


Chapter 7

Creating value for customers

Chapter objectives

By the end of this chapter, you will understand:

1. the meaning of the term 'value'
2. how customers weigh up 'benefits' and 'sacrifices' in the value equation
3. three major forms of value delivery strategy adopted by successful companies
4. what is meant by the term 'value proposition'
5. how marketers create customer value by mixing together a number of variables known as the 7Ps.
6. the importance of customization in creating value
7. how the Internet is changing the way that customers receive value from communication and distribution.

Introduction

In this chapter you will learn about how companies create and deliver value to customers. You'll find out what customers mean when they talk about value, and the various elements that make up a company's value proposition.

Our definition of CRM, repeated below, stresses the centrality of value creation and delivery:

CRM is the core business strategy that integrates internal processes and functions and external networks **to create and deliver value to targeted customers at a profit**. It is grounded on high-quality customer-related data and enabled by information technology.

Of the various forms of CRM that we have discussed, the task of directing the creation and delivery of value to targeted customers at a profit falls to strategic CRM.

Understanding value

Although the term 'value' is used in a number of different ways,¹ in a CRM sense it can be thought of as follows:

Value is the customer's perception of the balance between benefits received from a product or service and the sacrifices made to experience those benefits.

It is possible to represent this definition in the form of an equation:

$$\text{Value} = \frac{\text{Benefits}}{\text{Sacrifices}}$$

The equation shows that you can increase the customer's perceived value in two main ways: increase the benefits they experience, or decrease the sacrifices they make.

Let's look at sacrifices. Customers make several types of sacrifice.

- **Money:** the price of the product or service, which may or may not be the listed price. There may be additional costs such as credit card surcharges, interest charges on extended payments or warranty costs. There may be discounts applied for relationship customers, early payment or volume purchases.
- **Search costs:** the purchasing process may include exhaustive pre-purchase work in searching for solutions and comparing alternatives. This can take considerable time. In a B2B context, a purchaser's time may have a real monetary cost. When purchasing involves several people these costs may be very high indeed. This is one of the reasons that customers are motivated to remain with existing suppliers and solutions. There may also be travel and accommodation costs as buyers visit reference customers to see solutions onsite. Transaction costs are normally lower when search costs are eliminated and purchasing processes are routinized. Some suppliers are prepared to take on the costs of managing inventory for important customers, so that they are less tempted to search for alternative solutions. Known as vendor managed inventory (VMI), it reduces search and reorder costs for customers.
- **Psychic costs:** purchasing can be a very stressful and frustrating experience. For some customers, holiday shopping at Christmas and other festivals means struggling to come up with gift ideas for relatives they rarely see, travelling on crowded public transport, pushing through throngs of shoppers, dealing with temporary sales staff who don't have enough product knowledge, paying inflated prices, carrying home arms full of heavy packages, and doing all these in bad weather! Psychic costs can be so great for some customers that they postpone purchases until a better time. Others cancel purchasing completely.

Perceived risk is also a consideration in assessing psychic cost. Perceived risk takes a variety of forms: performance, physical, financial, social and psychological. Performance risk occurs when the customer is not fully sure that the product will do what is required. Physical risk is when the customer feels that there may be some bodily harm done by the product. Financial risk is felt when there is danger of economic loss from the purchase. Social risk is felt when customers feel that their social standing or reputation is at risk. Psychological risk is felt when the customer's self-esteem or self-image is endangered by an act of purchase or consumption. When perceived risk is high, psychic cost is correspondingly high.

Customers often feel uncomfortable at higher levels of perceived risk and may try to reduce risk in a number of ways, as indicated in Figure 7.1. When customers try to reduce perceived risk, they are in effect trying to reduce the denominator of the value equation, thereby improving value. Suppliers can help customers reduce their levels of perceived risk in a number of ways. For example, performance risk is

reduced by performance guarantees; financial risk is reduced by firm prices and interest-free payment plans.

- Delay purchase
- Seek word-of-mouth endorsement
- Negotiate service contracts
- Seek additional information from advertising copy
- Buy known brands
- Deal with reputable suppliers
- Seek performance guarantees
- Buy with credit card (protection if product fails)
- Negotiate discounts
- Take out insurance
- Demand pre-purchase trial

Figure 7.1
How do customers reduce perceived risk?

Clearly there is more to the sacrifice component of the value equation than money alone. This explains why customers buy what appear to be suboptimal solutions to their problems. Why would a customer buy a printer for \$300 when an identically specified machine is available for \$100? Perhaps the answer lies in search and psychic costs. There is more to the benefit component than quality alone, although Bradley Gale has developed a value-based customer choice model that uses customer-perceived quality as the numerator and monetary price as the denominator. This assumes that customers will prefer the offer that delivers the best value ratio of quality against price.²

Total cost of ownership

There is a trend towards considering costs from the perspective of 'total cost of ownership' or TCO. TCO looks not only at the costs of acquiring products, but also at the full costs of using, and servicing the product throughout its life, and ultimately disposing of the product. What is thought of as 'consumption' can be broken down into a number of activities or stages, including search, purchase, ownership, use, consumption and disposal. TCO is an attempt to come up with meaningful estimates of lifetime costs across all these stages.

When customers take a TCO view of purchasing, suppliers can respond through a form of pricing called economic value to the customer (EVC). In a B2B context, EVC works by proving to customers that the value proposition being presented improves the profitability of the customer, by increasing sales, reducing costs or otherwise improving productivity. EVC computes for customers the value that the solution will deliver over the lifetime of ownership and use. Suppliers can apply EVC thinking to each stage of the 'consumption' process described above. For example,

a computer supplier may agree to provide free service and to collect and dispose of unwanted machines after four years. Customers performing these tasks themselves would incur tangible costs. This is therefore the value that these activities have for customers.

EVC encourages suppliers to customize price for customers on the basis of their particular value requirements.

Customer value researchers have developed several typologies of customer-perceived value. Jag Sheth and colleagues have identified five types of value: functional, social, emotional, epistemic and conditional value.³ In a B2B context, a distinction is made between economic value (satisfying economic needs at low transaction costs) and social value (satisfaction with the relationship with the supplier).⁴

How companies compete to create value for customers

Companies compete in a number of different ways, as indicated in Figure 7.2.⁵ In a well-regulated economy, most companies compete by trying to deliver consistently better value than competitors. This means understanding customers' requirements fully and creating and delivering better solutions than competitors.

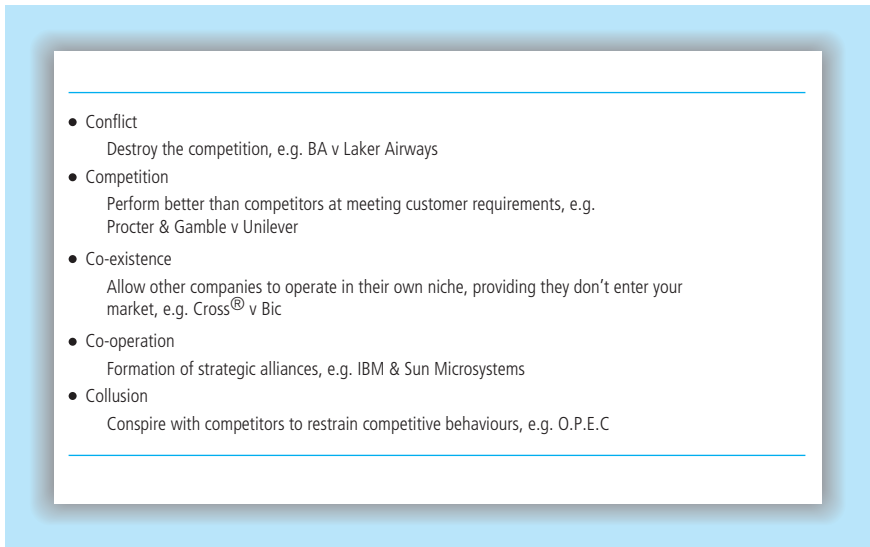
- 
- Conflict
Destroy the competition, e.g. BA v Laker Airways
 - Competition
Perform better than competitors at meeting customer requirements, e.g. Procter & Gamble v Unilever
 - Co-existence
Allow other companies to operate in their own niche, providing they don't enter your market, e.g. Cross® v Bic
 - Co-operation
Formation of strategic alliances, e.g. IBM & Sun Microsystems
 - Collusion
Conspire with competitors to restrain competitive behaviours, e.g. O.P.E.C

Figure 7.2
How companies compete
Source: Easton et al. (1993).

