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Service differentiation through relationships in b2b Product-Centric Businesses (PCBs)

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Service differentiation through relationships in b2b Product-Centric Businesses

1. Introduction

Many commentators such as Levitt (1986), Porter (1998), Grönroos (2000) have noted that traditionally Product-Centric Businesses (PCBs), i.e. companies whose primary activity has been selling products have increasingly focused on their services to provide differentiation. Service makes up one part of what Porter (1998) describes as the 'value chain' with Sustainable Competitive Advantage (SCA) being achievable through each activity in this chain. Porter (1998) proposes that market differentiation comes from firms in the same industry having a different value chain and therefore competing on a different basis from each other. Many authors have built on this work to propose that SCA is achievable through a firm's resources and capabilities, e.g. Barney (1991), Amit & Schoemaker (1993) and Fahy (1996). Fahy (1996), for example, coined the expression the Resource-Based View (RBV), whereby firms are viewed as bundles of resources and capabilities that provide the basis for SCA, with companies basing their strategy on the resources and capabilities best suited to the markets they serve. In the area of PCBs' services, different capabilities have been suggested including those surrounding information & communication technology (Allmendinger & Lombreglia, 2005; Auguste et al, 2006), the unique skills of a company's employees (Matthyssens & Vandenbempt, 1998; Neu & Brown, 2005) and the culture, organisation and human resources of the company (Bharadwaj et al, 1993; Matthyssens & Vandenbempt, 1998).

Whilst the concept of the value chain provides an anchor reference for later work on SCA, other academics have questioned its applicability to service industries. For example, Stabell & Fjeldstad (1998) view the value chain as a more appropriate analytical tool for traditional manufacturing companies and less applicable for service industries, since it obscures where value is being created. In addition to the value chain, these authors propose the concepts of the 'value network', whereby value is created by organising and facilitating exchanges between customers, and the 'value shop', whereby value is created by enabling customers to move from an existing state to a desired state through problem solving. Stabell & Fjeldstad (1998) note that organisations will often have more than one distinct value configuration, with hybrid organisations utilising two or more, possibly as part of one primary activity and other support activities. This is an appropriate model for many PCBs when developing a service capability, whereby the organisation may still have a manufacturing function (chain), but is also focused on solving customers' non-standard problems using experienced professionals (shop) and may also have customers that communicate with each other to resolve technical faults on common equipment (network).

The underlying assumption of SCA is rejected by authors such as Gadde et al (2003), who see conflict and rivalry between companies as less important than the development of relationships and company inter-dependence. This is more akin to the Interaction Approach as suggested by the IMP Group (Turnbull et al, 2002), which addresses the important issue of buyers and sellers being active participants in long-term relationships. This is a critical issue for many PCBs delivering services.

This research sets out to identify what factors are important to PCBs in creating success with respect to their service operations, bearing in mind the two approaches

outlined above, namely internal corporate resources and relationships. One of the objectives of the research is to better understand the capabilities that provide differentiation and consequently success, with this construct being comprised of a number of different factors. Although several scholars have researched this area over the last 10 years, there has not been an approach that fully addresses those factors that create success. To aid this research, a model (figure 1) is being developed to identify the important factors that create success for a PCB's service operations, with the current version shown below.

