990). The premise of Kohli and Jaworski was that there had been relatively little attention paid to the marketing concept, and in particular to the implementation of that concept. They set out to probe the operational significance of what they considered to be three core themes or 'pillars' of the marketing concept: customer focus, co-ordinated marketing and profitability. While there has been significant analysis of the market orientation-performance relationship, there has been relatively little activity to identify the factors that cause market orientation (Avlonitis and Gounaris, 1999).

Market orientation and learning orientation

A learning orientation can be defined as the process of improving actions through better knowledge and understanding (Fiol and Lyles, 1985). Learning orientation is significantly related to business performance (Baker and Sinkula, 1999). A learning orientation can be seen as a significant capability. It satisfies the criteria of Barney (1991) for competitive advantage: it is well positioned to provide superior value to customers, complex to develop, difficult to imitate, and appropriate in a dynamic environment (Slater and Narver, 1995).

Theoretically speaking, the market orientation and learning orientation literatures are very close – for two reasons (Bell, Whitwell and Lukas, 2002):

- Both are concerned with understanding organisational cultures and norms.
- Both encompass relationships and interdependencies between individuals and groups and the use of both tangible and tacit resources.

Major studies have included that by Baker and Sinkula (1999), who identified the mediating impact of learning orientation on the relationship between market orientation and performance. But what is the causal relationship between market orientation and learning orientation? (See Bell, Whitwell and Lukas, 2002.) There has been a struggle in the literature with regard to the causality of learning orientation and market orientation (Farrell and Oczkowski, 2002). For Day (1994), a market-sensing facility precedes market orientation; while for Slater and Narver (1995), market orientation is the principal cultural foundation of the learning organisation.

THE RESOURCE-BASED VIEW OF THE FIRM

The assumption underlying the literature that takes a resource-based view of the firm is that the desired outcome of managerial effort within the firm is sustainable competitive advantage (SCA), the achievement of which allows the firm to earn economic rents (Fahy 2001). The key to earning this reward is the possession of critical resources that are firm specific, valuable to customers, non-substitutable and difficult to imitate (Rugman and Verbeke 2002), and that lead to an SCA if deployed effectively (Fahy and Smithee, 1999). While we can distinguish capabilities from resources in theory, in practice they become blurred (Barney, 2002).

This capabilities-based perspective can be used to address the issue of how to develop a market-driven organisation. Day (1994) proposes that organisations can become more market-oriented by identifying and building special capabilities. Day defines capabilities as 'complex bundles of skills and collective learning, exercised through organisational processes, that ensure superior co-ordination of functional activities'. One capability is critical in developing a market orientation: the market-sensing capability, which is essentially the ability of the organisation to be aware of change in its market and to forecast accurately responses to its marketing actions (Day, 1994).

Criticisms of the resource-based view

In their critical 1997 examination, Teece, Pisano and Shuen identified the major limitation of the resource-based view of the firm. This view emphasises firm-specific capabilities and assets and the existence of isolating mechanisms as the fundamental determinants of firm performance. Its key limitation relates to the actual character of these isolating mechanisms:

> This perspective recognises but does not attempt to explain the nature of the isolating mechanisms that enable entrepreneurial rents and competitive advantage to be sustained. (p. 510)

Teece *et al.* (1997) attempted to identify the dimensions of firm-specific capabilities that can be sources of competitive advantage – and to explain how combinations of competences and resources can be developed, deployed and protected. They termed this approach the 'dynamic capabilities' approach.

Priem and Butler (2001) have made the charge against the RBV that it is essentially tautological; "a statement of relationship that is true by logic" (p.58). They instance the assertion by RBV theorists that because a resource is rare and inimitable, it is necessarily a source of competitive advantage. Empirical examination of the resource-based view has been fragmented and limited in scope (Fahy, 2001). There has been relatively little use of the resource-based view as a framework for analysis in marketing strategy (the exceptions include Wernefelt, 1984; Bharadwaj, Varadarajan and Fahy, 1993; Fahy *at al*, 2000).