Value is contextualized rather than absolute. A solution that works in one context has value; that same solution, not working in another context, has no value. In a B2C context, McDonald's may have great value as a solution to the question, 'where shall I hold my 8-year-old daughter's birthday party?' It has less value as a solution to the question, 'where shall I take my fiancée for her 27th birthday?'

To create better value for customers, companies have to reinvent the numerator (benefits) and/or denominator (sacrifices) of the value

equation. In a B2B context, this is often done in partnership with customers on a customer-by-customer basis. Unique solutions may be required. In B2C contexts, solutions are more often segment or niche specific, and are supported by market intelligence. To win and keep customers, companies have to constantly seek to improve the value they create. Given that this happens in a competitive environment, it is necessary not only to keep current with customer requirements, but also to stay up to date with competitors' efforts to serve these customers.

Sources of customer value

It is the job of professional marketers to develop the offers that create value for customers: the so-called value proposition. We can define value proposition as follows:

A value proposition is the explicit or implicit promise made by a company to its customers that it will deliver a particular bundle of value-creating benefits.

Michael Treacey and Fred Wiersema have identified three fundamental types of value proposition that are delivered by successful companies. Indeed, these authors say that companies cannot be all things to all customers and need to concentrate on one of these three value delivery strategies. The strategies are characterized by product leadership, customer intimacy and operational excellence, and are summarized in Table 7.1.⁶

	Value delivery strategies		
	Operational excellence	Product leadership	Customer intimacy
Company traits			
Core business processes that ...	Sharpen distribution systems and provide no-hassle service	Nurture ideas, translate them into products and market them skilfully	Provide solutions and help customers run their businesses
Structure that ...	Has strong, central authority and a finite level of empowerment	Acts in an ad hoc, organic, loosely knit and ever-changing way	Pushes empowerment close to customer contact
Management systems that ...	Maintain standard operating procedures	Reward individuals' innovative capacity and new product success	Measure the cost of providing service and of maintaining customer loyalty
Culture that ...	Acts predictably and believes 'one size fits all'	Experiments and thinks 'outside of the box'	Is flexible and thinks 'have it your way'

Table 7.1 Three value disciplines

- **Operational excellence:** companies that pursue this strategy do a limited number of things very efficiently, at very low cost, and pass on those savings to customers. Companies renowned for this are Wal-Mart, Giordano and McDonald's. Unexpectedly, Toyota might also fit this strategy. If customers take a total cost of ownership view of price, then Toyota, with its reputation for reliability, durability and competitive service costs, fits the operational excellence model well. Operational excellence is underpinned by lean manufacturing and efficient supply chains, close cooperation with suppliers, rigorous quality and cost controls, process measurement and improvement, and management of customer expectations.
- **Product leadership:** companies aligning with this value discipline aim to provide the best products, services or solutions to customers. Continuous innovation underpins this strategy. Companies renowned for this are 3M, Intel, GSK, LG and Singapore Airlines. Product leadership is reflected in a culture that encourages innovation, a risk-oriented management style, and investment in research and development.
- **Customer intimacy:** companies that pursue this strategy are able to adapt their offers to meet the needs of individual customers. Customer intimacy is based on customer insight. Companies renowned for customer intimacy include Saatchi and Saatchi, McKinsey and the US department store, Nordstrom. Adaptation and customization based on deep understanding of customer requirements underpin this strategy.

Value through the marketing mix

As mentioned above, it is the responsibility of marketing people to develop value propositions. They use a toolkit known as the marketing mix. The term 'marketing mix' is really a metaphor to describe the process of combining together various components to create value for customers. Eugene McCarthy grouped these components into a classification known as the 4Ps: product, price, promotion and place.⁷ This approach is widely applied by goods manufacturers.

Services marketing experts in both B2B and B2C contexts have found this 4P taxonomy inadequate because it fails to take account of the special attributes of services (these were described in the last chapter). To recap, services are performances or acts that are, for the most part, intangible-dominant, inseparable (produced at the same time and place they are consumed), heterogeneous (of variable quality) and perishable.

Service marketers' response to these special characteristics has been to develop a new toolkit for creating customer value. It contains another 3Ps, making 7Ps in total.⁸ The additional 3Ps are people, physical evidence and process, as shown in Figure 7.3. As we shall see later, though developed for services contexts, they can provide a useful framework for goods manufacturers too. Before we explore each of these sources of customer value, we'll look at the issue of customization.

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- | | |
|--|--|
| <ul style="list-style-type: none"> ● Good marketing mix – Product – Price – Promotion – Place | <ul style="list-style-type: none"> ● Service marketing mix – Product – Price – Promotion – Place – <i>Process</i> – <i>Participants</i> – <i>Physical evidence</i> |
|--|--|

Figure 7.3
Sources of customer value

Customization

CRM aims to build mutually beneficial relationships with customers at segment, cohort or individual level. A fundamental approach to achieving this goal is to customize the value proposition in order to attract and retain targeted customers. CRM aims to fit the offer to the requirements of the customer; it is not a one-size-fits-all approach.

Customization has both cost and revenue implications. It may make strategic sense because it generates competitive advantage and is appealing to customers, but there may be serious reservations because of the costs of customization. Companies need to ask whether investment in customization will generate a return higher than they could achieve through other strategies carrying a similar amount of risk. Customization may mean the loss of economies of scale, thus increasing unit costs. There may also be additional technology costs.

Case 7.1

Dell Computer customizes production using a product configurator

When Dell Computer's customers are online, they are able to design their own computers. Customers interface with the front end of a technology called a configurator. This is a rule-based system that enables or disables certain combinations of product features including chassis, hard disk capacity, memory, processor speed, software and connectivity. The technology is connected to back-office functions such as assembly and procurement. Each Dell Computer is made to order.

Customization means that companies have to be aware of, and responsive to, customers' differing requirements. Information systems designed to capture, store and distribute customer-related data also have a cost.

Configurator technologies can be quite sophisticated. In their simplest form they contain a set of rules (if the customer chooses chassis A, only allow one hard disk). At the other end of the spectrum are constraint-based optimization technologies. The constraints are applied in a systematic way to ensure the final configuration is optimum, for example, in producing least cost products.

Customization has been the norm in B2B markets for many years. Suppliers routinely make adaptations to suit the needs of customers. It is also true that customers make adaptations to suit suppliers. These adaptations serve as investments that make the relationship hard to break. As shown in Figure 7.4, suppliers can adapt, or customize, any of the 7Ps regardless of whether they manufacture goods or perform services. Although the additional 3Ps were developed for service companies, they also apply in the manufacturing context, as these examples show.

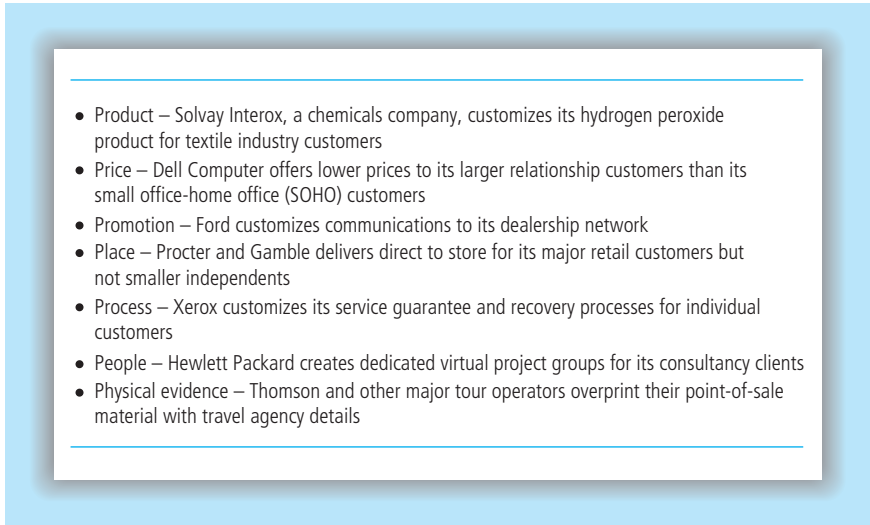
- 
- Product – Solvay Interox, a chemicals company, customizes its hydrogen peroxide product for textile industry customers
 - Price – Dell Computer offers lower prices to its larger relationship customers than its small office-home office (SOHO) customers
 - Promotion – Ford customizes communications to its dealership network
 - Place – Procter and Gamble delivers direct to store for its major retail customers but not smaller independents
 - Process – Xerox customizes its service guarantee and recovery processes for individual customers
 - People – Hewlett Packard creates dedicated virtual project groups for its consultancy clients
 - Physical evidence – Thomson and other major tour operators overprint their point-of-sale material with travel agency details

Figure 7.4
Customizing the 7Ps

- **Process:** important manufacturing industry processes are the order fulfilment process and the new product development process. Manufacturers can customize these to suit the requirements of different customers. Major FMCG manufacturers have evolved twin new product development processes. They have their own in-house processes, as well as customized processes in which they co-develop new products in partnership with major retailers.
- **People:** manufacturers can adjust the profile and membership of account teams to ensure that customers get the service they deserve and can afford. Kraft, for example, has customer teams for major retail accounts that consist of a customer business manager (c.f. key account manager), category planner, retail sales manager, sales information specialist, retail space management and supply chain specialist. This customer-facing team can then draw on additional company expertise if needed, including brand managers and logistics specialists. The

composition and membership of the team is agreed with each major retail account.