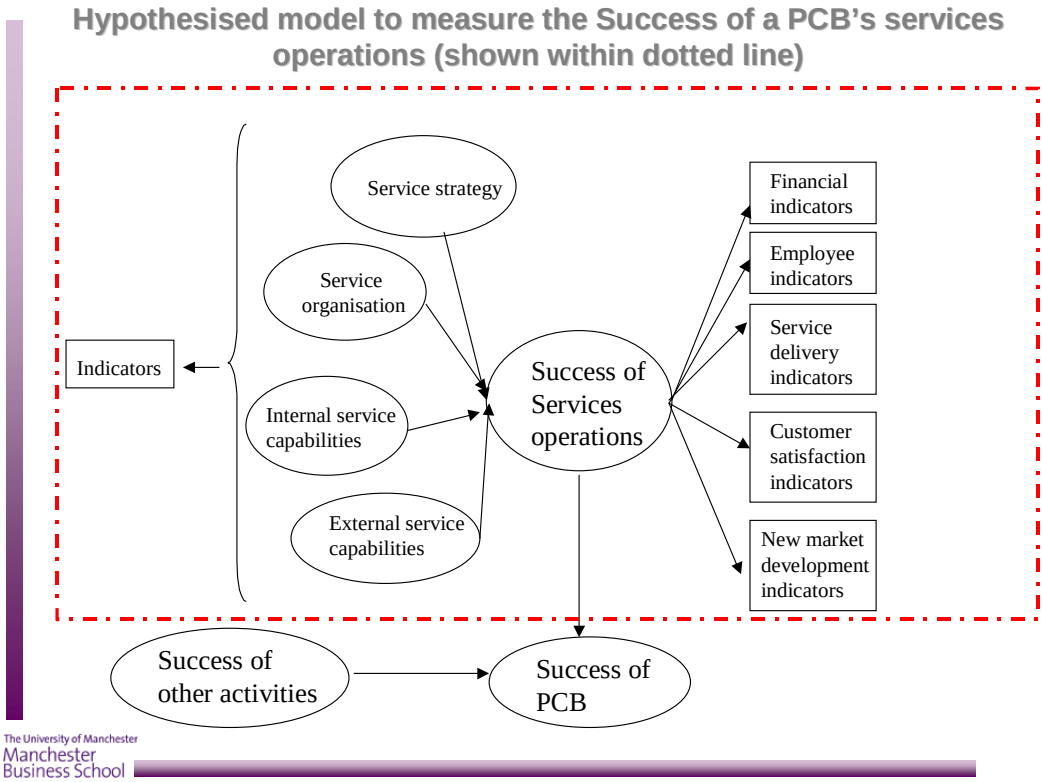

Figure 1.

The model shows how a PCB's service strategy, its service organisation, internal service capabilities (e.g. people, processes, product heritage) and external service capabilities (e.g. relationships with customers, other companies) are the factors that will affect the success of its service operations. This paper concerns the external service capabilities and addresses the issue of how a PCB's service relationships with other organisations can significantly enhance its market differentiation and success.

For clarification, external service capabilities concern the PCB's relations with its customers and other companies, such as other product suppliers, sub-contractors providing one element of an overall service or distributors providing services to the PCB's customer base. Equally, the focus of the research is chargeable service offers, e.g. consultancy, systems integration, maintenance, technical support, training and outsourced operations. Other services research has focused on 'customer service', which has been defined by Parasuraman (1998) as the overall quality of service provided by a supplier as perceived by the customer. Whilst the dividing line between service offers and customer service can be somewhat blurred, Parasuraman (1998)

notes that when service offers are given away ‘free’ with the product they are more akin to customer service.

2. Literature review

a. Why are PCBs seeking differentiation through services?

Business to business (b2b) PCBs, even those in high-tech sectors such as telecommunications have found it increasingly difficult to differentiate their products, with low-cost competitors from countries such as China aggressively pricing their products to gain market share. It is not therefore surprising that companies faced with these challenges are turning to their services businesses, with Oliva & Kallenberg (2003) summarising three of the main reasons why PCBs develop service capabilities; increased revenues, potentially higher margins and a more stable revenue stream. Davis (2003) elaborates the latter point by stating that to some extent services are counter-cyclical to products, i.e. as product sales slow so service sales often increase. Michel et al (2003) see the reasons more in terms of adding flexibility to their customer offer, creating value for the customer, being an important part of a differentiation strategy and enriching their position within the customer’s business.

A company may therefore decide that a strategy based on an enhanced role for services is the correct one, but the change from a PCB to one based more on services is not without difficulties. Despite some high profile successes in making this transformation such as IBM (Mathieu, 2001), research suggests that many companies struggle to make the change successfully. Authors such as Gebauer et al (2005) and Brax (2005) have defined this as ‘the service paradox in manufacturing companies’, whereby increasing investment in a services business widens its scope but not the profitability of the company. These authors identify significant differences between a services and manufacturing culture, with the former based on innovation, customisation and flexibility and the latter on generating efficiencies. Michel et al (2003) also note that a true services culture is not easily obtained for product companies if services are a means to sell more products. PCBs therefore need to decide whether to become more service-orientated and if so what are the key factors that determine whether this strategy will be successful at creating differentiation.

b. What role can relationships play in creating differentiation?

