

## **Innovative supply chain in made-in-Italy system. The case of medium-sized firms**

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### **ABSTRACT**

This paper aims to provide the empirical evidence of the interaction mechanism in the open innovation system with particular attention to aesthetic and rational innovation in an Italian creative sector. Factors including rapid technological development, the advent of innovative openness processes involving sub-sectors belonging to diversified supply chains, shorter product life cycles, more diversified and customized, demande and fierce marketing competition, make today's business model increasingly unpredictable and risky. Building on relational based view, resource-based view and network analysis the purpose of this paper is to empirically explore the relationships among supply chain integration (SCI) and inter-company performance in global diversified supply chain. This is an exploratory study and the qualitative research method has been employed. This research has founded its context in the Italian knitwear sector which is part of the creative industries of the Italian fashion system. The data were collected through a series of semi-structured interviews with workers belonging to various areas of activity and with external actors such as yarn suppliers, buyers, institutional and non-institutional lenders. The purpose of this research is also to promote research methodological approaches to analyse different uncertainty scenarios for the future.

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## **1. INTRODUCTION**

For an in-depth analysis of the competitive positioning of Italian manufacturing companies in the structure of the international offer, the fact that the market forms in which they operate are characterized by imperfect competitive conditions must be taken into consideration. Situation in which the changes that arise in the competitive comparison are almost continuous and this causes companies to adopt new technological and operational strategies. These must be the right ones to allow them to maintain the competitive differential against various competitors at least on critical success factors, such as product differentiation, the ability to manage complex order cycles, the use efficiently and on small scale of new process technologies, the use of new materials, etc.

Building on relational based view, resource-based view and network analysis the purpose of this paper is to empirically explore the relationships among supply chain integration (SCI) and inter-company performance in a global context.

About the methodology adopted in the research, still underway, we wish to clarify that the inductive method was used with empirical verification, in order to correctly interpret the management phenomena that emerged regarding supply relationship management.

The purpose of this research is also to promote research methodological approaches to analyse different uncertainty scenarios for the future.

Regarding the structure of the work, in a first part we propose the theoretical framework and the survey methodology, in the second some findings and managerial implications.

## **2. THEORETICAL FRAMEWORK**

The study of the supply chain management (SCM) is based on the analysis of the relationships that are established between the economic actors belonging to the same technological-productive supply chain and between those connected or ‘interdependent’ supply chains. The constitution of evolved forms of partnership, however, is inevitably linked to the interpersonal skills of the individual actors.

We want to highlight that Italian fashion firms are frequently asked to review the positioning of the products offered and to consider that the acquisition of new segments may allow us to achieve a renewed and effective international positioning.

A significant phenomenon is the repositioning in the international supply chain by Italian manufacturing firms operating in the B2B markets of fashion knitwear. In recent years there have been many companies that have modified the content of the strategies and characteristics of their organizational structure in order to protect new ‘interstitial spaces’ (or micro-segments) in international markets. This new and more favourable competitive positioning in the international business markets has been successfully achieved by those companies that have been able to change their position regarding the ‘global supply chains’. Precisely their particular ability to identify in which segments of the sector in which they operate, revealed in particularly critical years, when the international supply system was reorganized, was the element that allowed non-large companies to create differential assets in the competitive context.

In order to effectively exploit resources, firms must not only be able to leverage existing resources but also to develop new and dynamic capabilities to maintain competitive advantage in changing industry environments. This in agreement with the managerial literature about resource-based view (RBV) (Barney, 1991; Teece et al., 1997; Wernerfelt, 1984). Organizations can build these above-mentioned dynamic capabilities through organizational innovations, which are new methods used in business practices, workplace organization, or external relationships.

Many studies show that suppliers are willing to invest resources (organizational, know-how, etc.) only with some of the industrial customers belonging to a larger portfolio. In fact, the need to compete in a dynamic economic and competitive environment encourages the design of forms of cooperation that facilitate the exchange of relationship-specific information (Steinle e Schiele, 2008; Schiele et al., 2011). The following is therefore hypothesized.