- **Physical evidence:** manufacturers use many different forms of physical evidence, such as scale models, cut-away models, product samples and collateral materials. Kitchen manufacturers provide customized swatches of worktop and cabinet colours to their major retail distributors.

Case 7.3

Tailored value propositions at Heineken Ireland

Heineken, a major beer exporter, has been very successful in the Irish beer market, with brands collectively capturing around 17 per cent of the total market. This success has been attributed to a deep understanding of the market, a strong portfolio of brands and a commitment to customer satisfaction. To sustain its position, Heineken sought to focus on delivering superior service to its 9000 commercial customers, namely pubs, hotels and wholesalers. To accomplish this Heineken implemented a Siebel CRM system.

For Heineken, one advantage of the Siebel software has been its ability to create single, comprehensive, profiles of customers which can be used to tailor product bundles and services, and to provide improved levels of customer service. Heineken believes that the CRM system provides the ability to build higher quality relationships with customers. For example, sales representatives are able to prioritize their interactions with key customers and instantly analyse historical data to identify sales trends and buying patterns of both individual customers and geographic areas, using their notebook computers while on the road.

Mass customization

A distinction can be made between 'craft customization' and 'mass customization'. The latter implies that an organization can communicate with target audiences at a mass or segment level, but is also able to offer customized value propositions for individual customers. Craft customization involves customized offers, but not at a mass market level.


Mass customization can be defined as follows:

Mass customization is the use of flexible processes and organizational structures to create varied, and even individually tailored, value propositions, with neither a cost nor a lead time penalty.

This is not the same as offering customers more choice, customers certainly want their needs to be met; they do not necessarily want choice. Giving customers' choice has been the default strategy when companies have been unable to identify and meet customers' precise requirements. Choice means work for the customer in comparing offers; work adds to the cost of the consumption process.

A number of different types of mass customization have been identified, as shown in Table 7.2.⁹ A relatively minor form of mass customization involves 'match to order'. This simply involves finding

a match, from a range of standard products, to a particular customer’s requirements. At the other extreme is ‘engineer to order’, which involves the co-design, in a joint enterprise between customer and supplier, of a unique solution to that customer’s problem.



	Type of mass customization	How it works	Example
Minor	Match-to-order or locate-to-order	Selection of existing standard products or services to match customer requirements	Cars
	Bundle-to-order	Bundling of existing products and services to suit customer requirements	Conferences
	Assemble-to-order	Assembly of products or services from existing standardized components or processes	Computers
	Make-to-order	Manufacture of customized products including components	Tailored suits
Major	Engineer-to-order	Customer co-designs products or services which are then made-to-order	Aircraft

Table 7.2 Different forms of mass customization

It is in B2C markets that mass customization has lately become more widespread. Until recently, most B2C companies have either mass marketed standardized products or have developed product variants for particular niches. A growing number are now attempting to mass customize their offers. This is enabled by databases that store customer preferences, Internet-enabled interactivity that permits companies to learn about changing customer requirements through improved communication, modular product design, flexible manufacturing operations and supply chains, and mass customization technologies.

Mass customization is widespread in service industries serving end consumers. This is largely because of the inseparability of service production and consumption. The interaction between consumers and service producers during the service encounter lets customers influence both the service delivery process and the outcome.

Mass customization is also becoming more common in manufacturing companies. Dell Computer’s mass customization model allows customers to design up to 14 000 different personal computer configurations. Ford was able to produce 27 million different Ford Fiestas, more than were actually sold.

Key issues for CRM strategists are these:

1. Do customers want customized products and services?
2. What degree of customization is desired?
3. Are customers willing to pay a premium for customization?

Frank Piller and Melanie Müller have reviewed the research on these questions, paying particular attention to the shoe manufacturing industry.¹⁰ They found that consumers generally are aware of and value the benefits of mass customization (for shoe customers, better fit is the single most important benefit, followed at some distance by style and functionality), and the majority are willing to pay a premium – particularly women. Willingness to pay more varies across brands and customer segments. Adidas, for example, is able to command a 50 per cent price premium for customized sports shoes. Customization, however, does not universally mean that customers pay more. Some customized products eliminate features that have no value for customers, resulting in lower costs which are passed on in reduced prices.

Not all customer segments are willing to pay for mass customization. Levi Strauss has three different routes to market: jeans specialists, department stores and their own Original Levi Stores. Each channel reaches different market segments, and the company offers different product lines in each type of store. The Original Levi Store is the only channel where the company has offered mass customization. Customer measurements taken in-store are fed into the production system. A week or so later the customer receives a pair of customized Levi jeans. For Levi's, this differentiation allowed them to maintain a price premium in this one channel that has been impossible to achieve in their other channels. For customers there was the added value that the jeans fitted perfectly.

Amazon.com has become the world's largest and most successful online retailer, diversifying from books and CDs into other areas such as electronics and clothing. Much of Amazon's continued success has been related to its CRM strategy of retaining customers and growing share of wallet. Amazon utilizes CRM software to customize offerings to each customer. Based on information, such as previous purchases and products that have recently been browsed, Amazon's CRM software can predict a range of other products the customer is likely to be interested in. For example, a customer who purchases an Ernest Hemingway novel may receive a recommendation to purchase another novel by the author or a DVD documentary of Hemingway's life. Your author's customized Amazon.com webpage is presented in Figure 7.5.

Over the next few paragraphs we'll look at how value can be created by astute management of the marketing mix variables.

Value from products

Companies may make products, but customers do not buy products. Customers buy solutions to their problems. They buy benefits or, better said, they buy the expectation of benefits. Nobody ever buys a lawnmower because they want a lawnmower; people want attractive lawns. Products are means to ends.

Products that offer better solutions to problems create more value for customers. A better solution is one in which the balance between benefits and sacrifices of the value equation is enhanced for the customer.



Figure 7.5 Francis Buttle’s Amazon.com customized webpage

Marketers often distinguish between different levels of the product, sometimes known as a customer value hierarchy.¹¹ The **core** product is the basic benefit that customers buy. Companies competing for customer demand must be able to meet the core benefit requirements. Let’s consider the market for MBA-level education. MBA students typically are buying one or more of three basic benefits: salary enhancement, career development or personal growth. A second level is the **enabling** product. This consists of the physical goods and services that are necessary for the core benefit to be delivered. In the MBA case, this would comprise the buildings, classroom fixtures, faculty and educational technology. A third level, the **augmented** product consists of the factors that position and differentiate one competitor from another. In the MBA illustration this might be teaching method, for example, learning through real life projects, or an extensive international exchange programme, or a leafy out of town location.

Companies offering the same core benefit have to compete to deliver value to customers through enablers and augmentations. As Ted Levitt noted:

... competition is not between what companies produce in their factories, but between what they add to their factory output in the form of packaging, services, advertising, customer advice, financing, delivery arrangements, warehousing and other things that people value.¹²

Product-based value is created for customers through product innovation, additional benefits, product-service bundling, branding and product synergies. We explore these below.

Product innovation

Most 'new' products are modifications of existing products, cost reductions or line extensions. Very few products are 'new to the world' or create new product categories. New products in all of these categories can improve customer value perceptions, but it is the dramatic ground-breaking inventions that create leaps in customer value. History is littered with them: Stephenson's locomotive, Edison's incandescent light bulb, Hargreaves's spinning jenny and Newcomen's steam engine. More recently we have had the Sony Walkman and Apple iPod.

