

Understanding Value Propositions and Effects Ladders.

Background

A supplier's users are different in how they expect the supplier to respond to their demands. And the supplier's users face the same challenge in relation to meeting the range of unique demands of their customers. There are things that a supplier's user demands that are common across all of a supplier's users, so that its market can be defined as those users with these common demands that it can supply. This common demand is a *symmetric* demand because there is symmetry between what the supplier is offering and how its market is defined in relation to its users.

But there is also an *asymmetric* component of a supplier's users' demands. *Asymmetric* demand is that component of what the user wants that is particular to their way of competing. It is what distinguishes the form of one user's demand within a market from the demands of another. A *value deficit* arises when there is a failure by the supplier to address fully this asymmetric component of a user's demand. That is, a value deficit arises through a failure to address fully the needs of a user's particular way of competing.

Such deficits will always arise in relation to users. But the effects of digitalization on the efficiency and logistical reach of suppliers is also increasing the supplier's ability to organize its response to the user's demand more conveniently and relevantly. The balance of power between the symmetric and asymmetric components of demand is shifting towards having to address the value deficit explicitly in order to counteract fragmenting markets, if not to capture new forms of value [1]. The general tendency to move 'downstream' requires suppliers to face difficult choices in how they balance the differing competitive challenges of the supply- and demand-sides of their business. Value propositions provide an approach to capturing these new forms of value.

In what follows, the relation of a supplier to its user is considered. Insofar as the supplier chooses to address the asymmetric nature of the user's demand, it must understand the nature of the demands on the user by the user's customers within the user's *context-of-use*. This creates a parallel process for the supplier between working with its relation to the *direct demands* of its users, and working with the *indirect demands* of its users arising within each user's context-of-use from the user's relation to the demands of its customers.

Value Propositions

A *Value Proposition* is a proposed relationship with a user that offers a solution, which has a real or intrinsic value in resolving a user's problem. In this definition the user's problem may be, for example, "I want to run a training course" or "I want to do a market analysis". And the appropriate forms of supplier proposition might be "you need to be taught Belbin metrics" or "we will do a market survey for you". But in this definition "the user's problem" is also identified by focusing on the user's own particular relationship to its competitive space, which is the business environment in relation to which the user's responses create or maintain competitive advantage. From the supplier's point of view, this competitive space is the user's way of competing within the user's context-of-use. Key components in this definition are:

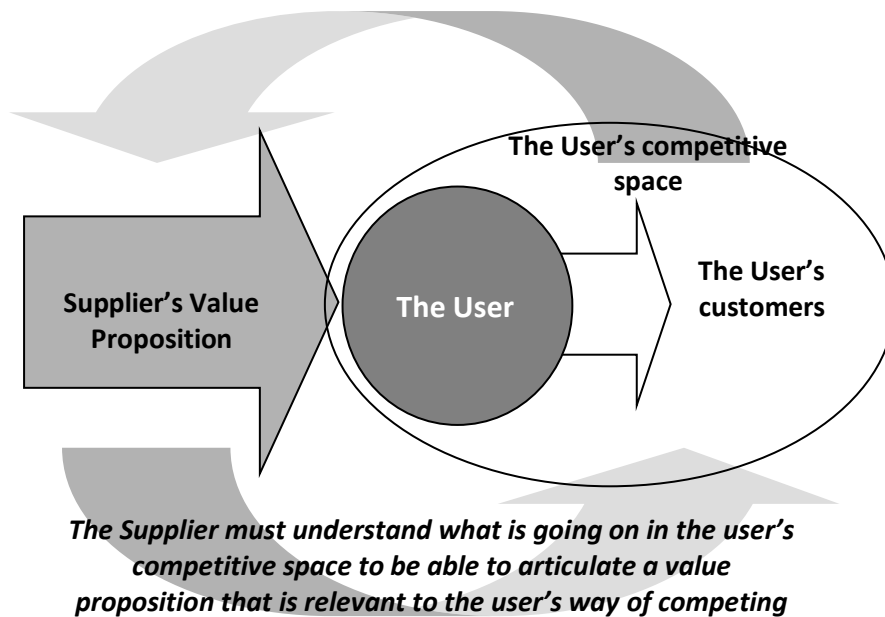


Figure 1: The User's Competitive Space

- ❑ A proposed relationship – a value proposition expresses what the supplier will do to add value to its user's business within the user's competitive space
- ❑ A solution to that user's problem – the supplier's proposition must address meeting the user's problem in a way that is particular to the user's way of competing
- ❑ Has "real or intrinsic value" – the user must be able to perceive how the proposition addresses the user's value deficit, and the more this is so, the more the user will be prepared to pay.