This paper addresses the relationships PCBs have with their customers and other companies and starts with a discussion on relationship marketing.

i. Bb2 relationship marketing

Many authors have defined relationship marketing, e.g. Morgan & Hunt (1994) characterised it as establishing, developing and maintaining successful relational exchanges. Others such as Parvatiyar & Sheth (2000) have sought to limit the scope of the definition to be mainly concerned with relationships with customers, although acknowledging that other organisational relationships also have a role to play. In the area of PCBs the need to include other organisations beyond the end customers is clear, with partnerships with other PCBs increasingly important.

Day (2000) notes the differences between relationships, from 'transactional' through 'value-added' through to 'collaborative', with the latter being characterised by close linkages at many levels and mutual expectation of long-term benefits. The environment in which many PCBs operate is more akin to one based on collaborative exchanges and the need to build trust is critical, i.e. where one party has confidence in their partner's reliability and integrity (Hutt & Speh, 2007).

ii. PCB-customer relationships

There are strong reasons why PCBs would wish to move from more of a transaction-based to relationship-based approach with customers (as set out in section 2a). From the customer's perspective, they will seek to develop closer relationships with some suppliers to bring about cost reductions through outsourcing (Wise & Baumgartner, 1999) or increased revenue (Ford, 2002), although this exercise may result in a reduced supplier base (Gadde & Snehota, 2000). The buyer will often seek to develop these 'partnership' relations when outsourcing certain operations that they could undertake in-house but have chosen not to because of their desire to focus on those aspects they see as core to their business (Gadde & Snehota, 2000). There are however issues with outsourcing non-core activities irrespective of the strength of the relationship, one of which being a loss of control, as Hakansson & Snehota (2002) identify. In other words, if an outsourcing arrangement involves the transfer of a company's staff and then something goes wrong with the relationship, getting those staff back may be impossible. A supplier must therefore try to build up a level of trust in the relationship to allay these fears. Gounaris & Venetis (2002) identified that it was the quality of industrial services that a service provider had previously supplied that was important in developing trust in mature relationships. This point is enhanced by the IMP Group (2002), who note that the characteristics of the product or service that is being exchanged will have a significant impact on the relationship as a whole, with the intangible nature services enhancing uncertainty over whether the supplier will meet the customer's needs.

Scholars researching the services that PCBs offer have highlighted a 'solution approach' to the customer as being critical. Sawhney (2006) defines a solution as an integrated combination of products and services customized for customers, which allows them to get a better outcome than they would have from the individual components of the solution. Matthyssens & Vandenbempt (1998) proposed that offering a pro-active total solution (a "one-stop shop") was a key success factor. Neu & Brown (2005) built on this idea by emphasising the need for front-line services personnel to act as 'trusted advisors' and for PCBs to have a learning relationship with individual customers, whereby both parties learn about each other's needs and capabilities over time. Tuli et al (2007) however, believe that Sawhney's (2006) definition of a solution is one more used by suppliers and that customers see a solution as a series a supplier-customer relational processes, from requirements definition, through customisation & integration, through deployment to post-deployment customer support. There must be some doubt however whether Tuli et al (2007) have identified anything particularly new since there will often be an implicit service wrap around many product offers, which would occur whether this is labelled a solution or otherwise.

iii. Relationships with other companies

Ford et al (2003) and Hutt & Speh (2007) identify that distributors can be an effective means to service the aftermarket of a manufacturer's products, with the latter suggesting that they are important both to suppliers and customers, who may view them as an extension of their 'buying function' providing advise and suggestions for product use. However, Buttle (2004) identifies that distributors may not necessarily be working towards the same objectives as the manufacturer. In the PCB environment, this could be offering services on another PCB's products or services that result in less take up of the PCB's products.