Occasionally, old technologies provide value-creating modern day solutions. Trevor Bayliss invented the wind-up radio after seeing a programme about the spread of AIDS in Africa. The programme highlighted the difficulty that health professionals faced getting safe sex messages to rural and poor areas where there were no power sources for conventional radios. Thirtyfive per cent of the world has no access to electricity. Large-scale manufacturing of the Freeplay® wind-up radio began in 1995. The radio has two energy sources: dynamo power and solar cells. The product has created value for all concerned: the manufacturers, investors, resellers, employees, Bayliss and, of course, radio audiences. It has sold over two million units, and the technology has also been applied to lanterns and mobile phone chargers.

Additional benefits

Companies can create value for customers by attaching additional benefits to their products. A lawnmower operates more quietly. A car comes with a five-year warranty. A forklift truck is supplied with a free options package. Sometimes additional benefits are accompanied by repositioning the product in a different segment of the market. Lucozade had been a glucose drink for older people and was widely associated with illness. The brand owner, GlaxoSmithKline, repositioned this product as an energy drink in the rapidly growing sports drink market, where it has enjoyed considerable success (see Figure 7.6).

Low involvement product categories have low personal significance or relevance to customers. Customers feel very little sense of commitment to any brand and are therefore easily switched to competitors. Adding additional benefits helps brand owners to increase the level of customer involvement. There are two main approaches: product modification and product association. Product modification means changing the product in some way so that it ties in more closely to the customer's needs, values and interests. Detergent manufacturers, for example, have reformulated their brands so that they are more environmentally friendly. Diaper manufacturers have resegmented the market so that there are different products for boys and girls, day and night, babies of different weights and even 'swimmer' models. Product association means linking the brand to some issue or context that is of high importance to customers. PlayStation, for example, links a soccer computer game to the FIFA World Cup, while Mobil tied its brand to the Olympics, donating to sports funds for every gallon or litre purchased.



Figure 7.6
Repositioning
Lucozade as a sports
drink

Product–service bundling

Product–service bundling is the practice of offering customers a package of goods and services at a single price. Tour operators routinely bundle several elements of a vacation together: flights, transfers, accommodation and meal plans, for example. For the customer, bundling can reduce money, search and psychic costs. For the company, there are economies in selling and marketing.

Changing the composition of a bundle can increase customer perceived value; adding or removing elements from the bundle can both have this effect. Adding elements to the bundle increases the benefits side of the value equation. In a B2C context, for example, supermarket operators can offer a bagging service at the checkout at no extra cost to the customer. If the people performing this task are diverted from other tasks, then there may be no additional costs for the operator. Removing elements from the bundle enables the company to establish a new price point, therefore adjusting the value equation for customers. In a B2B context, companies often ask for elements to be removed from a bundle in return for a lower price. For example, a training college with its own IT department may ask the supplier of its IT equipment for a lower price in return for not using the supplier’s help desk and IT support facilities. If the price is reduced by \$5000 and the saving to the supplier is \$6000, then both parties win.

Branding

A brand can be defined as follows:

A brand is any name, design, style, word or symbol that distinguishes a product from its competitors.

Brands create value for customers in a number of ways, on both sides of the value equation. Brands reduce search costs by clearly identifying one product as different from others. Brands can also reduce psychic costs. Over time, customers assign meanings to brands. If you buy a Mercedes vehicle, it may be because you understand that the brand attributes are excellence in engineering, assured quality build and high resale value. A customer who understands what the brand means is less at risk than a customer who does not understand. Brand knowledge like this is acquired from experience, word-of-mouth or marketer-controlled communication. Brands also offer an implicit assurance of a particular customer experience. For example, when you buy any products carrying the Virgin brand it may be because you believe that Virgin's brand values are service excellence, innovation and good value.

Product synergies

Companies can create value for customers by finding synergies between products in the company's product portfolio. For example, if you take a Virgin flight you will be offered a Virgin cola. If you buy Microsoft software, the company will offer you complementary software for related applications. These synergies are also sometimes created from relationships within a company's network.

Disney is particularly good at exploiting synergies. Disney characters, such as Snow White and the Little Mermaid, are created in Disney's film division. The characters then appear in theme parks around the world, in the USA, Paris, Tokyo and Hong Kong, and in other service environments such as cruises, retail stores and on the Disney TV network. Finally, the characters are licensed for use in other applications. For example, you'll find Disney characters on lunch boxes and school bags, on clothing and shoes, and on McDonald's packaging for special movie-linked promotions.

Value from service

A service, as noted earlier, is a performance or act performed for a customer. Service is an important part of many companies' value propositions. In most developed economies, about 70 per cent of gross domestic product is created by service organizations. For these organizations, service is the core product. Even in manufacturing firms, service is often an important part of the enabling and augmented product. For example, carpet manufacturers make floor coverings to international standards. While there is some potential to compete through product innovation, many manufacturers believe the best way to compete is through offering better service to their distributors, and corporate and domestic customers. Typical services include stockholding, design, measurement, cutting to order, delivery and fitting. Companies need to understand that their efforts to improve service should be focused. Companies should find out what service elements are important to customers and where performance needs to be improved. If the customer's biggest problem is your failure to deliver on time, in full

and with no errors, it makes little sense to invest in updating the livery of your vehicles and drivers.

In this section we look at a number of service-related methods for creating value: improving service quality, service guarantees, service level agreements and service recovery programmes.

Service quality

There are two major perspectives on service quality:

1. **Quality is conformance to specification:** this is consistent with Philip Crosby's view of quality.¹³ Conformance to specification might mean:
 - producing error-free invoices
 - delivering on time, in full as promised to customers
 - acknowledging a customer complaint within 24 hours.
2. **Quality is fitness for purpose:** Joseph M. Juran advanced the point of view that quality means creating products that are well suited to customer requirements, and which therefore meet their expectations. It is the customer, not the company, who decides whether quality is right.¹⁴ If you are a farmer, a Land Rover is the right quality vehicle. If you are an executive limousine company, a Mercedes is the right quality vehicle. In a services environment, fitness for purpose might mean
 - allowing the customer to select a preferred communication channel (phone, e-mail or postal service)
 - recruiting customer contact staff who are highly empathic and responsive
 - customizing service delivery for customers.

These perspectives on quality can happily coexist. Specifications for service performance can be based on customer expectations. If customers determine the standards, there need be no conflict between these two approaches.

Service quality theories

Two service quality theories have dominated management practice as companies try to improve their service performance: the SERVQUAL model and the Nordic model.

The Nordic model, originated by Christian Grönroos and developed by others, identifies three components of service quality:

- technical
- functional
- reputational (Table 7.3).¹⁵

Technical	The quality of the outcome of a service performance
Functional	The quality of the performance of a service
Reputational	The quality of the service organization's image

Table 7.3 Grönroos model of service quality¹⁶

Technical quality can be thought of as the ‘what’ of service quality. Was the floor vacuumed thoroughly and surfaces dusted meticulously by the office cleaning contractor? Was the stock check performed professionally by the specialist audit firm? Functional quality can be thought of as the ‘how’ of service quality. Was the cleaner courteous? Was the stock-check team responsive? Reputational quality is both a product of technical and functional quality, in that reputation derives from performance, and it also produces a halo effect which can influence customer perceptions of quality, for better or worse. If I’m attending an opera at Teatro alla Scala (La Scala) in Milano then it must be good. If I’m receiving service from a state monopoly then it must be bad.

The significance of this model is that it stresses the importance of understanding customer expectations and of developing a service delivery system that performs well at meeting customers’ technical and functional service quality expectations.

The SERVQUAL model, developed by A. ‘Parsu’ Parasuraman and colleagues in North America, identifies five core components of service quality: reliability, assurance, tangibles, empathy and responsiveness, as defined in Table 7.4.¹⁷ You can remember them through the mnemonic RATER.

Reliability	Ability to perform the promised service dependably and accurately
Assurance	Knowledge and courtesy of employees and their ability to convey trust and confidence
Tangibles	Appearance of physical facilities, equipment, personnel and communication materials
Empathy	Provision of caring, individualized attention to customers
Responsiveness	Willingness to help customers and to provide prompt service

Table 7.4 SERVQUAL components¹⁸

The SERVQUAL authors have also developed a measurement and management model to accompany the conceptual model. The measurement model uses a 44-item questionnaire that measures customers’ expectations and perceptions of the RATER variables.¹⁹ The relative importance of these variables is also measured. This enables you to compute the relative importance of any gaps between expectation and perceptions. Management can then focus on strategies and tactics to close the important gaps.