H.1 The supply chain integration strategies at the 'supplier side' increases manufacturing performance capabilities.

A further starting point for reflection and managerial investigation is the emergence of new buyer-supplier relationships in new product development (NPD) processes. Industrial innovation based on the involvement of suppliers in specific and experimental 'design-engineering' processes that highlight the need for buyers and suppliers to structure the international bargaining and relational governance in a new way.

More recent NPD studies start to show challenges of managing suppliers in a buyer's innovation process. There is mixed empirical evidence regarding the effectiveness of supplier involvement for enhancing buying company NPD performance. To explain why, the empirical literature has mostly focused on pre-contract strategies, such as supplier's base rationalization, supplier integration, supplier selection, or post-contract tactics, such as supplier involvement timing, supplier design responsibility, or project execution. Relatively less attention has been focused on the contracting process that the buying company uses to motivate supplier participation, which seems to imply as assumption: a supplier is always willing to participate in buyer innovation projects irrespective of the contract. This assumption is problematic because a supplier, as an autonomous organization, could reject a buying company's offer that is either too risky or does not produce enough return for the supplier, especially when the supplier possesses valuable resources for buying company innovation (Barney, 2012). The following is therefore assumed.

H2. The dynamism of the competitive environment represents important motivations for the participation of the supplying companies to NPD initiatives and the development of supply chain relations.

Many studies have pointed to creativity as a principal driver of innovation: individual creativity is identified as a core of creative process that can be enhanced through elements of strategic culture and managerial practices (Stojcic et al., 2018).

This paper aims to provide the empirical evidence of the interaction mechanism in the open innovation system with attention to aesthetic and rational innovation in a creative sector. The purpose of this paper is to provide empirical evidence of the specific open innovation mechanism to improve the design value of innovation processes that focus on aesthetic and rational factors.

Previous research has attracted the attention of research on technological innovation in the technological fields as the main research contexts (Duysters and Lokshin, 2011; Jiang et al., 2010; Spender et al., 2017). Therefore, to obtain a broader picture of the structural characteristics of the innovation ecosystem, this document aims to provide an understanding of aesthetic innovation by focusing on exploring the role of actors (area managers, suppliers, buyers, institutional actors) and of supply chain relationships to facilitate or less innovation in the creative sector.

Firms utilize relationships for competitive advantage by accessing, integrating, and leveraging external resources: relationships are relevant across a myriad of relationship forms, including alliances, joint ventures, supply agreements, cross-sector partnerships, networks, and consortia (Gölgeci et al., 2018).

An extension of resource-based view is the knowledge-based view (KBV) that proposes knowledge as being a firm's most strategically significant resource. Specifically, knowledge is embedded and contained within multiple entities and can converge to enhance an organization's competitive advantage (Grant, 1996). Previous research has examined open innovation and its related interactive mechanism then contributed to the understanding of how generate outcomes in innovative relationships (West and Bogers, 2014; Spender et al., 2017). Evidence regarding the role of actors remains fragmented. For instance, the relationship between innovation creator actors (firms, start up, teamwork) and innovation seekers (founders, business angels, etc.) is understood. The context of R & D collaborations and technology alliances is more analysed (Faems et al., 2010). Thus, research attention to diverse supply chain should be considered.

H3. In turn these organizational innovations may involve operational innovations which are entirely new ways of doing things, like filling orders.

### **3. FROM THE RESOURCE-BASED VIEW TO THE NETWORK ANALYSIS PERSPECTIVE**

Network analysis is a bit relational based view and a bit resource-based view. Within a relational theoretical field, the network perspective sees market as business network, where business units or firms are represented by nodes, and long-term complex interactions between them are represented by links (Håkansson and Ford, 2002).

In the strand of research resource based, academic interest in the prerequisites of business, or strategic networks' successful exploitation is much more recent. From a resource-based perspective firms differ in their capability to shape and exploit networks, to extent that their capability to leverage networks has been identified as distinctive.