LINKING MARKET ORIENTATION TO THE CAPABILITIES PERSPECTIVE

The competitive advantage (Day & Wensley 1988) of a firm is based on a complex set of capabilities – that is, "resources that have characteristics such as value, barriers to duplication and appropriability" (Fahy and Smithee, 1999). Market orientation is one of these capabilities. According to Capron and Hulland (1999), the market orientation research by writers such as Kohli and Jaworski (1990) can be linked back to resource-based theory. The strategy literature, and in particular the resource-based view of the firm, provides much scope to develop our understanding of the market orientation construct. Research is needed to explore the potential intricacies of the relationship between market orientation and other capabilities, such as entrepreneurship, innovation and organisational learning, in different market conditions (Hult and Ketchen, 2001). It will also make a useful contribution to the broader strategic marketing literature to acknowledge the role of market orientation as a marketing capability, since progress in measuring market orientation may assist with a further understanding of the nature of marketing knowledge (Fahy *et al.*, 2000).

The market orientation/capabilities interface: the deconstruction of a capability

While distinguishing between three different types of capability, Collis (1994) points out that it is difficult to make distinctions, and it is impossible to develop an exhaustive and mutually exclusive typology of organisational capabilities because of their "infinite variety" (p.145). Day and Van den Bulte (2002) point to the problems of identifying the nature of a capability; this problem is common to many strategy and marketing concepts. They advise the approach taken by Porter (1980), who specified the conditions that determine whether an industry is attractive: his 'five forces' were parameterised so that the theory could be tested. For this reason, Day and den Bulte recommend that a distinctive capability is best identified by decomposing it into distinct elements that can be parameterised. Their approach is influenced by Leonard-Barton

(1992), who defines a "core capability" as "the knowledge set that distinguishes and provides a competitive advantage". Leonard-Barton importantly defines four dimensions to a core capability from a knowledge perspective: employee knowledge and skills; technical systems; managerial systems; and values and norms associated with knowledge creation and control.

Day and Van den Bulte (2002), in their recent and critical examination of the customer-linking capability (Day 1994), deconstruct this capability into three components:

1. **Information about relationships** – the use of data that is trackable, timely and comprehensive to strengthen customer relationships. This approximates to the technical systems dimension (Leonard-Barton, 1992), which covers information databases and procedures.
2. **Configuration** – the organisational structure, incentives and reward or resource commitments that provide the context within which customer information and knowledge flows are embedded. This, according to Day and Van den Bulte (2002), is likely to be a structure that is focused around customer groups rather than vertical functional hierarchies. There are elements of organisational configuration in the "values and norms" dimension of Leonard-Barton (1992) also.
3. **Orientation towards relationships** – this relates to relevant values, behavioural norms, shared mental models, and decision criteria. It approximates to the "values and norms" dimension promoted by Leonard-Barton (1992).

In their study, Day and Van den Bulte found configuration to be the main component of the customer relating capability, with support from the orientation dimension. Information was found to be less significant: it was effectively the beginning of the organisational development process. Employee knowledge and skills, while perhaps implicitly present in Day and Van den Bulte's configuration and orientation dimensions, is not explicitly isolated as a dimension of the customer-linking capability.

Importantly, these distinctive elements are defined relative to the competition. This helps to account for parity of ability in situations where rivals are equally effective (Collis, 1991). Day and Van den Bulte (2002) consider their compositional approach to be a defence against the charges of tautology levelled at the resource-based view (Priem and Butler, 2001).

DEVELOPMENT OF A CONCEPTUAL FRAMEWORK

There has been relatively little analysis of the antecedents to market orientation (Avionitis and Gounaris, 1999). A capabilities perspective (Day, 1994) will facilitate a more meaningful understanding of the development of market orientation. It is proposed that the market-sensing capability (Day, 1994) in particular, acts as an antecedent to market orientation. In order to identify this key capability, it is necessary to unpack or decompose it, following the precedent of the decomposition of the customer-linking capability (Day and Van den Bulte, 2002). A conceptual framework for the decomposition of the market-sensing capability as an antecedent of market orientation is presented here (see Figure 1 below). Day and Van den Bulte (2002) decomposed the customer-linking capability into three dimensions; information, configuration, and orientation. It is proposed that the market-sensing capability is comprised of four dimensions, which have specific resonance in market-sensing activities: Organisation Systems, Marketing Information, Organisation Communication, and Learning Orientation (which was operationalised by Sinkula *et al.* in 1997). Propositions of a positive relationship between these dimensions and market orientation, and ultimately performance, are presented below.