The management model, reproduced in Figure 7.7, identifies the reasons for any gaps between customer expectations and perceptions (gap 5). Gap 5 is the product of gaps 1, 2, 3 and 4. If these four gaps, all of which are located below the line that separates the customer from the company, are closed then gap 5 will close. The gaps are as follows:

- Gap 1 is the gap between what the customer expects and what the company’s management thinks customers expect.

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- Gap 2 occurs when management fails to design service standards that meet customer expectations.
- Gap 3 occurs when the company's service delivery systems – people, processes and technologies – fail to deliver to the specified standard.
- Gap 4 occurs when the company's communications with customers promise a level of service performance that the service delivery system cannot provide.

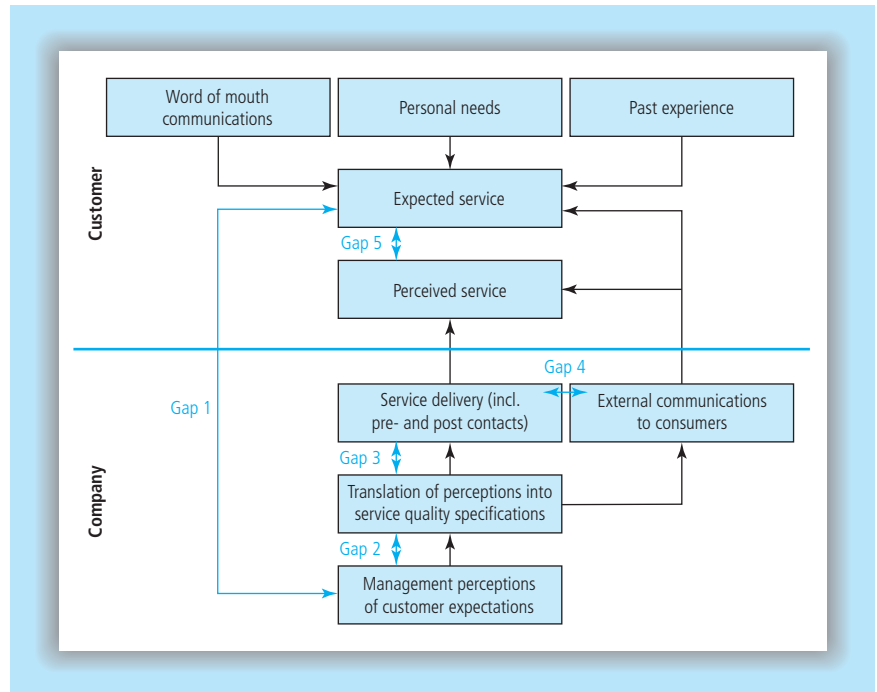


Figure 7.7
The SERVQUAL gaps model

The importance of SERVQUAL is that it offers managers a systematic approach to measuring and managing service quality. It emphasizes the importance of understanding customer expectations (see Figure 7.8), and of developing internal procedures that align company processes to customer expectations. Among the strategies and tactics that might be employed to close gaps 1–4 are the following:

1. To close gap 1 (between what customers expect and what managers think customers expect):
 - conduct primary research into customers' service quality expectations
 - learn from front-line customer contact staff
 - flatten the hierarchical structure
 - include expectations data in customer records.
2. To close gap 2 (between what managers think customers expect and service quality specifications):
 - commit to the development of service standards wherever possible
 - assess the feasibility of meeting customer expectations
 - develop a standards documentation process
 - automate processes where possible and desirable

- outsource activities where you lack the competencies
 - develop service quality goals.
3. To close gap 3 (between service quality specifications and actual service delivery):
- invest in people: recruitment, training and retention
 - invest in technology
 - redesign workflow
 - encourage self-organized teams
 - improve internal communication
 - write clear job specifications
 - reward service excellence.
4. To close gap 4 (between actual service delivery and the promises communicated to customers):
- brief advertising agency on customer service expectations
 - train employees not to overpromise
 - penalize employees who overpromise
 - encourage customers to sample the service experience
 - excel at service recovery
 - encourage and manage customer complaints.

There is growing evidence that investment in service quality improvements pays off in enhanced customer satisfaction and customer retention, although like other investments there does appear to be a point at which diminishing returns set in.²⁰

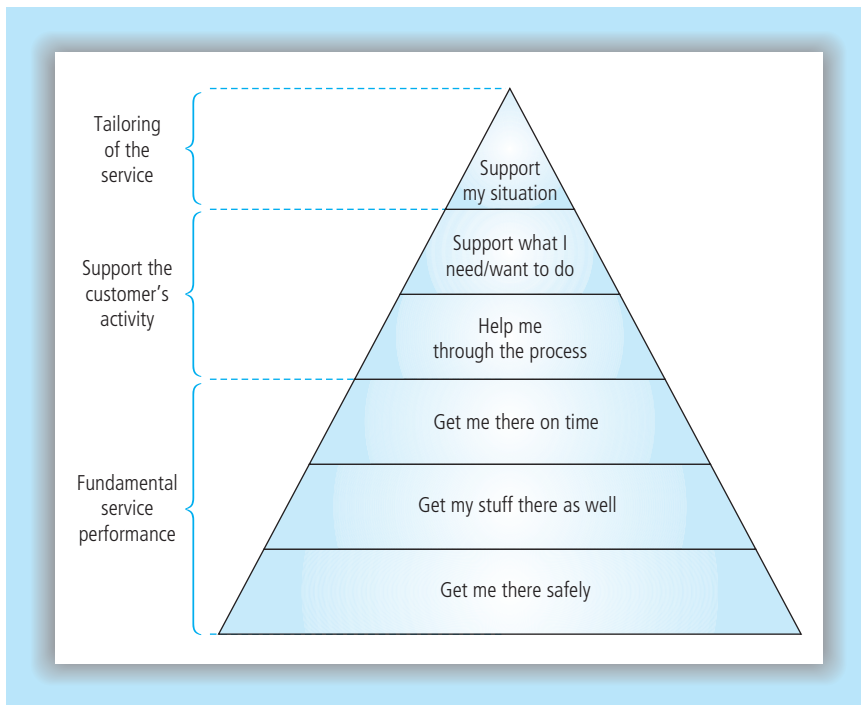


Figure 7.8
SAS airlines' understanding of customer expectations

The SERVQUAL model has been subject to much criticism, but it is still in widespread use in original and customized forms.²¹ One criticism is that customers often do not have clearly formed expectations, and

therefore that the disconfirmation approach is inappropriate. Some of these critics have developed an alternative, perceptions-only, model of service quality that they have dubbed SERVPERF.²²

Service guarantees

From the customer's perspective, guarantees can be an effective way to reduce risk and thereby increase value. A service guarantee can be defined as follows:

A service guarantee is an explicit promise to the customer that a prescribed level of service will be delivered.

Service guarantees can either be specific or general. Specific service guarantees apply to particular parts of the customer experience. For example:

Sleep tight or it's a free night. We guarantee it (Howard Johnson's).
PG&E will meet the agreed upon appointment time set with our customer during contact with our call centre or automatically credit your account with \$30 (Pacific Gas and Electric).

General service guarantees apply to the entire customer experience (see Figure 7.9). For example:

We guarantee to give perfect satisfaction in every way (LL Bean).
Guaranteed. Period (Land's End).