With regard to specific network capabilities, it can be observed that if firms seek increased market, innovation and financial performance, they need to develop network specific capabilities (Yu et al., 2013). One such critical capability refers to management skills and competencies in developing

valid views of networks and their potential evolution, a condition to perceive the opportunities embedded in networks.

Recent empirical studies refine the conceptualization of network pictures by testing the dimensions of this concept and adopting a dynamic view, focused on the processes through which networks are understood and strategy enacted within them. Networks are structures that convey information in markets, provide a competitive advantage to some actors over others, and offer opportunities otherwise unavailable (Czakon and Kawa, 2018).

#### **4. INNOVATIVE OPENNESS PROCESSES WITHIN MANUFACTURING SYSTEMS**

Knitwear firms develop processes that seek out and transfer external knowledge into their own productive innovation activities. They are also available to identify with the same supply partners the new co-creative innovative processes to move unutilized internal knowledge to other organizations in the surrounding environment. They are also available to identify with the same supply chain partners the new co-creative innovative processes. We want to put the attention on the wide distribution of useful knowledge, such that no single research organizations or single companies have a monopoly on useful knowledge. This, together with environmental uncertainty and the complexities of innovation, requires more permeable organizational boundaries that enable combinations of innovative resources (within R&D, Manufacturing and marketing areas) beyond and individual actor's resource endowment.

The innovative phenomena found produce value not so much through the collaborative exchange process but also by the participant's ability to capture the value of other innovative actor's value creation effort in cross supply chain innovative processes.

The tension between value creation and value capture is considerably attenuated by the innovative openness phenomena. For example, value creation in open innovation requires firms to be open in order to leverage the knowledge of diverse contributors, while value capture necessitates a tighter, more protective process (paradox of openness) (Laursen and Salter, 2014). This tension is lost in manufactured-based enterprises that are able to industrialize new knowledge in their production systems. Knowing how to process generates the growth of embedded knowledge: this favours the appropriation of the value of 'protective practices'. Managers need to work toward the development of an open-innovation capability, which comprises four value processes: value provision, value negotiation, value realization, and value partake (Appleyard and Chesbrough, 2017; Chesbrough et al., 2018). The value added of dynamic innovative componential lies in structural innovation characteristics and in creative processes.

Many studies have pointed to creativity as a principal driver of innovation. In this paper we want to verify the strategic and operational significance of the impact that innovation has on significant performance parameters such as profitability, financial performance, competitiveness on international markets (see table 1). Based on empirical research, it was possible to more analytically identify a

variety of first and second level metrics. Firms can develop processes to seek out and transfer external knowledge into their own innovation activities. They can also create channels to move unutilized internal knowledge to other organizations in the surrounding environment.

**Table 1.** Metrics (I and II level) for performance evaluation.

<b>Outcomes</b>	<b>Detail level</b>	<b>Micro-level analysis</b>
Market aspects	-Kinesthetic value  -Rational value	-emotion, donning, safety  -increase in opportunities for use
Economic aspects	-Profitability of the firms  -Productive know how improvement  -Employment opportunities  -Economic impact for other stakeholders	- Roi and cash flow of the collection  - productivity of worker and capital  - increase in the know-how of workers  - innovation spillover effects
Knitwer-suppliers relationship	-Relationship specific aspects  -Specific factors at the micro-level analysis	-relationship age, shared business volume  -founders (type and number), dynamism and complexity of innovative projects

Source: our elaboration based on empirical investigation.

It has been found that the greater the knowledge gap between companies, the greater the opportunities that companies can derive from forms of intership (Tomlinson and Fai, 2016)

From here, the following is shown:

- a. the importance of new supply chain relationships in the innovative processes of innovation;
- b. the knowledge gap in the supply chain does not hinder the design of innovative openness phenomena, which may even represent opportunities for small and medium sized firms (SMEs), even in traditional sectors.

