

# Ideal Types of Strategic Innovation

## *An Exploratory Study of Chinese Cosmetic Industry*

Xu Yang<sup>1</sup>, Sreenivasan Jayashree<sup>1</sup> & Govindan Marthandan<sup>2</sup>

<sup>1</sup> Faculty of Management, Multimedia University, Cyberjaya Campus, Persiaran Multimedia, 63100 Cyberjaya, Malaysia

<sup>2</sup> Graduate School of Management, Multimedia University, Cyberjaya Campus, Persiaran Multimedia, 63100 Cyberjaya, Malaysia

Correspondence: Xu Yang, Faculty of Management, Multimedia University, Cyberjaya Campus, Persiaran Multimedia, 63100 Cyberjaya, Malaysia. Tel: 86-139-6127-2319. E-mail: yangsunyaa@gmail.com

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### **Abstract**

The purpose of this paper is to research strategic innovation in the Chinese cosmetic industry. The constituents of strategic innovation were analyzed from nineteen types of strategic innovation in the paper. With Exploratory Factor Analysis, the result of this paper came up with the concept of strategic innovation for the cosmetics industry in the Chinese market. Strategic innovation could be defined as: Strategic innovation is anything that tends to create new market, by enhancing product or service value in order to disrupt competition.

**Keywords:** strategic innovation, Chinese cosmetic industry, new market creation, product value addition, competitive disruption, service value addition

### **1. Introduction**

Strategic innovation research was conducted during the 1980s and early 1990s (Burgelman, Kosnik, and Van, 1988). Gary (1998) mentioned that strategic innovation was the only method for small companies and new comers to be successful as they have minimum resources. Strategic innovation is believed to create strategies, and come up with unique products or services and new processes to improve growth to change the game and produce new value for corporations (Derrick and Soren, 2007).

In a specific industry, with the deepening of globalization, an enterprise with a dominant position could further expand for market share, while firms which have fallen into an inferior position should analyze the main causes of the gap, and try to create something new in order to seek a unique market space. At this point, the traditional strategic model is facing severe problems and the traditional mode of operation is unable to meet business survival needs. The absolute importance of strategic innovation in the modern competitive climate has also been tested widely. Meanwhile, cosmetic firms in the Chinese market are competing intensely (Wu & Pangarkar, 2006). Globalization has changed the environment of these firms. Many cosmetic firms need to recombine available resources according to their environment. Thus, strategic innovation becomes one of the core competitiveness for these firms (Snyder & Duarte, 2003). This study focuses on the constituents of strategic innovation within the cosmetic industry in the Chinese market.

Strategic innovation reconceptualized the companies' business models and reshape their existing markets. Strategic innovation could build a new market share (Kim & Mauborgne, 1999), and strategic innovation means changing the rules of the game of the corporations (Markides, 1997). Moreover, strategic innovators are believed to be able to overcome conventional logic by developing a new 'theory of the business' that creates a new market space (Kim & Mauborgne, 1999). Researchers like Rajoapalna and Speritze (1996) believe that strategic innovation is to achieve sustained growth by responding to the external environment and internal changes.

### **2. Research Problems and Question**

Foreign firms have managed to dominate the Chinese cosmetics market by being quick in entering the market,

and introducing their brands through heavy investments (Ronald Ho, 2002). These firms generate a majority of the whole industry revenue, and they are preferred by consumers over domestic cosmetic firms. Multinational companies developed strong footprints while Chinese companies have not developed adequate practices for innovation (Dekkers 2009). With the rapid development of foreign cosmetic firms in the Chinese market, their strategies are imitated simply by domestic cosmetic firms for better performance (Li & Chen, 2011). The question of whether strategic innovation influences corporate profitability and growth has not been seriously considered by Chinese domestic cosmetic firms.