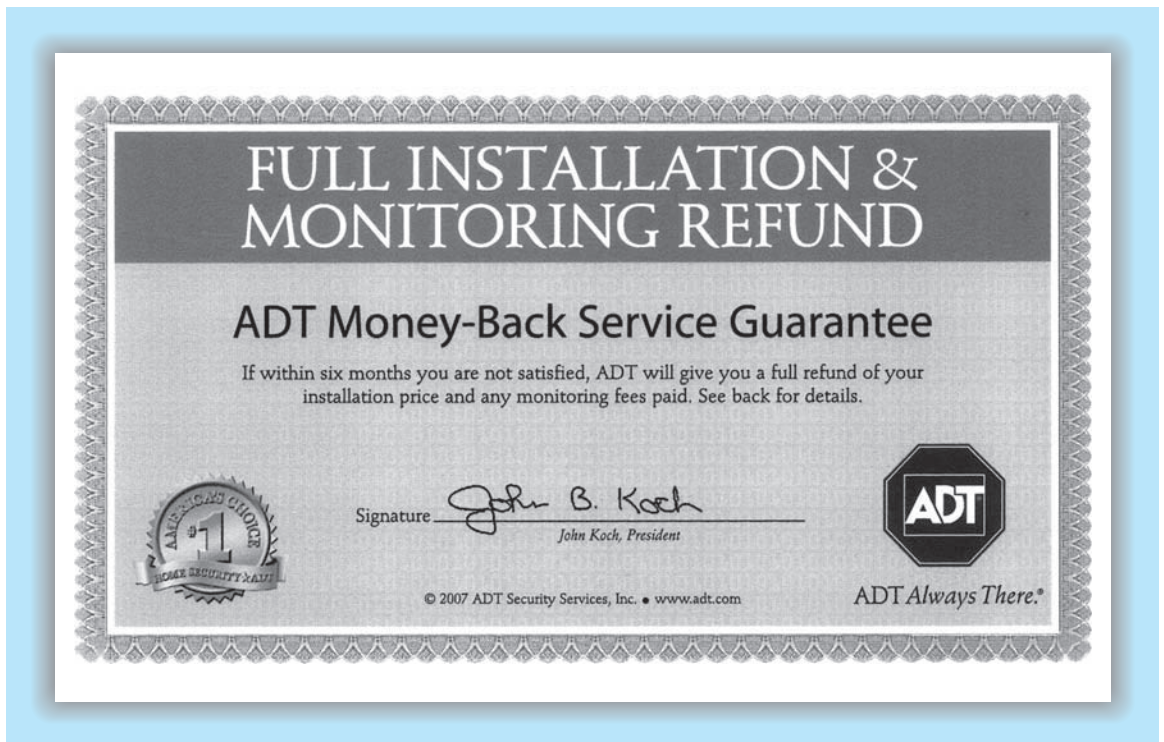


Figure 7.9
ADT Money-Back Service Guarantee²³

Although these examples are of guarantees offered to external customers, they can also be designed for internal customers. For example, the housekeeping supplies department at Embassy Suites guarantees that its internal customer, the housekeeping department, will get supplies on the day requested. If not, the department pays \$5 to the housekeeper.

Service guarantees can be customized for individual customers or segments. An IT service centre guarantees a three hour service to priority one customers and 48 hour service to all others. Should the company fail to honour these guarantees it 'fines' itself by issuing a credit note to the customers.

Some guarantees, such as the Land's End example cited above, are unconditional. Others are conditional. For example, the PG&E guarantee above does not apply when a customer makes a same day appointment or when a service person misses the appointment to respond to an immediate emergency. If the guarantee is unconditional and the consequence of invoking the guarantee is that customer doesn't have to pay, there is effectively zero financial risk.

Service-level agreements

Service-level agreements (SLAs) can be defined as follows:

A service level agreement is a contractual commitment between a service provider and a customer that specifies the mutual responsibilities of both parties with respect to the services that will be provided and the standards at which they will be performed.

SLAs can apply to both internal and external customer relationships. For example, it is not uncommon for utility companies to outsource their customer contact function to a third party. An external SLA is negotiated that carefully defines both parties' expectations of the services to be performed, the service processes to be followed, the service standards to be achieved and the price to be paid. The SLA may well form part of an enforceable legal contract. A number of metrics are used to measure performance of the supplier and compliance with SLA service standards. These include:

- **availability:** the percentage of time that the service is available over an agreed time period
- **usage:** the number of service users that can be served simultaneously.
- **reliability:** the percentage of time that the service is withdrawn or fails in the time period
- **responsiveness:** the speed with which a demand for service is fulfilled. This can be measured using turn-around time or cycle-time
- **user satisfaction:** this can be measured at the time the service is delivered or periodically throughout the agreed service period.

See Figure 7.10 for an example of a service level agreement scorecard.

Many companies also have internal SLAs between service departments and their internal customers. An IT services department, for example, may establish a number of different SLAs with different customer groups. It might undertake to process payroll for the human resource



Figure 7.10
Service level agreement scorecard²⁴

department or to maintain and service desktop devices for a contact centre. This is unlikely to be formalized in a contract.

SLAs create value for customers by reducing uncertainty about the services that will be delivered, their standards and costs. A successful SLA clarifies the boundaries and relative roles of customer and supplier. Each knows the other's responsibility. Service automation technologies discussed in Chapter 16 allow companies to manage service levels.

Service recovery programmes

Service recovery can be defined as follows:

Service recovery includes all the actions taken by a company to resolve a service failure.

Services fail for many different reasons.²⁵ Sometimes technical service quality fails; at other times the failure is in functional service quality. Sometimes the fault lies with the company, sometimes with the customer and sometimes with a network member. Typically customers are not concerned with who is to blame; they just want the situation resolved.

Research shows that when companies resolve problems quickly and effectively there are positive consequences for customer satisfaction, customer retention and word-of-mouth.²⁶ It has even been found that customers who have been let down, then well recovered, are more satisfied than customers who have not been let down at all.²⁷ This can perhaps be explained in terms of the RATER dimensions of service

quality. Getting service right first time demonstrates reliability, but recovering well after service failure shows empathy and responsiveness. Reliability can be programmed into a company's service production and delivery processes. Empathy and responsiveness demonstrate the human attributes of concern for others and flexibility. Conversely, customers who have been let down once, only to experience unsatisfactory recovery, can turn into 'terrorists' who actively look for opportunities to spread bad word-of-mouth.²⁸

When customers experience service failure, they have the choice of doing nothing or voicing their displeasure. Customers who choose to voice their feelings can complain to the service provider, complain to associates and others in their personal network, or complain to a third party such as a consumer affairs organization or industry ombudsman.

Equity theory suggests that customers who complain are seeking justice and fairness. Equity theory explains that customers compare the sacrifices they make and the benefits they experience (as in the value equation) to other customers' sacrifices and benefits. When customers pay the same price, but experience an unsatisfactory level of service compared to other customers, they feel a sense of inequity or unfairness. When they complain, they want the company to fix the imbalance. They want justice.

Research suggests that there are different types of justice. Figure 7.11 highlights the three forms of justice that complainants seek: distributive justice, procedural justice and interactional justice.²⁹ Distributive justice is achieved if the customer gets the material outcome wanted after a complaint. Customers might be satisfied with an apology or a credit note against future purchases. Alternatively, a customer may want the service to be reperformed. If distributive justice is concerned with what is received, procedural justice is concerned with the customers' evaluation of the processes and systems that are encountered during the complaints handling episode. Customers generally do not want to complete forms, provide difficult-to-find proofs of purchase or write formal letters confirming the complaint. These requirements do not suggest that

- Distributive justice
 - what the firm offers by way of recovery and whether this output offsets the costs incurred by the customer from service failure
 - distributive outcomes include compensation, re-performance, apologies
- Procedural justice
 - customers' perception of the process experienced to obtain recovery
 - some procedures offer prompt recovery, others delayed; some require complaints to be legitimized
- Interactional justice
 - the customer's perception of the performance of service recovery people
 - empathy, politeness, courtesy, effort

Figure 7.11
Service recovery and justice seeking

a company is organized and willing to resolve the problem quickly. Interactional justice is achieved if the customer judges that specific complaint-related interactions with the provider's people have been satisfactory. They want employees to be responsive and empathetic.

Value from processes

In the previous section we have described some business processes that help create customer perceived value: the service quality management process and the service recovery process. Elsewhere in the book we touch on additional processes that impact on customers: the order-to-cash cycle, the selling process, the campaign management process, the database development process and the innovation process, for example.

In Chapter 3 we defined a business process as a set of activities performed by people and/or technology in order to achieve a desired outcome. Business processes are how companies get things done. Companies are comprised of very large processes. IBM, for example, has identified 18 critical processes, Xerox 14 and Dow Chemical 9.³⁰ These big processes are in turn composed of smaller processes. For example, the manufacturing process takes a number of inputs – materials, technology, labour – and converts them into products. This big process is composed of several smaller processes, such as machining, assembly and packing processes. Companies have thousands of processes. But processes are more than simply workflow; they are also resources that can be used to compete more effectively, to create more value for both customers and company.³¹ Xerox's 14 key business processes appear in Figure 7.12. Many of these macro-processes have an impact upon customer experience or value perceptions, including customer engagement, market management, product maintenance and product design and engineering processes.