In practice, we want to reiterate that the similarity of embedded know-how and R&D architectures among the supply chain actors can even mitigate positive effects.

Generally speaking, this study provides evidences that product innovation has a positive effect on both export propensity and export intensity by increasing the chance of opening new foreign market segments and new competitive processes (Van Bevere and Vandebussche, 2010; Tavassoli, 2018; Wu and Jia, 2018).

Innovation, that is, the propensity for innovation of the companies belonging to the investigated sub-sector is effectively measurable no longer monitoring the amount of investments in R&D over the years, but observing the expansion of the innovative portfolio, i.e. the addition of further 'innovative business models'. Following the empirical survey, it emerges that outputs are more useful than inputs to interpret the positive impact that innovation has on exports; in practice, success on the micro-segments of international markets depends heavily on the variety of business models that arise from innovative business activities. In addition, since considering R&D as a measure of innovation excludes those smaller firms which do not have any separate R&D department, the research focused on the innovative efforts repeated several times over the course of a year by the creative enterprises of the Italian fashion system.

The creativity of the supply chain permeates the supply chain relationship and produces the virtuous following effects:

- they favour the new down-stream supply chains
- they produce positive effects on the supply chain offer
- they generate new cross-industry up stream relationships:
- they favour the resource alignment regarding the technological capabilities in each supply chain enterprise

We focus our attention to technological innovation, in the belief that aesthetic innovation can be either facilitated or inhibited within this open innovation setting where limited protection and dynamic knowledge flows occurring across organizations (Eikhof and Haunschild, 2007; Lin, 2018).

Because incremental and breakthrough innovation involves different types of resources and activities (e.g., Colombo, von Krogh, Rossi-Lamastra, and Stephan, 2017; Qi Dong, McCarthy, and Schoenmakers, 2017), the heterogenous knowledge that a focal firm might be exposed to from its network partners is likely to influence its innovation differently.

In the current economic contexts, we are witnessing profound changes in the processes of structuring supply chains at an international level (Arregle et al., 2009; Cantwell, 2009; Miller and Eden, 2006; Rugman and Verbeke, 2004).

## **5. METHODOLOGY**

This is an exploratory study and the qualitative research method has been employed. With the aim of exploring rational and aesthetic innovation in the creative sector, this research has founded its context in the Italian knitwear sector which is part of the creative industries of the Italian fashion system.

During the empirical survey, forty Italian companies belonging to the Italian luxury knitwear fashion located in central Italy were taken into consideration.

The analysis covered the period 2010-2018 and involved the industrial companies, customers and other economic operators in the supply chain (yarn suppliers, IT service providers, intermediaries, territorial and research entities, etc.)

The data were collected through a series of semi-structured interviews with workers belonging to various areas of activity and with external actors such as yarn suppliers, buyers, institutional and non-institutional lenders.

Owing the study's exploratory nature, we decided to adopt a research methodology based on the use of a qualitative analysis of business cases (Yin, 2003). Case studies have several advantages; first, they allow one to understand the relationships between a phenomenon and its context and enable scholars to match different data that could enhance a research object's analysis (Dubois and Gadde, 2002). Second, as Stake (1995) notes, case study methods allow one to investigate and to interpret new innovative phenomena both in managerial and in strategic sense, in real time.

## **6. REQUESTED SUPPLIER'S PERFORMANCE**

The focus of the studies within channel management literature is to understand how to manage the supplier's commitment and responsiveness to the time-sensitive requests of the company (Figure 1). The behaviour of suppliers in terms of their responsiveness is found to be less a function of competitive pressures and more a function of close relationships and open communication between the focus company and its suppliers (O'Connor et al., 2018).

### **a) Response of suppliers to Operations-based challenges**

Operations-based challenges cover the efficiency of the product development and manufacturing processes. When suppliers perceive their major challenge to be operational in nature, such as product development and human resources productivity, they are likely to resort to business re-engineering type response (to use the answers of the type re-engineering of the business).