Less research has been identified about PCB relationships with third parties (i.e. organisations such as other product suppliers, systems integrators and distributors) than with customers. This is probably because early research viewed services as primarily something applied to a PCB's own products, whilst subsequent research suggesting services independent from own label products has failed to address the critical nature of relationships with other companies, e.g. Auguste et al (2006). One researcher who did address this area was Mathieu (2001), who suggested that PCBs could work collaboratively with competitors to help build and maintain the skills & resources to provide competitive advantage, with the PCB focusing on core activities and using partners for those on the periphery. As the market for PCB services has developed, so commentators such as Araujo & Spring (2006) have noted that when customers have transferred what were internal operations into external services, it has led to complex relationships between specialised producers and service providers bringing growth in service provision.

3. Methodology

Research for this paper has been two-staged; firstly, desk research to analyse large UK PCBs that are using services to differentiate their businesses and secondly, interviews with managers in a number of these PCBs to better understand their success drivers for services. This methodology is designed to answer the previously stated research question concerning which factors are important to PCBs in creating success with respect to their service operations.

a. Desk research

The criteria for selecting PCBs to study were that the companies were manufacturers operating in the UK with a turnover greater than £200M pa and strongly using services to differentiate their businesses. An initial assessment was made of every company that met these criteria using the Fame database and company websites, with those companies that did then segmented by industry. The companies were then assessed to determine their use of services and the importance they attached to them, e.g. do they have a separate division selling services? The research has focused on larger PCBs with smaller ones to be assessed by quantitative research at a later stage. An initial list of 30 large PCBs was identified as being suitable to arrange interviews with according to the above criteria.

b. Qualitative research

The second stage of the research was to interview a number of industry executives involved in managing or working in their companies' service businesses. Although 30 companies were identified in the desk research, given that not every company approached would want to take part, a minimum target of 20 was set with whom to arrange interviews, operating across a range of sectors. Each interview was semi-structured, taped with the interviewees' responses to the different questions transcribed and returned to them for validation.

c. Data analysis

This research is being analysed using template analysis, which is a technique used to thematically organise and analyse textual data (King, 2004). King (2004) notes that the technique is useful when comparing the perspectives of different groups within a specific context, with the context of this research being managers in b2b PCBs who have responsibility for their companies' services businesses.

An initial template was created after a literature review and three pilot interviews to test the usefulness of the questions. A strength of template analysis is that by continuing to analyse results as they become available a good perspective on the subject can be reached before the completion of all the interviews. The interviews were initially analysed manually and then by using the qualitative research package NVivo.

d. Limitations of methodology

There are at least two potential limitations to the methodology used to investigate the research question. Firstly, even though the desk research identified the population of large UK PCBs, those chosen for interview were ones that were clearly using services as a strategy for differentiation. This will result in a bias towards those PCBs using services rather than some other method to provide differentiation. A more comprehensive postal survey is planned for later in 2007 to better identify the service strategies of the wider population.

Secondly, this is a 'supply-side' investigation with the unit of analysis being the PCB or a division of the PCB, meaning that PCBs' customers have not been interviewed as part of the research, since the importance of each measure of 'service operations success' can ultimately only be assessed by the PCB itself. If the unit of analysis was the customer relationship then success could only truly be judged by both parties. A previous paper in a related area (Homburg et al, 2000) also adopted this approach to measuring success.

4. Results

In total, 40 managers have been interviewed for this research from 22 PCBs (although given that some of divisions of the PCBs are effectively standalone businesses the number is 25). A breakdown by sector is shown overleaf. The majority of interviewees worked in their company's services businesses, either in general

management, sales, marketing or service delivery positions. The interviews took place between November 2006 and July 2007.