- 
- | | |
|---|---|
| 1. Customer engagement | 8. Supplier management |
| 2. Inventory management and logistics | 9. Information management |
| 3. Product design and engineering | 10. Business management |
| 4. Product maintenance | 11. Human resource management |
| 5. Technology management | 12. Leased and capital asset management |
| 6. Production and operations management | 13. Legal |
| 7. Market management | 14. Financial management |

Figure 7.12
Xerox's 14 key
business processes

Process innovation can create significant value for customers. For example, First Direct started out as a telephone bank with no branch network. Customer management was entirely IT enabled, with customer service being delivered from a number of call centres. The bank's customer

satisfaction ratings have been consistently higher than competitors' branch operations. Daewoo established a direct-to-customer distribution channel that replaced the normal distributor arrangements of other automobile manufacturers. Customer experience was under better control and costs were reduced. easyJet speeded up customer service by improving plane turnaround times from 50 minutes to 33 through improved teamwork.

Case 7.3

Process innovation at SECOM

SECOM is the largest supplier of security services in Japan. Historically, service was very labour intensive as security guards were located at client sites. SECOM automated the detection of security breaches by combining crime detection sensors and telecommunications technology and moving its guards to a central location, from where they were despatched to deal with incidents. The business experienced high growth as a result. Subsequently, new technologies were added; remote sensing, image enhancement, geographical information systems and automated payment systems for clients.

In this section, we examine one additional process that impacts on the external customer's perception of value: the complaints management process.

The complaints management process

Customers complain when they experience one of two conditions: their expectations are under-performed to a degree that falls outside their zone of tolerance, or they sense they have been treated unfairly. Equity theory, described above, explains the customer's response to being treated unfairly. Customers also have a zone of tolerance for service and product performance. The range of tolerable performance will depend upon the importance of the product or the particular product attribute that is giving cause for complaint. Tolerances will be stricter for more important products and attributes. For unimportant products and attributes, customers tend to be less demanding. Where customer experience falls outside their zone of tolerance, there is cause for complaint.

Nobody likes receiving complaints, but they are unavoidable. Even the best companies sometimes fail customers and give cause for complaint. Therefore, it makes sense to implement a policy and process to receive, handle and resolve customer complaints. A positive view of customer complaints accepts that customers who complain are giving you a chance to win them back and retain their future value. Not only that, but complaints provide information that can help you identify, and correct, root causes of problems. Furthermore, the presence of a documented complaints-handling process has been shown to be strongly associated with excellent customer retention.³² Worryingly, customers who don't complain may already have taken their business elsewhere.

A successful complaints handling process enables companies to capture customer complaints before customers start spreading negative word-of-mouth or take their business elsewhere. Research suggests that negative word-of-mouth can be very influential.³³ Up to two-thirds of customers who are dissatisfied do not complain to the organization.³⁴ They may, however, complain to their social networks. Unhappy customers are likely to tell twice as many people about their experience as customers with a positive experience.³⁵

Many customers who are unhappy don't complain. Why? There are a number of possible reasons:

- They feel the company doesn't care. Perhaps the company or the industry has a reputation for treating customers poorly.
- It takes too much time and effort.
- They fear retribution. Many people are reluctant to complain about the police, for example.
- They don't know how to complain.

Companies can address all of these issues by making their customers aware of their complaints policy and processes. A complaints management process that is simple and easy to access should facilitate the capture of complaints. Some companies use dedicated freephone and fax lines. Some reward complainants. Stew Leonard's, the Connecticut retailer, rewards in-store complainants with an ice-cream.

Complaints enter companies at many different customer touchpoints – accounts receivable, order processing, sales engineering, logistics, customer contact centre – and so on. A well-designed complaints-handling process will capture complaints from various touchpoints and then aggregate and analyse them to identify root causes. Ultimately this should enable the company to achieve a higher level of first-time reliability, reduce the amount of rework, and lift levels of customer satisfaction and

1. Make your complaints-handling policy and processes visible and accessible to customers and employees
2. Train employees how to respond to complaints
3. Ask for specifics. Not 'what do you think about your experience?'. Instead ask, 'what one thing could we have done better?'
4. Empower employees to resolve complaints
5. Install a dedicated free-phone line
6. Link complaints to your mission to become more customer-focussed
7. Designate a customer service executive to deal with written complaints
8. Enable customers to complain at all touch-points
9. Ensure all employees understand the complaints management process
10. Reward customers who complain
11. Collect complaints data and analyse root causes
12. Implement technology to support complaints-handling and generate useful management reports

Figure 7.13
Improving the
complaints
management
process

retention. An international standard, ISO 10002, has been released to help companies identify and implement best practice in complaints policy and process. Software is available to help companies improve their complaints-handling expertise.³⁶ Figure 7.13 details some ideas for improving complaints management processes.

Value from people

Many companies claim that people are their key differentiators, and a major source of customer value. This is especially so in professional services such as counselling, consulting and coaching where people are the product. The UK-based home improvement retailer B&Q has also added value to the shopping experience by recruiting former building tradesmen such as carpenters, electricians and plumbers to help customers diagnose their problems and choose the right products in-store. Even in the high-tech arena, people can be regarded as strengths that deliver value to customers. Nortel, for example, claims:

'At Nortel we believe that our people are our strength. Their knowledge, commitment and talents drive our success'.

There are many important roles that need to be filled for CRM to deliver its promise of enhanced customer retention and company profitability. We examine these in greater detail in Chapter 17.

One of the more important jobs in CRM is the customer contact role. The customer contact role is a boundary-spanning role. That is, the role occupant sits in the space between an organization and its external customers. They are paid by the company, but work closely with customers. Boundary spanners have two fundamental and interdependent roles: information management and relationship management. Boundary spanners are accountable for collecting information about customers. What are the customer's requirements, expectations and preferences? What are the customer's future plans? Who is involved in the customer's buying decisions? The boundary spanner may have responsibility for maintaining the accuracy of the customer data records. This information enables the role occupant to perform the second role, managing the customer relationship. This might involve winning, growing and maintaining the customer's business, handling customer queries and complaints, representing the customer's interests to his employer and ensuring the customer's satisfaction.

There is a trend towards key account management that is driven by a number of trends: global customers, consolidated purchasing, vendor reduction programmes and customers who want better service and closer relationships with their suppliers. The role of key account manager, national account manager or global account manager is extremely important. Occupants need an advanced, and rare, skill, knowledge and attitude profile including selling skills, negotiating skills, communication

skills, analytical skills, problem-solving skills, customer knowledge, market knowledge, competitor knowledge, customer orientation, as well as a detailed understanding of what their own company's network can deliver.

Value from physical evidence

Some companies create value for customers by managing physical evidence. This is especially important for service companies with intangible-dominant outputs. In the absence of physical evidence, customers may find it very hard to determine whether or not they are receiving value. Physical evidence can be defined as follows:

Physical evidence consists of the tangible facilities, equipment and materials that companies use to communicate value to customers.

Physical evidence includes a company's premises and their internal and external environments, print materials, websites, corporate uniforms and vehicle livery.

It makes sense for companies to audit and create an inventory of the physical evidence that can influence customers' perceptions of value. Banks, for example, generally occupy traditional buildings with columns, porticoes, steps and large, heavy doors. This is designed to communicate conservative values, security and probity. McDonald's uses primary colours, bright lights and the ubiquitous golden arches in the form of the letter 'M'. Hospitals convey impressions of good hygiene and care through white uniforms, immaculately clean premises and well-maintained gardens. You only need to reflect on the traditional clothing, livery and appearance of funeral services to understand the significance of physical evidence.

Web portals also act as physical evidence. The only physical evidence that remotely located customers who don't receive visits from sales representatives might have of a supplier is their web portal. Many companies have developed portals for their customers and partners. Users generally obtain access through a secure sign-on procedure and then have access to information relevant to their own role, for example as customer or partner. Managers of the portal can push information out to users on a segment or individual basis. Users can transact, communicate and enquire online in a secure environment. A web portal can be defined as follows:

A web portal is a website that serves as a gateway to a range of subject-related resources.

In addition to corporate portals, there are general consumer portals, such as Yahoo! (www.yahoo.com) and MSN (www.msn.com), and specialized or niche portals. There are many niche portals for special interest groups such as gardeners (www.garden.com), cricket fans (www.cricinfo.com),

investors (www.fool.com) and chief executives (www.ceoexpress.com). Portals act as gateways to the rest of the Internet, and often include features such as search engines, directories, customizable homepages and e-mail.

General portals provide customer value by bringing together related content from different sources, providing convenient access for users. For example, the website www.buzgate.org (see Figure 7.14) is a portal that provides access to a comprehensive array of online public and private sector resources for small- and medium-sized businesses (SMB).



Figure 7.14 Information availability online at www.buzgate.org³⁷

Portals like these function in much the same way as a high street retailer, in that they act as repositories for many different products (resources).