Operations-based challenges focus suppliers' efforts on business re-engineering in several ways including automation, research and development, production efficiency, and human resources initiatives (those aimed at increasing worker productivity).

### **b) New product development (NPD) activities in the relational processes of supply chains**

Suppliers contribute to buyers' product innovation efforts in a wide variety of ways. One major benefit can be a more efficient development process, better product quality, and improved product manufacturability.

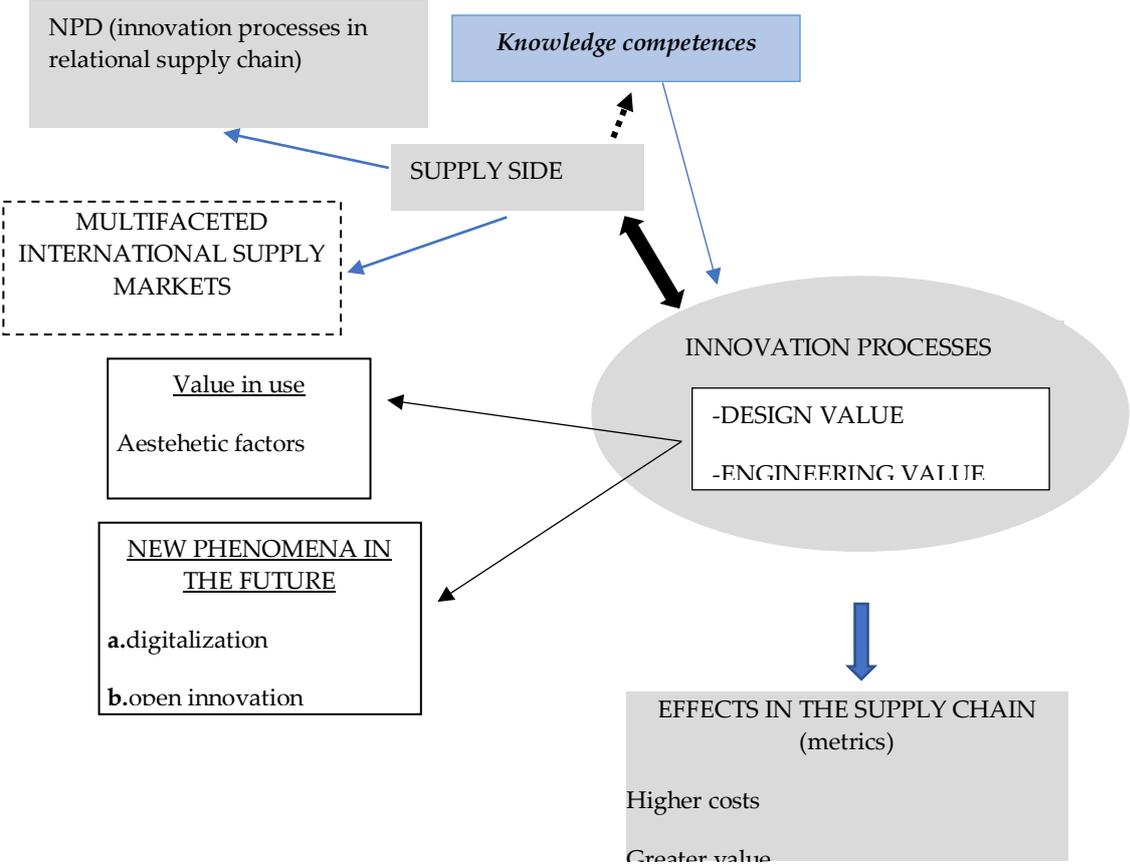
When engaged in the process at the right time with an appropriate level of design responsibility, suppliers contribute to the success of a buyer's NPD project by providing access to advanced technology, helping understand design feasibility, improving translation of customer requirements into manufacturing specifications.

Of the few empirical studies that examine ‘contract design in innovation’, the focus has been on comparing the effectiveness of fixed-price and flexible contracts (cost sharing or performance based) (Gopal and Sivaramakrishnan, 2008; Yan et al., 2018).