Whatever the supplier is proposing will have a *commercial dimension* – that is the terms under which assistance is provided and the way in which risks and rewards are shared, and an *implementation dimension* that is the manner in which assistance is provided (content/timing/scope). The *value stairs* define how these two things relate to each other within the context of a specific user relationship. It is how these two dimensions come together in relation to the user's organization that enables the supplier to capture value from the way it is creating value for the user. Within the user's context-of-use, value will be expressed by the user in terms of the cumulative levels over time of its revenues minus the associated expenditures. Additional value created for the user will therefore be calculated in terms of the supplier's through-life impact on these cumulative revenues and expenditures.

How will the user determine the value of the supplier's proposal?

The user will only be able to assess the value of a proposition when it is considered within its context-of-use. And this context-of-use is determined by a number of factors, which include:

- The user's chosen strategic position in its competitive space
- The user's response to the user's customers' demand drivers on that strategic position
- The user's owners / stakeholders expectations

In addition, the personal agenda of decision-makers will impact on the perceived value of each of these.

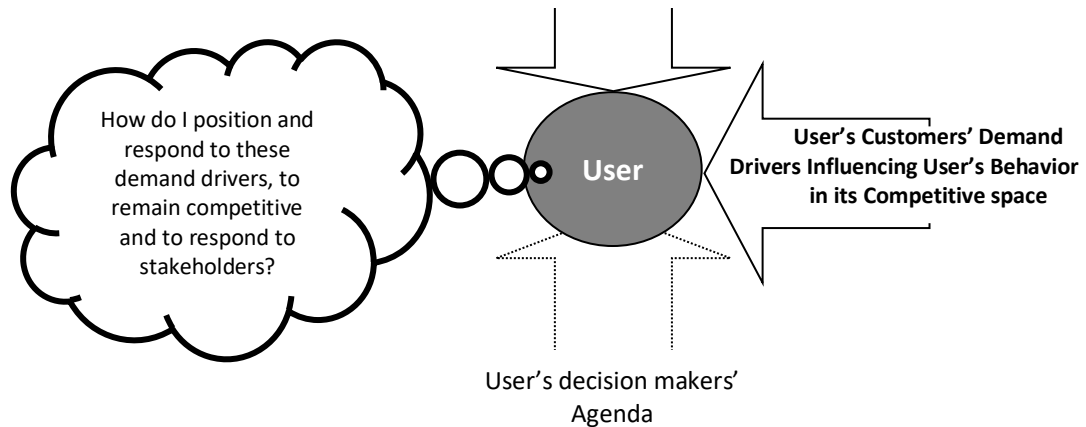


Figure 2: The agenda of user's decision-makers

Therefore, there are different value influences. To understand the dynamics and nature of the influences it is first necessary to understand the relationship between the user and its competitive space. In particular, it is necessary to know:

- How the user chooses to position itself in its competitive space
- any anticipated or proposed changes to this positioning and
- the relationship between the user and the user's customer(s)

A supplier's positioning in the competitive space of the user

Critical to the user's actual or proposed response to its own competitive space is the concept of how the supplier is choosing to position itself in relation to the demands it is facing¹. This is known as the supplier's strategic positioning. The supplier's response to its competitive space will result in its placing a greater, or potentially singular emphasis on either a supply-side or a demand-side approach – in our terms becoming

- 'supply-side oriented' or
- 'demand-side oriented'.

The supplier's strategic positioning may be in a process of moving from one orientation to another and is not a decision made in isolation. The competitive space in which a supplier operates has characteristics – i.e. it is 'organized' in a particular manner; it is also populated by other competitors. The choice a supplier makes about strategic positioning must take these factors into account.

The supply-side oriented organization

The supply-side oriented organization will be internally focused and will attempt to provide a relatively homogeneous product or service into the competitive space based on symmetric assumptions about demand. Its approach to the user's competitive space will be dominated by supply-side thinking. Examples of 'supply-side oriented' organizations are: automobile and component manufacturers, package holiday companies and clothing manufacturers.

A *supply-side* oriented organization primarily organizes itself around the efficiency of internal processes and operations - for example, competing on cost and reliability, or around the nature of the product itself in terms of product range, product or service features, etc. The management mind-set throughout a supply-side oriented organization prides itself on meeting internally generated performance targets in relation to market segments defined by the nature of their product or service [2].

¹ The emphasis here is because these same distinctions can also be applied to the user. Only a demand-side oriented supplier will concern itself explicitly with rKP-type propositions, although it may still be providing them implicitly through informal processes.