Although the cosmetics industry has been increasing at an annual increase of 13 percent in the past decade (TNS project, 2007), the domestic cosmetic firms still have trouble in acquiring a strong competitive power in the marketplace. Chinese cosmetic enterprises face competitive pressures of globalization. China's cosmetic firms need, not only practical experiences in business strategy development but also support from a theoretical foundation (Wu, 2002). There were some research on specific industry, country and only famous companies were analyzed (Cho & Pucik, 2005; Elenkov et al., 2005; Jackson & Debroux 2008). Past researches had provided models that were based on theoretical concepts. The models were not validated with empirical data and did not go through a series of statistical tests to assess psychometric properties (Brainard & Tobin, 1968) and though the relationships among strategic innovation, profitability and growth were analyzed in past literature (Cho & Pucik, 2005), Chinese firms were not included in the analyses.

The aim of this paper is to explore the constituents of strategic innovation in the Chinese cosmetic industry. Two kinds of firms are involved in this study. One is foreign cosmetic firms which are doing their business in the Chinese market, and another is domestic cosmetic companies which sell cosmetics to local customers. In order to achieve the research objectives, only cosmetic firms which were involved in strategic innovation were chosen as samples.

### 3. Literature Review

There have been a growing number of researches discussing about strategic innovation over the past decades. Strategic innovation is a crucial means to create competitive advantage (Baden & Pitt, 1996; Baden & Stopford, 1994) and to beat the commodity magnet (Rangan & Bowman, 1995). Strategic innovation refers to a situation in which firms succeed dramatically in attacking an established industry leader (Markides, 1997; 1998), thus creating competitive advantage. In some researches, strategic innovation is used for creating a new marketplace (Kim & Mauborgne, 1999) by firms changing the rules of a game, and not by playing a better game than other players (Markides, 1997). Drucker (1994) believes that the competitive game is driven by firms following well-defined traditional approaches to the market. Authors such as Baden & Stopford (1994) have argued that many industries pose the challenge of maturity in which established and unquestioned mindsets of managers lead to more or less fatalistic attitudes. Rajoapalna and Speritze (1996) believe that strategic innovation achieves sustained growth by responding to the external environment and internal changes. With strategic innovation, firms could distribute qualified services with new methods to distant customers. Firms also need to build up multi-disciplinary exercises for the changing rules (Derrick & Soren, 2007).

Some former practitioners and researchers treat strategic innovation as an all-inclusive term even though they are referring to very different events and processes (Cooper, 1990). The definition of strategic innovation from Daft and Becker (1982) includes different types of innovation, like new services or products. Damanpour and Schneider (2006) believe innovations could be a new product/service, a new structure or administrative system, a new production process technology, or a new plan or program, process, product, or service which is new to organizations. According to Zain (1995), strategic innovation is always the output of successfully matching organisational requirements with environmental changes e.g., new ideas, process, techniques and services. After reading literatures, totally nineteen types of strategic innovation were gathered. Table 1. lists the ideas from literature.

Table 1. Types of strategic innovation

Types of strategic innovation	Authors
Product Innovation	Goldenberg & Mazursky, 2002
Packaging Innovation	Matusow, 2010
Research and Development	Martin & Michael, 1994
Communication innovation	Chua & Morris, 2009
Corporate Financial Innovation	Bhattacharyya & Nanda, 2000
Human Resource Innovation	Holbrook & Hughes, 2000
Material Innovation	Parker, 1986
Alliance and Network	Cooke, 1996
Sale channel innovation	Stuart, 2010
Marketing Innovation	OECD, 2005
Mergers & Acquisitions	Vijay & Rakesh, 2008
Inbound Logistics Innovation	Sameer, Cindy & Michelle, 2006
Outbound Logistics Innovation	Sameer, Cindy and Michelle, 2006
Operations Innovation	Hammer, 2005
Sales Innovation	Stevenson, 2011
Service Innovation	Nijssen et al., 2006
Procurement Innovation	Denali, 2010
Technology Innovation	Sagar, 2006; Butler, 2006
Firm Infrastructure Innovation	Michael et al., 2009