The analytical contract management literature has extensively studied contractual coordination in a buyer-supplier production context. The focus of this stream of work is on the design of a contract, specified by parameters, such as revenue share, fixed fee, investment levels, quantity discounts, that maximize supply chain utility by aligning buyer and supplier incentives.

The literature showed that relational governance complements formal contract in more ambiguous, uncertain and complex innovation contexts (Carson et al., 2006; Mani et al., 2012) other Authors find that flexible contracts within a firm provide the greatest incentives for employees to innovate when compared to fixed-fee and pay-by-performance contracts. There are also few studies that examine the effectiveness of fixed price, cost/material sharing, and performance-based contracts vary in different outsourcing contexts.

**Figure 1.** Significant phenomena in a strategic and managerial sense



Source: our elaboration

Although not directly examining contractual design in NPD projects, a few empirical studies discuss potential benefits of aligned goals or risks of conflicting objectives: buyer-supplier conflict intensity is negatively associated with NPD performance.

## 7. CONCLUSIONS

During the empirical survey, it was noted that, especially in recent years, small and medium-sized industrial companies belonging to a supply chain formulate strategies that make them variously interdependent with different supply chain stages.

Small and medium-sized enterprises operating in international business markets become economic actors in stages complementary to those to which they traditionally belong and consequently are included in interdependent supply chains. In this way international supply chains are affected by 'externalities' that increase their indeterminacy (or uncertainty): they increase their weight and their value the intangible elements of the economic relationship, whether established in the context of contractual relations or inserted in strategic partnerships. The study of trust relationships that develop between organizations are particularly important for understanding the evolution of competitive dynamics that have characterized the international business markets in the last few years.

About inter-firm relationship and from a supplier's perspective, it represents an assurance that the relationship will be subject to good-faith modification if it proves detrimental in light of changed circumstances.

Firms increasingly rely on business-to-business (B2B) relationships to gain resources and capabilities. In the context of a B2B relationship, the focal firm means the recipient of resources and the partner firm means the provider of these resources (Zaefarian et al., 2011).

Factors including rapid technological development, the advent of innovative openness processes involving sub-sectors belonging to diversified supply chains (specially at the 'supply-side' level) shorter product life cycles, more diversified and customized demand and fierce marketing competition make today's business model increasingly unpredictable and risky (Sreedevi and Saranga, 2017; Tang and Tomlin, 2008).

Another knowledge indirectly acquired by this research field is to understand how the consistency between the objective and the perceived competitive uncertainty might affect the supply chain.

The purpose of this research is also to promote research methodological approaches to analyse different uncertainty scenarios for the future.

## **8. ORIGINALITY AND RESEARCH VALUE FOR THE FUTURE**

Regarding the improvement of company management, many mature and well-known techniques have been proposed for the analysis of the production process (planning choices, engineering activities) and optimization, including continuous improvement and radical re-engineering approaches (Lehnert et al., 2017).

The current paper investigates empirically the relationship between relatively radical changes in R&D firm-choices occurring within small time windows and an assessment of the extent of the firm's exploratory knowledge activity.

The research provides important contributions for both strategic management and innovation literatures, especially when the author considers the role of firm-specific operations systems resources to drive the innovation of the manufacturing-based firm innovativeness.

The author also contributes to the literature by highlighting useful links that can improve the company's innovation through interaction with industry-level operators (suppliers and buyers) and other external resources such as unusual financial institutions (crowdfunders, angel investors).

This research work allows us to better understand how creativity positively influences companies in the fashion system by implementing radically new innovative processes and efficiently performing production activities.

For the future development of the research work, it cannot be overlooked that in-depth knowledge of the environmental conditions under which the companies implement different types of supply chain risk management strategies, logistics flexibility and relationship flexibility can be a valid aid to the implementation of the most modern also supply chain risk management (SCRM) procedures.

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