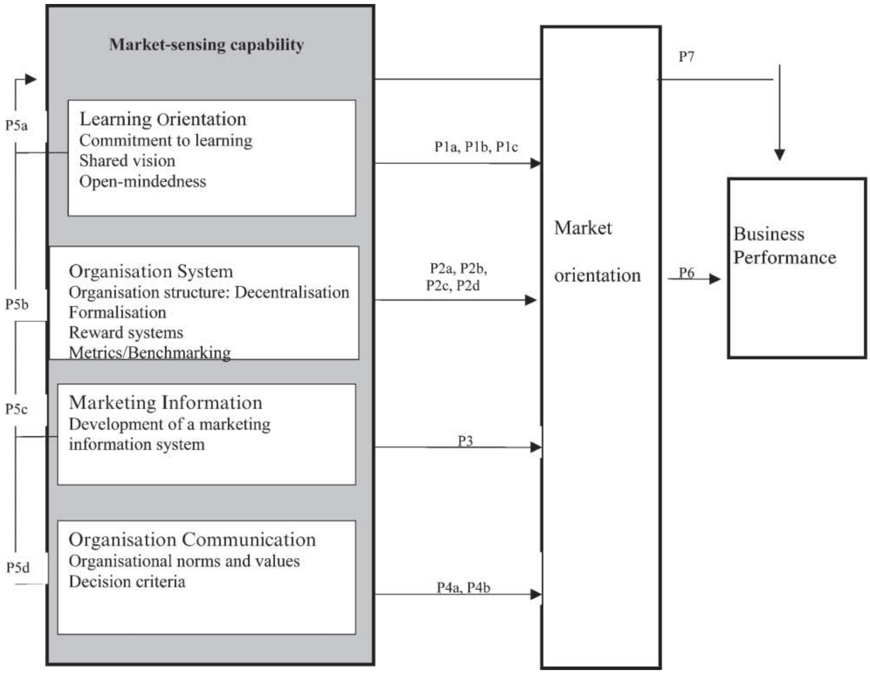

FIGURE 1. Decomposition of the market-sensing capability as an antecedent to market orientation.

It is essential that the sources of learning are not limited to the organisation itself: the scope of market orientation must include all stakeholders and constituencies whose knowledge has the potential to contribute to the business (Slater and Narver, 1995). Baker and Sinkula (1999) point out that a superior learning environment will leverage the use of all resources, including the behaviours that accompany a market orientation. They characterise a learning orientation as affecting a firm's propensity to value generative and double-loop learning – which is critical, because it allows the organisation to change its "view of the world". Day (1994) argues that the market-driven company is well positioned to anticipate the needs of its customers and respond to them effectively: ". . .a market orientation is inherently a learning orientation".

Proposition 1a: The greater the commitment to learning in the organisation, the greater the market orientation.

Webster (1988) emphasises the importance of good HR practice in facilitating a market-driven organisation. This includes attention to the recruitment and development of professional marketing managers. Webster also acknowledges the importance of providing an incentive, and recommends the development of programmes to reward superior marketing performance. The importance of top management involvement in these activities is critical. Webster points to organisational communications and management development resources (including in-company and on-campus executive development programmes, management meetings and seminars, and company publications) as potential vehicles for reinforcing organisational commitment to customer-oriented beliefs and values.

Proposition 1b: The greater the shared vision in the organisation, the greater the market orientation.

"Throughout a market-driven organisation there is an openness to trends and events that present market opportunities" (p.242) – this is how Day (2003) introduces the importance of what he terms "a spirit of open-minded inquiry", the opposite of "close-mindedness".

Proposition 1c: The greater the open-mindedness in the organisation, the greater the market orientation.