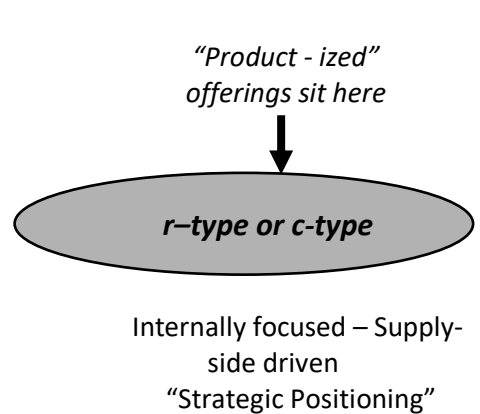


Figure 3: The r-type or c-type proposition

The propositions emanating from a supply-side oriented organization are of two kinds: first, a proposition that can be easily reproduced by that organization (and, to some extent, competitors) in a way that ignores differences between users’ contexts-of-use, referred to as an *r-type* proposition. An example would be the r-type proposition of a manufacturer of petfood:

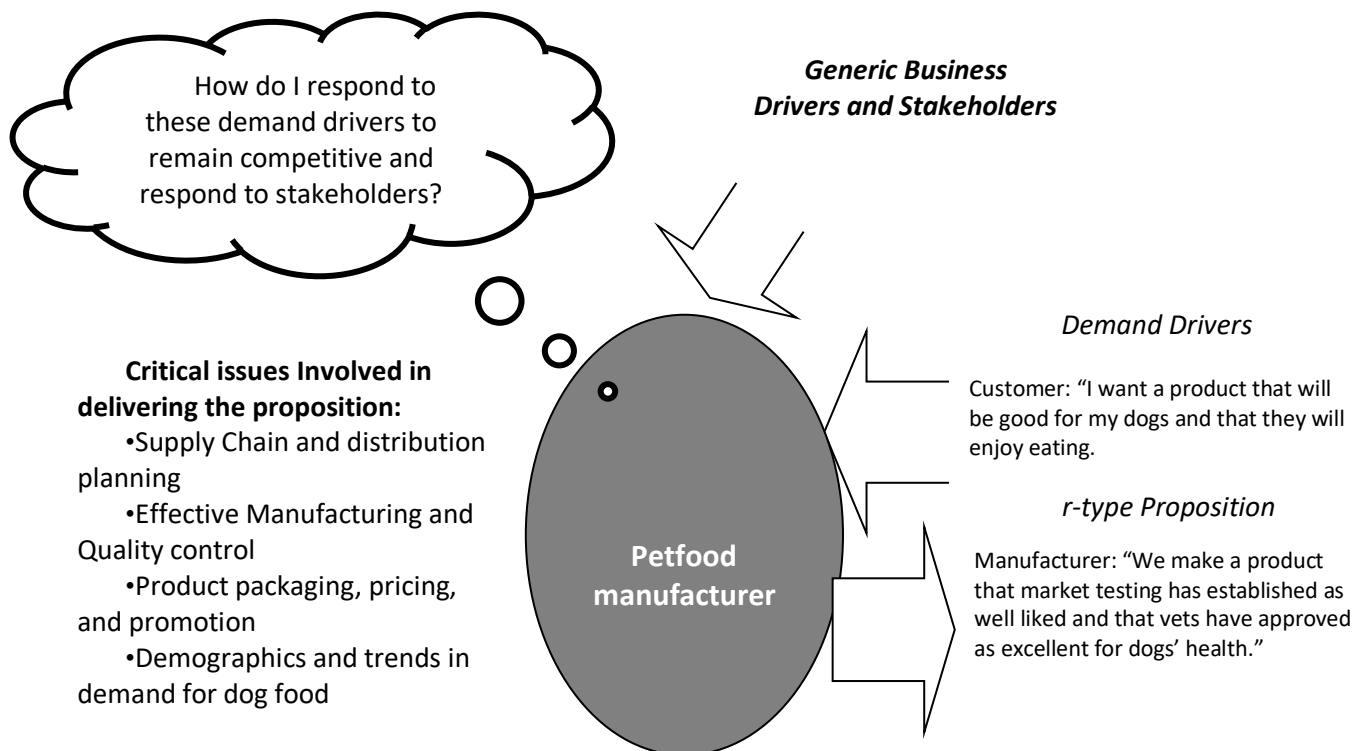


Figure 4: A petfood manufacturer’s r-type proposition example

Second, a ‘customization’ proposition (*c-type*) – a proposition which offers to provide experienced and skilled resources and capabilities to the user in a way that can be customized to a user’s particular use of it, where those resources and capabilities have to be used by and under the direction of the supplier. The supplier retains design control over the forms of customization possible.

The demand-side oriented organization

A ‘demand-side oriented’ organization organizes itself around the requirements of its users within their contexts-of-use – for example, competing on responsiveness to specific requirements, competence, flexibility, quality, personalization, and total “customer

intimacy” [2]. Its approach to the user’s competitive space will be dominated by the demand-side issues (e.g. personal and specific customer requirements or problems) that the user is facing in organizing its response. Thus a *demand-side* oriented organization primarily focuses itself around satisfying the demands of its users that are particular to them within their contexts-of-use.²