Goldenberg and Mazursky (2002) believed with product innovation, the firm made new products, or upgraded old products to meet consumer demands. Matusow (2010) said packaging Innovation was the firm used new packaging and new designs of brands and entire product categories to show the inner spirit and the unique organizational culture of the enterprise. Martin and Michael (1994) thought the firm already set a Research & Development centre to revise product technology and range of products. Chua and Morris (2009) thought communication innovation was the firm found ways to better active listening and feedback to conquer barriers to transmit ideas and information to consumers, employees and share holders. Bhattacharyya and Nanda (2000) said financial innovation was the firm already developed a corporate financial system in order to improve operational efficiency and reduce costs and risks. Holbrook and Hughes (2000) said human resource innovation was the firm already developed some new programs to better retain and recruit employees. By material innovation (Parker, 1986), the firm made some material qualities improvement. Cooke (1996) thought alliance & network was the firm had venture partners to develop some specific marketplace solutions, co-brand the products/ services in a particular geographic district, or joint funds for mutual investment. Stuart (2010) said channel innovation was the firm chose many new types of sales channels, like direct sales, online store sales and supermarket sales etc. In OECD (2005), marketing innovation was the firm developed new marketing methods like product promotion or pricing. Vijay and Rakesh (2008) said mergers & acquisitions was the firm purchased other firms for the benefit of both parties and purchased firms' shares in the opening market. Sameer, Cindy and Michelle (2006) said inbound logistics innovation was the firm increased high technology for goods transformation and flow for internal efficiency from the raw materials stage to products stage, and outbound Logistics Innovation was the firm increased high technology for goods transformation and flow for external efficiency from the products stage to the end user. Hammer (2005) believed operations innovation was the firm established new performance standards that shifts the market according to customer needs. Stevenson (2011) said sales innovation was with the aim of gathering the wants of targeted consumers, the firm redefines some activities connected with getting purchasers to buy the product, which includes advertising, path collection and etc. Nijssen et al.(2006) said service innovation was the firm improved new customer interaction channels, delivery systems or technical concepts founded on some technological or methodical way. Denali (2010) said procurement innovation was the firm used some methods to acquire products/ services at the most probable price. Ambuj (2006) said technology innovation was the firm already tried methods to get advanced technology. Michael et al. (2009) believed corporate infrastructure innovation was the firm already used actions like common administration, preparation, accounting, finance, legal support, and governmental relationships for supporting the work of the whole value chain.

#### 4. Measures Used in the Paper

With the nineteen factors of strategic innovation were identified for this research from the literature review, A 5-point Likert scale (Trochim, 2006) questionnaire would be used in the measurement. The cosmetic managers could choose the agreement scale of their company used these nineteen types of strategic innovation. Table 2 lists the agreement scale of nineteen types of strategic innovation (strongly agree named 5, agree 4, neither 3, disagree 2, strongly disagree 1).