Sector	No. PCBs	No. interviewees
Aerospace & defence	3	6
Building materials	1	1
Chemicals	2	4
Energy	3	3
Electrical machinery	2	3
Information technology	4	8
Medical systems	1	1
Metals	1	2
Telecommunications	4	6
Transport	4	6
Total	**25**	**40**

A number of factors have been identified during these interviews that PCBs believe create success for their service operations (see figure 1). Those that have been grouped under the heading of 'external service capabilities' concern relationships between the PCB and their customers and other companies and are discussed below.

a. Relationships with customers

A number of themes have been identified: i) engendering trust and confidence in a relationship, ii) relating services offered to the customer's business model, iii) being product agnostic, and iv) a solution approach. These will now be discussed in turn.

i) Engendering trust and confidence in a relationship

The importance of developing strong relationships with customers as set out by many authors previously is confirmed by this research, with many interviewees stressing the need for the customer to trust them and be confident in handing over work, possibly in an outsourcing arrangement. The issue is therefore how to create the right level of trust and confidence. One PCB said that it was their ability to show empathy between their position and that of the customer's that was important, e.g. the logistics services they offered were required both by themselves and other companies involved in manufacturing. Also, several other PCBs spoke about how having staff 'embedded' with a customer meant they can act a part of the customer's team.

A PCB's reputation could also have attributes that can be successfully leveraged in a services environment, e.g. one PCB stated that research had shown that customers believed them to be a company that 'didn't walk away from problems', with this being an important issue in the delivery of a long-term services contract. Equally, other PCBs have used strong reputations for security or safety as levers in the services environment, whilst others have emphasised their longevity, having strong financial resources and a good local presence. In some cases the customer may not want a supplier who has all the latest technology at their disposal but rather a dependable operator who won't let them down over the long-term.

One interviewee believed that the market was fed up with empty and broken promises and that an approach based on 'realism' was the way forward, i.e. not over-stating what you can do, but when you say you will do something, actually doing it! He felt that this left the company vulnerable to some extent from competitors that over-hyped what they could actually do, but in the long run this was the best approach to gaining customer trust and confidence. Another interviewee stressed that a PCB should have no ego and not pretend that they know better than the customer, because quite often they do not.

Several interviewees stressed that trust and confidence was built up slowly in a relationship, with the need to 'get the basics right' first, such as on-time in-full deliveries, before moving onto more complicated services on own brand products and possibly these services on third party products (i.e. those of other companies). This supports the argument put forward earlier by Gounaris & Venetis (2002) that it was the quality of industrial services that a service provider had previously supplied that was important in developing trust in mature relationships. One person used the expression 'eating the elephant in small chunks' rather than trying to do it all at once! This way knowledge of the customer's business is built up to enable more complicated activities in future. Another aspect of this emphasised by more than one interviewee was being predictable and doing what they said they would, so that the customer always knew that the PCB could do the job or advise if there were any issues affecting its completion.

ii) Relating services offered to the customer's business model

A trend identified in this research is the greater alignment of a PCB's services to that of a customer's business processes. This issue has previously been addressed by authors such as Mathieu (2001) and Gebauer et al (2005) who stated that services related to a customer's business provide more SCA than services related to products. An interviewee addressed this point concerning technical support contracts, whereby it was no longer just a case of meeting Service Level Agreements (SLAs), but rather judging the impact of an incident on the customer's business. This approach may increasingly be factored into future SLAs, since there is little point achieving a desired level of service 99 times out of 100, if the other one results in a massive loss for the customer.

Another example of this trend that one interviewee gave was at the implementation stage of a mobile phone network, i.e. instead of the customer saying they want a certain number of base stations in specific locations to provide coverage, they will state the level of coverage they want in a particular area and leave it up to the PCB to determine how many base stations are required and where to put them. The onus and risk has thus been shifted from the customer to the supplier. Equally, in another example in the transport sector, the customer expects the PCB to provide them with the maintenance schedule of the vehicle, including where and when the work will be carried out.