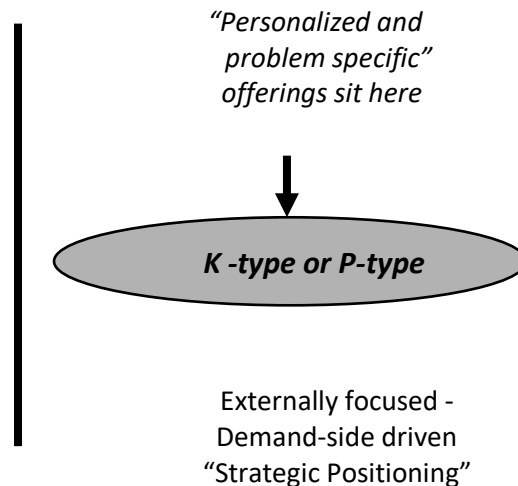


Figure 5: The K-type and P-type propositions

The propositions emanating from a demand-side oriented organization will utilize the organization’s capabilities, know how, and problem identification expertise in response to the demands of its users within their competitive space; the propositions that do this being referred to as K-type and P-type propositions (see ‘Effects Ladders’ below).

The demand-side oriented organization will be externally focused and will attempt to provide a relevant and personalized response to its user. As a result of this it will, in addition to responding to a particular user’s requirement, introduce some form of change into the way the user’s competitive space is currently organized. This fact may provide temporary or lasting competitive advantage for the user.

Examples of ‘demand-side oriented’ organizations are: supermarkets, private health specialists; bespoke tailoring; specialist tour operators; private banking organizations; specialist motor manufacturers; consultancies; event organizers.

In a demand-side oriented organization, the value proposition offered by a supplier to a user may be one of, or a combination of, the following:

- a ‘Problem identification’ proposition (*P-type*)³ – a proposition which defines how the demand situations which are affecting the user’s customers should be organized, identifying the issues and problems to be addressed in arriving at appropriate solutions, and then delivering those solutions.⁴ The supplier is able to deliver this proposition by working with the user’s relationship to their customer and applying the supplier’s own (high level of) experience and knowledge.
- an application of a ‘Know-how’ proposition (*K-type*) – a proposition which offers to take responsibility for the definition of a solution to a particular set of issues and problems and delivering that solution to the user in a way that is particular to the

² This is why the transnational model is so relevant to the supplier’s chosen demand-side strategic position. The whole concept of the transnational organization is one of agility, enabling teams to develop appropriate responses (value propositions) to their “local” user(s) by drawing on supporting global infrastructures in the particular ways that allow them to satisfy the particular needs of their user(s).

³ P also stands for ‘pain’. The user has a pain, and wants it to be formulated as a problem that can be ‘solved’.

⁴ The P-type proposition therefore creates a demand organization that can be targeted by K-type propositions.

user's relationship to their customer. The user exercises design control over the solution and the solution is uniquely aligned to its customers.

An example of a demand-side oriented business and a K-type proposition would be a supermarket:

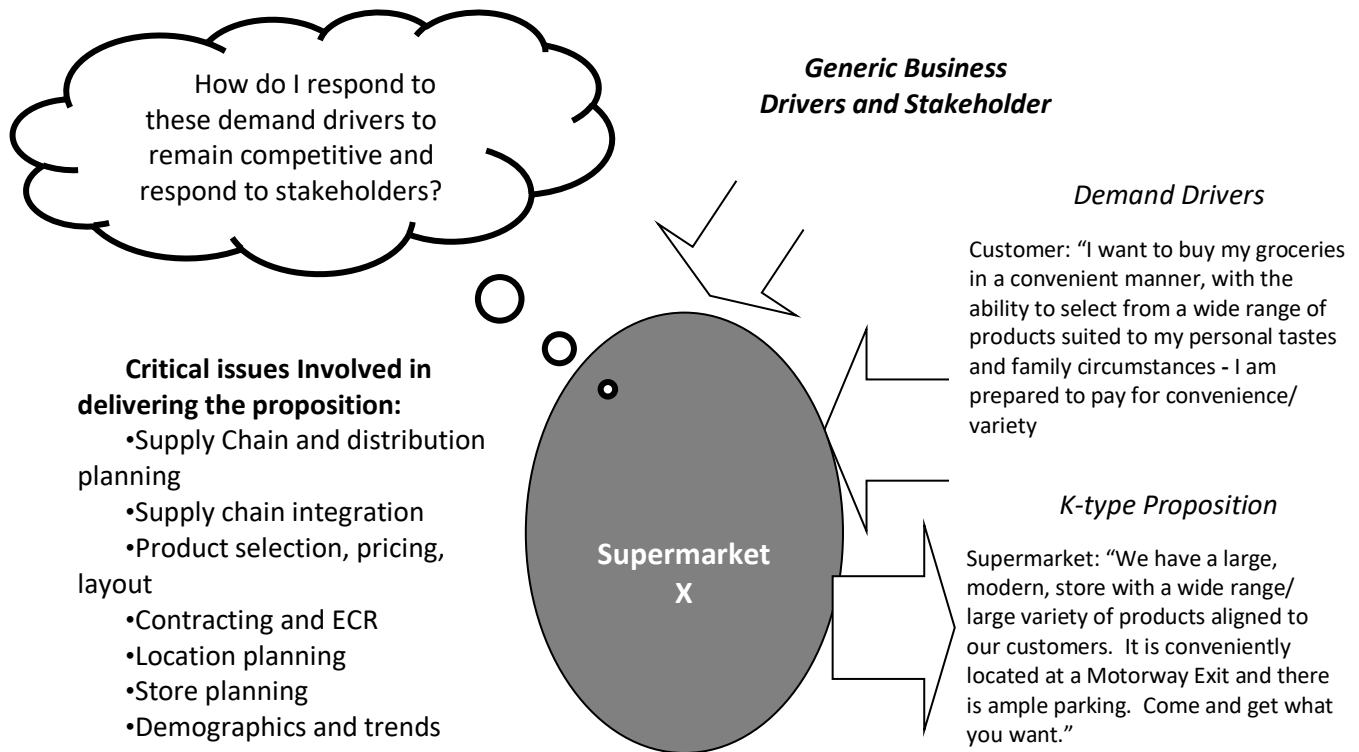


Figure 6: A supermarket K-type proposition example

'P-type' propositions can be found in the office facilities / building competitive space:

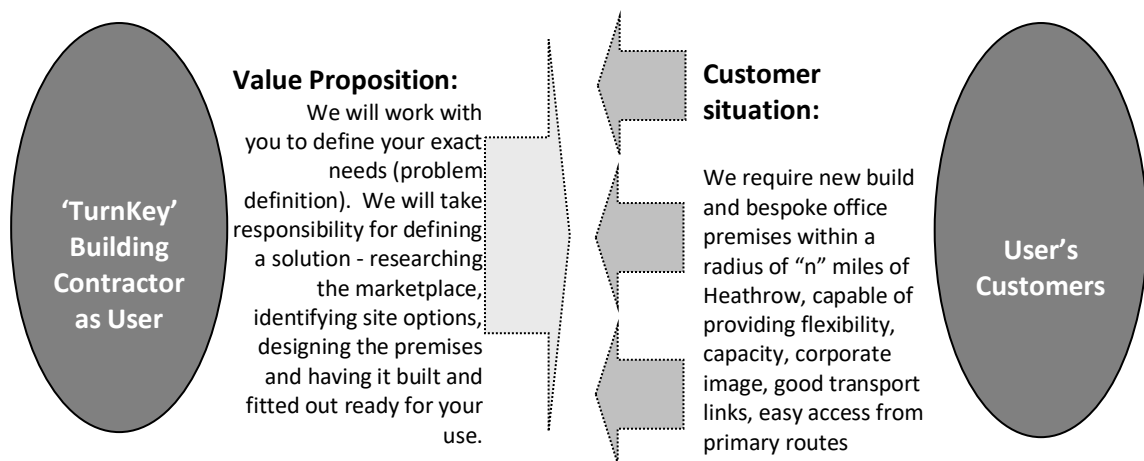


Figure 7: An example of a P-type propositions in the office facilities/building competitive space

The Turn-key Building Contractor Example

In this example, the contractor is offering a 'P-type' proposition – helping to define the exact needs of the user's relationship to its customers (the building's occupants), so that the user can remain competitive in its competitive space – the supplier taking responsibility for the delivery of the solution through K-type propositions that will make use of their own and other sub-contractors' c-type capabilities. These propositions – and their result – would only

be attractive to the user – and of perceived value – if they focused on solving the needs of the user’s relationship to its customers within the user’s own competitive space.

The parallel in the consultancy competitive space would be what Gartner refers to as the “one stop” management consultancy / business integrator practice.

Supply-side vs demand-side oriented organizations and Effects Ladders

From the Supplier’s perspective the fundamental difference between the two types of approach to propositions is explained by the following attitudes:

- The Supply-side oriented supplier (r-type or c-type propositions): Does as much as possible for the supplier’s business without jeopardizing the relationship with the user.
- The Demand-side oriented supplier (K-type or P-type propositions): Does as much as possible to identify and resolve the user’s problems without jeopardizing the sustainability of the supplier’s business.

For the demand-side oriented supplier, the *Effects Ladder* becomes the means of understanding the particular way(s) of organizing the user’s response to the demand situations of its customers, thus defining the particular problems that can be targeted by the supplier’s propositions. This Effects Ladder is therefore used to describe the relationship between the user and the user’s customers.⁵ Thus, the Effects Ladder enables the supplier to understand the user’s relationship to its competitive space, enabling the supplier to provide relevant, and therefore attractive, K-type and P-type value propositions.