Table 2. Agreement scale of strategic innovation

Types of strategic innovation	1	2	3	4	5
Product innovation ---My company always made new products, or upgrade old products to meet consumer demands.					
Packaging Innovation ---My company already used new packaging and new designs of brands and entire product categories to show the inner spirit and the unique organizational culture of enterprise.					
Research &Development--- My company already set R&D center to revise product technology and range of products.					
Financial Innovation--- My company already developed corporate financial system in order to improve operational efficiency and reduce the costs and risk.					
Human resource innovation--- My company already developed some new programs for better retains employees and recruits.					
Material innovation--- My company made some material qualities improvement.					
Alliance &Network--- My company already had venture partners to develop some specific marketplace solutions, co-brand our products and services in a specific geographic region, or joint funds for mutual investment.					
Channel innovation---My company found new ways to deliver products and services that customers already used and loved like direct sales, online store sales and supermarket sales etc.					
Marketing innovation--- My company already developed new marketing methods like new ideas and ways of advertising, public relations, promotions, and pricing policy.					
Mergers &Acquisitions--- My company already purchased other firms for beneficial to both parties and purchased firms' shares in the open market against the wishes of the target's board.					
Inbound Logistics Innovation--- My company already increased high technology for the goods transformation and flow for internal efficiency from the raw materials stage to products stage.					
Outbound Logistics Innovation--- My company already increased high technology for goods transformation and flow for external efficiency from the products stage to the end user.					
Operations Innovation --- My company already established new performance standards that shift the market according to customer needs.					
Sales Innovation--- In order to meet the needs of targeted customers, my company already redefine new sales plan and sales method that could be better effective and appropriate to the market.					
Service Innovation--- My company already improved new customer interaction channels, distribution systems or technological concepts based on some technological or systematic method.					
Procurement Innovation--- My company already used some methods to acquire goods or services at the best possible total cost.					
Technology Innovation --- My company already tried methods to get advanced technology.					
Firm Infrastructure Innovation--- My company already used activities such as general management, planning, finance, accounting, legal support, and governmental relations to support the work of the entire value chain.					
Communication Innovation--- My company already send the business information more effectively by new ideas, technologies , products and services to conquer barriers, transmit ideas and information to consumers, employees and share holders.					

## 5. Methodology

In this paper, the scale scores of types of strategic innovation would be checked, and the three years average scale scores for 2005, 2006 and 2007 would be used in the analysis (Wang et al., 2009; Cho & Vladimir, 2005). The variables of this paper are the scale degrees of the types strategic innovation that cosmetic managers chosen.

Based on the China Association of Fragrance Flavour and Cosmetic Industries (2008), there are about 4000 cosmetics manufacturers in China in 2008. Prush and Sri (2006) have recommended, for the number of variables, the ratio of sample size could be a criterion: the suggested range was from 2:1 to 20:1. The questionnaire items were in a structured, close-ended format, which provided the respondents with specific response categories by applying the interval type of scaling method. The questionnaire was sent to senior managers of cosmetics firms who were contacted and had agreed to participate in the survey in China. Normally the companies' strategies would be planned for next five years development of the companies. Hence those managers who constantly have five years experience in the company are specialized managers and they understand strategic innovation of the company (School of business administration South China University of Technology, 2007). In this paper, the managers with experience less than five years in strategic management were not included in the survey. The respondents were requested to identify the major types of strategic innovation in order to classify the constitutions of strategic innovation in the cosmetics industry.

Pilot testing was conducted to check the appropriateness of the questionnaire, and the reliability and validity of the pilot testing were also checked (Table 3). The data for pilot test was collected from 30 respondents. The variables include 19 items of strategic innovation. The Cronbach alpha was .73. This showed that the pilot test was reliable because the scale reliabilities were above the commonly accepted threshold value of 0.70 (Hair et al., 2006).

Table 3. Reliability of pilot testing

Variables	Chronbach Alpha (Pilot test) n=30	Number of items
Strategic innovation	.73	19

This study used exploratory factor analysis to extract the constituents of strategic innovation, and use Structural Equation Modelling to simultaneously examine the relationships between the dependent variable and independent variables to determine the underlying structure of the data while controlling for measurement error.

## 6. Data Analysis

Terziovski (2010) in his study used a sample of 600 Australian SMEs and found that SMEs were similar to large firms with respect to strategic innovation. A total of 800 questionnaires were sent to senior managers. A total of 275 questionnaires were received by the cut-off date, and 8 questionnaires were discarded because, the respondents were unsuccessful in completing the questionnaire. Thus, the sample size was 267 with a response rate of 33 percent. From the questionnaires received, the result shows that 44.6 percent respondents' strategic innovation experience was less than 5 years (119 feedbacks). 55.4 percent respondents' have rich strategic innovation experiences (148 feedbacks). Therefore, the survey result is based on reliable respondents who have worked in this industry for more than 5 years, and therefore are assumed to have understood strategic innovation practices in their companies.