Researchers have studied the relationship between strategy and structure for a long time, according to Moingeon *at al* (1998), who link this theme to studies of the creation of competitive advantage in a firm. A positive culture is characterised by an organisational structure that facilitates cross-departmental and inter-functional actions (Ruekert, 1992). The most effective form of organisational structure to assist this communication is the "horizontal corporation", which is characterised by process organisation, flattened hierarchy, teams, customer-driven performance, rewards, supplier and customer contact, and employee training (Byrne,1993). This flat structure is characterised by a lack of centralisation.

Proposition 2a: The less the degree of centralisation in the organisation, the greater the market orientation.

The 1993 study by Jaworski and Kohli finds support for the assertion that centralisation of decision-making serves as a barrier to market orientation. However, the findings differ in relation to the specific element of the construct that is affected. Contrary to the proposition presented in their 1990 study, formalisation (defined by the authors as relating to the existence of formal rules and procedures and the organisation's efforts to enforce these rules) is not found to be significant. Similarly, departmentalisation is not seen as being significant. While it might be thought that emphasis on rules and conformance might make an organisation bureaucratic and hinder market orientation, the authors rationalised the absence of formalisation as an influencing force by arguing that the nature of formalisation rather than the emphasis on rules is important. They argued that some rules can actually facilitate market orientation, e.g. a dictat that departments meet each month for a market assessment meeting. Therefore, it is hypothesised that formalisation will actually have a positive relationship with market orientation.

Proposition 2b: The greater the degree of formalisation in the organisation, the greater the market orientation.

Jaworski and Kohli (1993) note that because a market orientation involves doing something new or different in response to market conditions, it may be viewed as a form of innovative behaviour. The authors point to the importance of countering the negative effects on innovation of centralisation by empowering employees to make decisions – in effect, by decentralising. The importance of the human factor in the organisation as a precursor to developing a market orientation is stated quite emphatically by Webster (1988):

> Perhaps the key to developing a market-driven, customer-oriented business lies in the way managers are evaluated and rewarded. (p.38)

Proposition 2c: The greater the reliance on market-based factors for evaluating and rewarding managers, the greater the market orientation.

The issue of benchmarking is raised by Day (1994, 2003), who recommends benchmarking as a way of moving beyond simple competitor analysis. Benchmarking is not just about doing regular tear-down analyses of competitors products and studying firms for insights into performance; in market-driven firms, benchmarking must involve examination of attitudes, values, and management processes of other firms (Day, 1994). According to Day, the benchmarking process should reveal developments in capabilities and processes that can increase competitive advantage.

Proposition 2d: The greater the use of benchmarking in the organisation, the greater the market orientation.

The information that should be sought by the marketing department to assist in strategic planning, according to Webster (1988), includes the analysis of demand trends, competition and, in industrial markets, the competitive conditions faced by firms in those segments. The importance of strategic planning in influencing the nature of market orientation was later identified by Greenley (1995). Strategic planning requires the development of a sophisticated marketing information system. Webster advocates the dissemination of market information throughout the organisation, so that all employees can help to achieve customer satisfaction. Managers in the organisation should adopt an advocacy role to make the entire business market-driven; Webster sees this as a key role for the corporate marketing staff. However, while there has been an acceptance in the literature that market orientation is informational in character (e.g. Deng and Dart, 1994), the potential role of information as an antecedent to market orientation has not been examined. Avlonitis and Gounaris (1999) do identify the importance of management information systems in the organisation, albeit as being a key success factor in the view of senior management.

Proposition 3: The more developed the marketing information system in the organisation, the greater the market orientation.

Writers such as Webster (1988) effectively set the stage for the later examinations by Kohli and Jaworski (1990) and Narver and Slater (1990) of the implementation of the marketing concept. Webster identifies the values and beliefs involved in building a customer-focused business as being critical, thereby establishing a clear cultural context for market orientation. Echoing Drucker (1954) and Levitt (1960), Webster emphasises the importance of ensuring that everybody in the organisation (not just the marketing people) are customer-focused. Webster sees it as the responsibility of marketing management to make this happen, and sees this advocacy role as a key one for marketing staff. One way of doing this is to ensure that information about customer service and satisfaction flows throughout the organisation.