The Effects Ladder

This Effects Ladder has a number of characteristics:

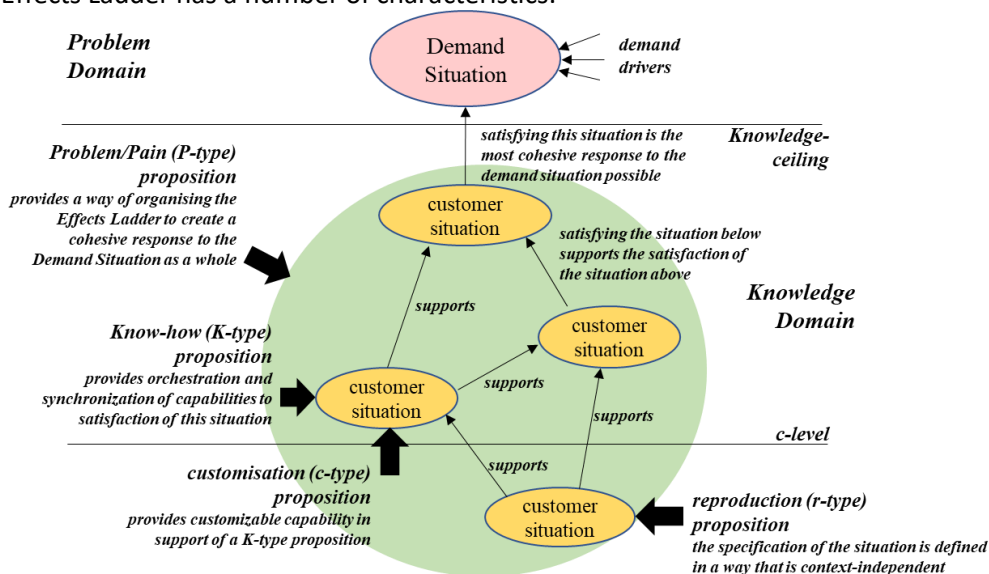


Figure 8: The Effects Ladder

- The demand situation being addressed by the user is broken down into a number of subordinate problems (customer situations for the user), which together organize the user’s response to its customer’s demand situation. These may be targeted individually or severally by propositions.
- Above the *K-ceiling* is the domain in which problems are too large and/or intractable (the *Problem Domain*), requiring that they be broken down into an effects ladder of

⁵ The Effects Ladder is thus describing the *indirect* effects that the supplier wants to have on the way the user competes within its competitive space, i.e., effects that change the way the user relates to its context-of-use.

problems below the K-ceiling (within the *Knowledge Domain*) that are not too large and/or are tractable.

- *c-level* is the level below which problems can be solved with no knowledge of the user's context-of-use. These problems below *c-level* are the ones amenable to *r-type* or *c-type* propositions alone.

The domain between *c-level* and the *K-ceiling* (the *Knowledge Domain*) is constantly moving, as both suppliers and users learn new ways of creating value (hence both *c-level* and the *K-ceiling* rising!). It is this zone that is targeted by a demand-side oriented supplier.⁶

The key challenge facing a demand-side oriented supplier is how it manages the risks of targeting effects ladders with propositions that make the supplier's business sustainable.

The rKP cycle

The question of sustainability of the supplier's business can be understood in terms of two dimensions:

- The demand-side user *engagement* ('intimacy') of the supplier business, and
- The *defensibility* of the know-how that is the basis of its propositions. This defensibility will determine the profit potential of the propositions, and is the other side of its imitability by competitors, which will be partly a function of the nature of the underlying technology, and partly of the business processes by which that underlying technology is brought to bear on the user's situations. The processes of knowledge diffusion will ultimately reduce defensibility however good the patent protections.

This gives us the following diagram:

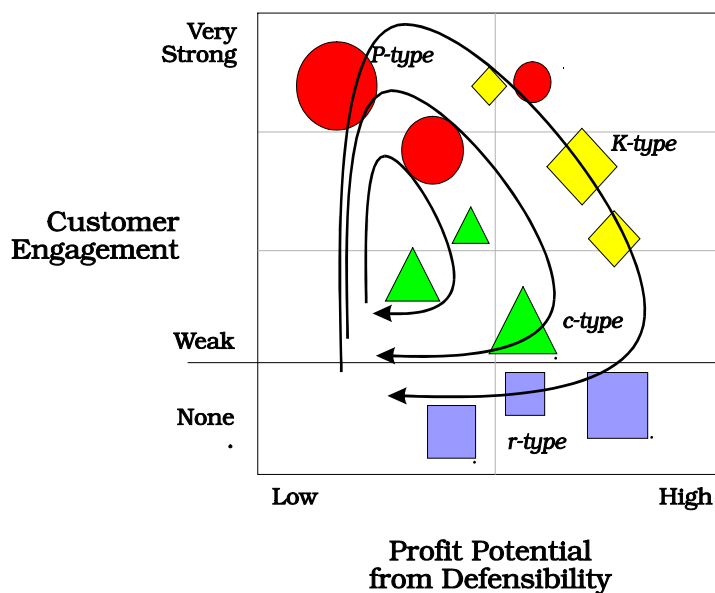


Figure 9: the rKP Cycle

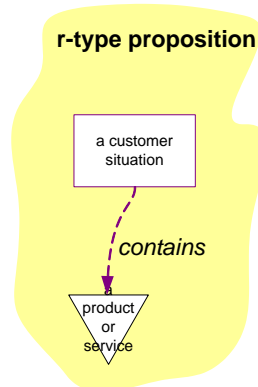
The distinction between supply-side and demand-side orientation will be reflected in the economics of the *K-type* and *P-type* propositions versus those of the *r-type* and *c-type* propositions. The general point to be made about this cycle is that globalization accelerates the diffusion/commoditization of know-how, placing increasing emphasis on the ability to profit from the *PKc* part of this cycle.

⁶ Note that propositions that target the *K-domain* assume demand asymmetry, while *r-type* and *c-type* propositions targeting below *c-level* assume symmetry.

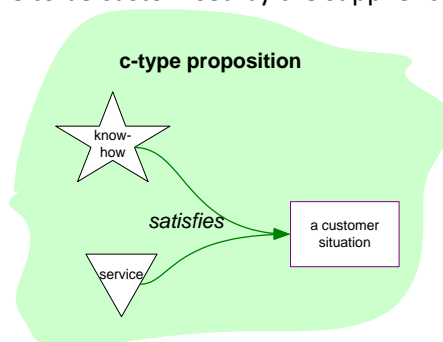
Appendix – PAN representations

These different kinds of proposition each correspond to different structural conditions within a PAN model. Thus

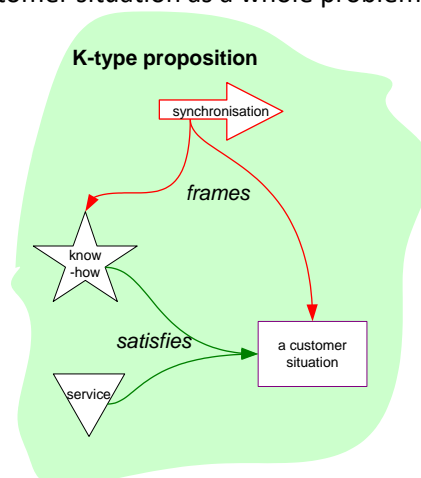
- With the r-type proposition, the relationship of an outcome to a customer situation is solely one of ‘contains’ – the outcome is something that gets used by the customer situation but has no relationship to it as a context-of-use.



- With the c-type proposition, the outcome does have a relationship to the customer situation as a context of use, represented by there being a ‘satisfies’ relationship. This has to be accompanied by a relationship to know-how (and/or design) that enables the outcome to be customised by the supplier to the customer situation.

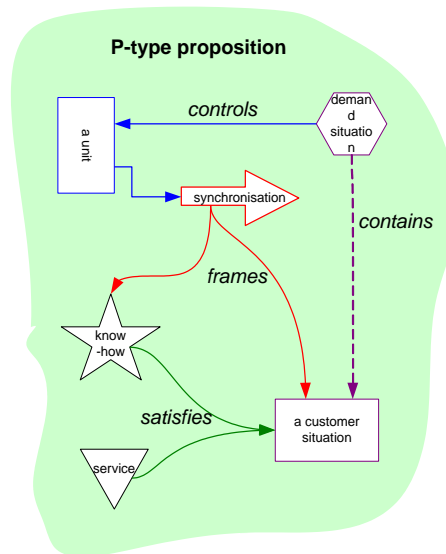


- The K-type situation takes this a step further by adding a synchronisation relationship that can govern the way the outcome is used alongside other outcomes in satisfying the customer situation as a whole problem.



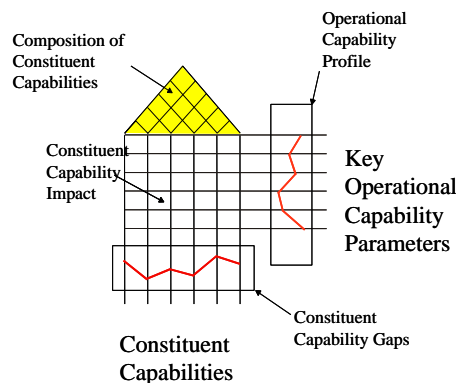
- Finally, the P-type proposition adds a ‘controls’ relationship between the containing demand situation and the unit controlling the synchronisation relationships governing the K-type relationships. Note that the form of the effects ladder represented in PAN will be the result of a P-type process. The presence of this

‘controls’ relationship is therefore just to indicate that the commercial design of the value propositions is subordinated to the needs of the demand situation.