The reliability of the questionnaire was checked using the Cronbach alpha coefficient. As shown in Table 4: the Cronbach alpha for different parts of constructs were as follows: in the questionnaire sent to 267 respondents, about strategic innovation comprising of 19 items, the Cronbach alpha was .773. These values showed that the questionnaire was reliable because the scale reliabilities were above the commonly accepted threshold value of 0.70 (Hair et al., 2006).

Table 4. Reliability of data

Variables	Chronbach Alpha for final data (n=267)	Number of items
Strategic innovation	.773	19

Nineteen types of strategic innovation which had to be grouped into different constituents of strategic innovation.

To do this, exploratory factor analysis was used to extract the constituents from these types of strategic innovation. Factor analysis is a method applied to detect structure in the relationships between variables in order to classify the variables and reduce the number of variables (Huang, 2010). Ho (2006) believed that the crucial function of factor analysis is a lot of inter-correlated measures for a few properly typical factors or constructs. Hair et al. (2006) said factor analysis could be used to describe the fundamental variables' structure, and it could be used to outline and divide indicators into a suitable factors.

The results of the factor analysis for 19 types of strategic innovation in the cosmetics industry showed that the Kaiser's overall measure of sample size is .817, which supports the adequacy of the sample for factor analysis. The result also showed that the Bartlett's test of sphericity test was statistically significant (Sig = .000), and which points out that sufficient correlation is present, so that the data was suitable for factor analysis (Table 5).

Table 5. KMO and Bartlett's test of adequacy and suitability of sample size

KMO and Bartlett's Test		
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.817
Bartlett's Test of Sphericity	Approx. Chi-Square	2234.301
	df	171
	Sig.	.000

In this research, only factors with eigenvalues of one or greater were considered. The result shows that, based on the latent root criterion or eigenvalue greater than one, in factor analysis, four factors could be extracted as an optimum number of factors in the present study. The results showed that the four extracted factors accounted for 62.89 % of the total variance (Table 6).

Table 6. Varimax rotation factor pattern of types of strategic innovations

Strategic innovations	Factor 1	Factor 2	Factor 3	Factor 4
Alliance & Network	.854			
Marketing Innovation	.852			
Channel innovation	.815			
Sales Innovation	.813			
Mergers & Acquisitions	.793			
Material Innovation		.878		
Product Innovation		.868		
Research & Development		.840		
Technology Innovation		.813		
Packaging Innovation		.493		
Outbound Logistics Innovation			.838	
Operations Innovation			.823	
Inbound Logistics Innovation			.819	
Communication Innovation			.806	
Firm Infrastructure Innovation			.422	
Procurement Innovation				.839
Human resource Innovation				.814
Service Innovation				.794
Corporate Financial Innovation				.449
Eigenvalues	4.245	3.006	2.710	1.990
Percentage of variance	18.538	16.968	15.486	11.904

As a result, nineteen types of strategic innovations were extracted to four factors. Factor one had

cross-correlation with “New Market Innovation” that comprised of five types of strategic innovations and accounted for 18.54% of the total variance. Factor two named as “Product Value Addition” included 5 strategic innovation types and accounted for 16.968% of the total variance. Factor three is correlated with “Competitive Disruption” that consisted of 5 strategic innovation types and accounted for 15.48% of the total variance. Factor four had cross-correlation with “Service Value Addition” comprising of four types of strategic innovations and accounted for 11.90% of the total variance. As a result, all the nineteen types of strategic innovation had a factor loading of more than .40 in their underlying factor. In this research, these four factors from the factor analysis are the key constituents of strategic innovation, so the key constituents of strategic innovation are new market creation, product value addition, competitive disruption, and service value addition in this research. The key constituents of strategic innovation are shown in Table 7.