Value from customer communication

Companies are now able to create value for customers from communication practices that were impossible in earlier years. A significant change is that companies are now able to facilitate multilateral communication: company-to-customer, customer-to-company and even customer-to-customer. Traditionally customer communication has been one way: from companies to customers. The conventional tools for company-to-customer communication are unilateral: advertising, sales promotion, publicity, public relations and personal selling. With the exception of selling, these communication channels are non-interactive. Customer-company communication is enabled through e-mail, web forms, instant messaging, phone, fax, web collaboration, as well as old-fashioned correspondence. Companies can also facilitate customer-to-customer (peer-to-peer) communication by web logs (better known as blogs), chat rooms, newsgroups and online communities. Collectively, these are known as customer generated media (CGM). Southwest Airlines, for example, has established a blog intended to 'give our readers the opportunity to take a look inside Southwest Airlines and to interact with us. This is as much your blog as it is ours.

Three processes are responsible for the enhanced power of communication to create value for customers: disintermediation, personalization and interactivity.

Disintermediation

Today, the development of new technologies has led to the emergence of many direct-to-customer (DTC) communication tools including e-mail, direct mail and SMS messaging to cell-phones. Companies are now able to get their message direct to customers. Equally, customers can get their messages direct to companies and to other customers in the ways described above.

Personalization

High-quality customer-related data, CRM technologies and DTC channels, in combination, enable companies to tailor offers and communications to individual customers. This is what Don Peppers and Martha Rogers have called one-to-one marketing.³⁸ Data on customers' buying history and propensities-to-buy can be used to develop offers that meet with a much higher response rate and conversion rate than conventional mailings. The content, timing and delivery channels for communications can be based on customer preferences.

Another form of personalization is found online. CRM technologies are available that allow customers to personalize their own corporate web pages. Customers of www.lastminute.com can personalize their home page (mylastminute.com) using technology that stores their preferences. This enables the company to refine its messaging to the customer base. It claims to achieve click-through rates that are 30 per cent higher than non-targeted messaging.³⁹ You can also create your own daily newspaper at www.ft.com, based on your personal interests and preferences. This can then be used as your homepage.

Case 7.2

Customized communication at Mercedes-Benz

Mercedes-Benz decided to launch its new M-Class off-road vehicle in the USA knowing that it was already a crowded market. However, they accessed publicly available and corporate data to obtain details of all current owners of off-road and Mercedes vehicles. Mercedes then undertook a series of personalized direct mailings to the database, with the objective of raising awareness about the vehicle. The pretext for the communication was to ask for help in the process of designing the vehicle. There was an overwhelming response and the respondents were sent questionnaires which asked for guidance on design issues.

Two months later Mercedes pre-sold its first year sales target of 35 000 vehicles. It had been expecting to spend some US\$70 million marketing the car, but by using this CRM-based approach it only needed to spend US\$48 million, saving US\$22 million. The programme was so successful that Mercedes is looking to use the same approach in the future with other model launches.

Personalization can also be performed on communications between customers and employees, such as customer service agents. For example, scripts can be tailored to enable agents unfamiliar with a product or customer segment to perform competently in telephone interactions.

Interactivity

Interactive technologies have been around since the advent of the telephone. Recently, the Internet has revolutionized the scope for interactivity through three major technologies: e-mail, instant messaging and the World Wide Web (WWW). E-mail enables customers and companies to interact effectively. For example, customers can e-mail for information that is unavailable on the frequently asked questions (FAQ) pages of corporate websites. E-mail gives customers access to a specific named person or work group, such as help@ or info@. Contact with a name gives customers the sense that there is an individual who is taking care of them. Instant messaging enables communications to take place in real-time, which is not always possible with e-mail.

The WWW is an Internet-enabled service that allows computer users to communicate globally with each other. A company can upload a website and anticipate huge reach. Websites come in a variety of

forms: some are simply electronic brochures; others enable transactions to be made; another group of sites are highly interactive. Some excellent websites offer an experience similar to human dialogue. Configuration engines allow the most appropriate products to be offered based on an analysis of the customer's specific needs. Problem resolution logic allows customers to find the best solution to a problem, and web chat windows allow human dialogue over the web, if all else fails.

Value from channels

The traditional task of the distribution function is to provide time and place utilities to customers. Effectively this means getting products and services to customers when and where they want. Consumer goods companies have usually constructed channels using intermediaries such as wholesalers and retailers. B2B companies usually sell direct or employ industrial distributors. The location of service providers may be critical or irrelevant to the creation of value for customers. Customers want their grocery retailers to be conveniently located, but don't care where their Internet service provider is located.

An emerging task for intermediaries in the B2B environment is value augmentation. Channel partners in technology industries add services and complementary products that are not available from the core product manufacturer. The purchase of an ERP system, for example, may require implementation services, technical services, business process re-engineering, change management, customization of software or specialized hardware, such as radio frequency (RF) handheld units in the warehouse. Channel partners not only distribute the ERP product, they also provide or coordinate others to provide these additional products and services.

Internet-enabled disintermediation has allowed many companies to replace or supplement their traditional bricks-and-mortar channels. Many companies have elected to develop transactional websites so that they can sell direct. Others have developed brochureware sites that direct interested prospects to traditional channel members. One major benefit attached to this latter option is that it reduces the level of channel conflict that can be extremely high if an intermediary believes that a supplier is attempting to sell direct to the intermediaries' customers. Additional routes to market include:

- portal directories such as Yahoo! and Excite
- search engines such as AltaVista and Infoseek
- electronic shopping malls such as www.eMall.sg and www.emallroad.com
- virtual resellers such as Amazon and CDNow.⁴⁰

Customers may find that it is too costly and inefficient to deal with a large number of potential disintermediated suppliers. This has created

opportunities for reintermediation. Reintermediation adds an electronic intermediary to the distribution channel. Illustrations include:

www.netbuydirect.com for a wide range of factory-direct products

www.lastminute.com for holidays, flights, accommodation, car hire and gifts

www.laterooms.com for discounted hotel rooms

www.moneyworld.com for mortgages, credit cards, bank loans, insurances and pensions.

Ultimately, companies face four options when creating value for customers from electronic channels.⁴¹

1. **No Internet sales:** this might be the best option for small businesses with a local clientele. Companies on the Internet access an international audience. If they are unable to fill the demand that might arise, they are perhaps better off using traditional channels.
2. **Internet sales by reseller only:** a reseller, selling on behalf of many producers, may be big enough in terms of customer numbers and revenues to invest in online transactional capability. Fulfilment of orders may be performed by the reseller or producer.
3. **Internet sales by producer only:** it would be unusual for a company selling through bricks-and-mortar channels to establish a web presence that is in direct competition to those channel members. This would generate significant channel conflict.
4. **Internet sales by all:** both reseller and producer sell online.

Which of these strategies will add value for customers depends upon whether customers enjoy additional time and place utility from online purchasing.

Summary

This chapter has stressed the importance of creating value for customers. Value creation and delivery is a role for strategic CRM. Value can be thought of as the relationship between the benefits experienced from a product or service and the sacrifices made to enjoy those benefits. Value is therefore enhanced when sacrifices are reduced or benefits increased. Three major types of sacrifice have been identified: money, search and psychic costs. Companies can offer improved value to customers by creating and delivering better solutions to customers' problems.

Researchers have identified three major value delivery strategies that successful companies have adopted: operational excellence, product leadership and customer intimacy. Marketers are generally responsible for designing customer value propositions. Value propositions are constructed by mixing together a number of variables that will

appeal to customers. These variables are known as the marketing mix. For goods manufacturers they comprise the 4Ps: product, price, promotion and place. In the services environment, the 4Ps are supplemented by three additional Ps: process, physical evidence and people. In the B2B environment, value propositions have long been customized. Customization is now emerging as a powerful force in the B2C environment too. Any of the 7Cs can be customized.

Management can create additional value by their management of the 7Ps. For example, product innovation, branding and product–service bundling are ways to create additional value. Similarly, service quality improvement programmes, service guarantees, service level agreements and service recovery programmes may be seen as value adding.

The Internet, customer-related databases and CRM technologies are allowing companies to tailor their customer communication strategies at segment or, often, unique customer level. Messages can be communicated directly to customers, side-stepping the media long used for broadcast advertising. They can also be personalized, not only in the form of address, but also in content and timing. Unlike traditional media, the newer channels, including the Internet, are interactive. Companies can get instant feedback from their customers.

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