Geometries-of-use

In a PAN stratification, the effects environment requires particular synchronisations of operational capabilities. Each one of those operational capabilities itself has to have capability parameters that must be satisfied and can be represented as a capability profile. A geometry-of-use is then the set of constituent capabilities that must be orchestrated in order to support the required profile and synchronised with other operational capabilities to produce the effects – the yellow composition ‘hat’ in the diagram below. (In the PAN model, the constituent capabilities are the ‘outcomes’ with a ‘satisfies’ relationship to the customer situation.) The relationships between all of these things can be summarised in the following QFD format as follows:



In describing the orchestration and synchronisation of constituent capabilities, it is useful to distinguish two kinds of design and/or know-how:

- P-type and K-type design and/or know-how which has a direct relationship to the customer situations within an effects ladder as a whole⁷, indicating that it has to anticipate the consequences of its actions on the customer situation(s), in particular their indirect effects within the demand situation as a whole; and
- r-type and c-type design and/or know-how that does not have a direct relationship to the customer situation, only dealing with the way the outcome is itself formed⁸.

⁷ These are ‘green dot’ processes that are difficult for competitors to imitate because of their dependency on customer intimacy.

⁸ These are ‘red dot’ processes that can be defined independently of the customer situation, and are therefore more vulnerable to imitation.

References

1. Hagel III, J. and J. Seely Brown, *The Only Sustainable Edge: Why Business Strategy Depends on Productive Friction and Dynamic Specialization*. 2005, Boston, MA: Harvard Business School Press.
2. Treacy, M. and F. Wiersema, *The Discipline of Market Leaders: Choose Your Customers, Narrow your Focus, Dominate Your Market*. 1995, London: Harper Collins.

Glossary

demands

- context-of-use** – the context within which a user makes use of a product or service provided by a supplier, likely to be shaped by the user’s relationship to its own customers. 1
- direct** – the demands arising directly from a supplier’s users..... 1
- indirect** – the demands from a supplier’s user arising within each user’s context-of-use from the user’s relation to the demands if its customers. 1

effects ladder

- the means of understanding the particular way(s) of organizing the user’s response to the demand situations of its customers, thus defining the particular problems that can be targeted by the supplier’s propositions..... 7
- c-level** - the customization level below which problems can be solved with no knowledge of the user’s context-of-use. These problems below c-level are the ones amenable to r-type or c-type propositions..... 8
- K-ceiling** – the level below which problems are not too large and become tractable. 7
- Knowledge Domain** – the domain in which problems are not too large and become tractable..... 7
- Problem Domain** - the domain in which problems are too large and/or intractable..... 7

orientation

- demand-side** – the orientation of an organization around satisfying the demands of its users that are particular to them within their contexts-of-use. 5
- supply-side** – the orientation of an organization around the efficiency of internal processes and operations. The management mind-set throughout a supply-side oriented organization prides itself on meeting internally generated performance targets in relation to market segments defined by the nature of their product or service. 3

relation to demand

- asymmetric** – that aspect of a user’s demand that is particular to their way of competing, and which distinguishes the form of one user’s demand from another’s..... 1
- symmetric** – demands that are common across all of a supplier’s users defining the supplier’s market..... 1
- value deficit** – that which arises when the supplier fails to address fully the asymmetric component of a user’s demand. 1

value proposition

- a proposed relationship between a supplier and a user that offers a solution, which has a real or intrinsic value in resolving a user’s problem..... 1
- 1r-type** – a proposition that can be easily reproduced in a way that ignores differences between users’ contexts-of-use..... 4
- 2c-type** - a proposition which offers to provide experienced and skilled resources and capabilities to the user in a way that can be customized to a user’s particular use of it, where those resources and capabilities have to be used by and under the direction of

the supplier. The supplier retains design control over the forms of customization possible.	4
3K-type - a Know-how proposition which offers to take responsibility for the definition of a solution to a particular set of issues and problems and delivering that solution to the user in a way that is particular to the user’s relationship to their customer. The user exercises design control over the solution and the solution is uniquely aligned to its customers.	5
4P-type - a proposition which defines how the demand situations which are affecting the user’s customers should be organized, identifying the issues and problems to be addressed in arriving at appropriate solutions, and then delivering those solutions. P stands for ‘problem’ but also stands for ‘pain’. The user’s customer has a pain, and wants it to be formulated as a problem that can be ‘solved’. The supplier is able to deliver this proposition by working with the user’s relationship to their customer and applying the supplier’s own (high level of) experience and knowledge.	5
sustainability	
defensibility - the other side of a proposition’s imitability by competitors, partly a function of the nature of the underlying technology, and partly of the business processes by which that underlying technology is brought to bear on the user’s situations. The processes of knowledge diffusion will ultimately reduce defensibility however good its patent protections	8
engagement – the extent of the supplier’s intimacy with the user’s business.	8
value stairs	
- a relationship between the commercial dimension of a value proposition and its implementation dimension within the context of the specific user relationship.	2
commercial dimension - the terms under which assistance is provided and the way in which risks and rewards are shared between supplier and user.	2
implementation dimension - the manner in which assistance is provided (content/timing/scope).....	2