Table 7. Constituents of strategic innovation

Constituent of strategic innovation	Types of strategic innovation
New Market Creation	Alliance & Network
	Marketing Innovation
	Channel innovation
	Sales Innovation
	Mergers & Acquisitions
Product value addition	Material Innovation
	Product Innovation
	Research & Development
	Technology Innovation
	Packaging Innovation
Competitive Disruption	Outbound Logistics Innovation
	Operations Innovation
	Inbound Logistics Innovation
	Communication Innovation
	Firm Infrastructure Innovation
Service Value Addition	Procurement Innovation
	Human Resource Innovation
	Service Innovation
	Corporate Financial Innovation

New Market Creation consists by 5 types of strategic innovation, which are mergers and acquisitions, marketing innovation, channel innovation, alliance and network, as well as sales innovation. These five variables activate the variables for new market creation. All these strategic innovation activities help a firm to expand into new markets. The analysis confirmed that new market creation is an important constituent of strategic innovation for cosmetic firms in the Chinese market.

Product value addition includes material innovation, product innovation, research & development, technology innovation, and packaging innovation. The new modern cosmetic product manufacturers were more involved in the flow of R&D, technology and material innovation. Product innovation has been spurred by increases in the demand for high technological products, and becomes vital for cosmetics firms. Customers are always interested in high quality products made up of new materials, as high quality products attract more customers who are willing to pay for it.

Competitive Disruption consists of outbound logistic innovation, operations innovation, communication innovation, inbound logistic innovation and firm infrastructure innovation. An industry develops a dominant process and infrastructure that becomes the established industry recipe. A strategic innovator takes a position outside of existing outbound logistics and inbound logistics by creative new operations and even new

communication with customers and employees. Competitive disruption measures the extent to which strategic innovators deviate from the existing structure in their industry and adopt entirely new methods on the rules of the game.

Service value addition includes procurement innovation, human resource innovation, service innovation, and corporate financial innovation. Service is important to transfer cosmetic product value to customers. Cosmetic products are not a necessity in life, so good service and patient staff could attract customers to the cosmetics shop again. And financial innovation could bring more value for firms and their customers. Moreover good service comes from human resource support and financial support.

According to the result of factor analysis, the concept of strategic innovation for the cosmetics industry in the Chinese market could be defined as: Strategic innovation is anything that tends to create new market, by enhancing product or service value in order to disrupt competition.

## 7. Conclusion

This study analyzed 267 samples about their preferences to types of strategic innovation with the purpose of finding out the constituents of strategic innovation. An exploratory factor analysis was used to analyze strategic innovation. The multidimensional data sets were reduced to lower dimensions. A total of nineteen types of strategic innovations were identified. From the nineteen types of strategic innovations, four constituents were extracted and named as new market creation, product value addition, competitive disruption and service value addition. With these results, an attempt is made the definition of strategic innovation. Strategic innovation is anything that tends to create new markets, by enhancing product or service value in order to disrupt competition. This result proved the idea of Cooper (1990)---strategic innovation was an all-inclusive term, Furthermore, this paper analysed the constituents of strategic innovation--even the former researchers found many types of strategic innovation, they did not reduce constituents of strategic innovation with exploratory factor analysis. Only described some types of strategic innovation, the former definitions of strategic innovation were not applicable and comprehensive. After the constituents of strategic innovation were extracted from types of strategic innovation, strategic innovation could be generally defined by those constituents. This research also contribute to strategic innovation research in special industry. Before it, there was no papers researched strategic innovation in cosmetic industry. This paper was complementary to the former researches.

In this paper, China is the exclusive place of focus. Comparative studies may give different insights into strategic innovation, exploring various dimensions. Future studies could be extended to cosmetics industry in other countries for comparative analyses. Only nineteen types of strategic innovations were analyzed in the study. There may be other variables that have not been addressed and hence in future studies, more types of strategic innovation could be analysed and discovered.

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