Proposition 4a: The greater the degree to which organisational values and norms are customer-oriented, the greater the market orientation.

According to Day and Van den Bulte (2002), decision criteria represent an element of orientation towards relationships. Literature cited by Day and Van den Bulte (including Peppers and Rogers, 1997; Wayland and Cole, 1997) include the criterion that there is greater openness to sharing information about customers, instead of each function retaining and perhaps protecting its own information.

Webster (1988) also identifies the use of organisational communications and management development resources to achieve customer orientation. The role of organisational dynamics was assessed by Jaworski and Kohli (1993); they found that interdepartmental conflict inhibits market orientation, and that 'connectedness' promotes market orientation. What has not been examined is how this connectedness and harmony have come about. Perhaps there is reason to believe that the organisational communications and management development resources advocated by Webster play a part.

Proposition 4b: The greater the use of decision criteria that facilitate the sharing of information in the organisation, the greater the market orientation.

Learning orientation is composed of the following elements (Baker and Sinkula, 1999): commitment to learning, shared vision and open-mindedness.

It has been argued that organisational learning without the accompaniment of market-oriented behaviours may actually lead to a decline in performance (Farrell and Oczkowski, 2002). According to Day (1994), a market-driven approach can only emerge if learning processes enable firms to learn about the market.

Proposition 5a: Learning orientation is positively associated with the market-sensing capability.

According to Miller and Whitney (1999), the core of distinctive competence and competitive advantage may lie not in the possession of certain organisational resources or skills that can be imitated by others, but in the configuration of the organisation. Miller and Whitney characterise this as the "orchestrating theme and the degree of complementarity... among mission, means, market, and support systems" (p. 13). The work of the configuration school (including Black and Boal, 1994) influenced Day and Van den Bulte (2002), who showed that configuration is an element of the customer-linking capability. An important aspect of configuration is the organisation system within the organisation; the degree of formalisation and decentralisation, and the linking of reward systems to performance, all of which should facilitate the development of the market-sensing capability.

Proposition 5b: Organisation system is positively associated with the market-sensing capability.

The activity of sourcing, tracking, storing and disseminating information by means of databases and other devices was found by Day and Van den Bulte (2002) to be a component of the customer-linking capability. It is also likely, therefore, that the development of a marketing information system will positively affect the market-sensing capability.

Proposition 5c: Marketing information is positively associated with the market-sensing capability.

Organisation communication is facilitated by cultural factors; the correct organisational norms and values, and decision criteria. This reflects the critical role of corporate culture (Webster, 1988) in developing a market focus. It is also proposed that this open communication will facitate the development of market-sensing.

Proposition 5d: Organisational communication is positively associated with the market-sensing capability.

There is a growing body of literature that supports the links between market-oriented behaviour and company performance, including several papers concerned with the services sector (e.g. Han *et al.*, 1998; Van Egeren and O'Connor, 1998). However, Gray and Hooley (2002) maintain that the evidence, particularly in the services sector, is equivocal, and that relatively little analysis has been done of the moderating effect of the environment on the construct.

Proposition 6: The greater the market orientation of an organisation, the higher the business performance.

This paper proposes that the market-sensing capability leads to market orientation. A significant number of studies have indicated a positive association between market orientation and performance (Narver and Slater, 1990; Kohli and Jaworski 1990; Slater and Narver 1995; Gray *et al.*, 1999).

Proposition 7: The market-sensing capability, though the mediation of market orientation, has a positive effect on business performance.

CONCLUSION

This paper has examined the need to develop more explicit analyses of how market orientation is created in a firm. A conceptual model is developed here within a capabilities framework, based on the decomposition of the market-sensing capability, that can achieve this perspective on the creation of market orientation. The paper also contributes to the literature on capabilities in helping to address the charge of tautology, and provides an opportunity for further empirical analysis of this body of literature. In addition, this model adds to the limited amount of research on the relationship between market orientation and learning orientation.

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