Several PCBs now speak of their service businesses in terms of availability, with one of the leading exponents of this approach stating that they prefer it if the customer dictates the output required, enabling them to offer an asset's availability (e.g. a plane) at a fixed price over a give period of time. This approach also works with

services, with some PCBs stating that their businesses were moving towards offering SLAs based on customer processes rather than selling products or standalone services. One PCB hosts regular meetings with their sub-contractors, the customer and their end-users to fully identify all the factors that could stop them delivering on the level of availability required by the customer. Another spoke about the pricing of services in this environment as more to do with what value the PCB brings to the customer and what it would cost them if the service were not provided (or if they had to do it themselves). In this environment the customer is paying for when the asset is working rather when it is not, i.e. paying to fix an asset is akin to paying twice since if an asset is not available it is not making money *and* it is costing money to repair.

A PCB with a wide range of customers will be well placed to see how different operators are driving their businesses, with 'low cost' operators in several markets such as telecoms and transport taking a very different perspective as to what is their core business. In this situation, customers will increasingly look to PCBs to provide an asset or service on an availability basis since they have the product knowledge and are increasingly developing the operational know-how of how that product is being used. Once this is combined with knowledge of third party products, the PCB is in a strong position to differentiate itself against lower cost competitors whose knowledge is limited to basic services on their own products.

Another facet of this issue is trying to develop a good understanding of what customer's customers or end-users require. Some PCBs have achieved this by having a product range that addresses this market as well, with this enabling them to identify future end user requirements and trends. Another PCB said that their customers had organised workshops with end customers to bring home to the PCB's engineers the impact of un-resolved technical faults.

iii) Being product agnostic

A few interviewees expressed the view that only by divesting the business of products could a PCB truly act in the customer's best interests, since otherwise there would always be pressure on them to sell more products even if it wasn't in the customer's interests. Others have disputed this view, although it would appear that unless there are very strong 'Chinese walls' between product and service businesses this suspicion could be in customers' minds.

Several PCBs adopt the position that whilst they have the capability to deal with third party products, they make no secret of the fact that they have a suite of products, which they will sell to customers if it is in both parties' interests to do so. This third party capability may not be widely promoted but instead used tactically with key customers, with the aim to change out a competitor's legacy equipment to own brand equipment in the long run.

iv) A solution approach

A solution approach was something many interviewees mentioned as a key factor in dealing with customers, along the lines suggested by Sawhney (2006). One interviewee used the analogy of a doctor, whereby the PCB will go to a customer's site to 'diagnose a problem', then provide the 'medicine' to fix the problem and put in

place a follow-up regime to check its still working. Other interviewees expressed this in terms of the need to understand the customer's problems, their competitive landscape and business objectives and to be able to devise a solution. This must precede any attempt to sell products, i.e. this is a consultative engagement that should not feel like a selling activity (as previously noted by Neu & Brown, 2005). As one interviewee said,

"If this approach is shaped towards a specific end point then you are failing. You may invest and work with the client and find a solution, at which point you may find that you have created an opportunity for another company. This is okay because you will have acted in the best interests of that customer and performed as a trusted advisor, gained respect and enhanced the relationship because of it".

Some interviewees have said changing the orientation of a PCB from one selling products to one that is a more solution-based based is incredibly difficult, with the 'medicine' quite often not the sale of more equipment or even own brand services. Unlike in say a pure services company where the sales teams will perhaps be more used to selling solutions, many PCBs still have account managers who are likely to have a product rather than service focus. This approach therefore requires strong consultative sales skills as well as a good knowledge of own label products, those of third parties and other items such as application software that 'link' products together. One interesting factor with this sales process is that the finishing point may not be what the customer originally asked for, so flexibility in the whole approach is vital.

Whilst there are those who will question the credibility of a PCB genuinely acting as a consultative solution seller, some interviewees have said that their superior technical know-how of the products often gives them a 'voice' with the customer, even if it is heard in addition to the more traditional solution sellers.

b. Relationships with other companies

i) Distributors and sub-contractors

Many PCBs use distributors to reach customers that they cannot service directly or for whom an intermediary is a more appropriate route to market. The ability to quickly and cost effectively increase geographic coverage has been cited as an important reason for adopting a strategy based on the use of distributors. The research supports Hutt & Speh's (2007) view of the importance of this route to market for PCBs.

Often PCBs will accredit distributors who conform to guidelines, e.g. having a certain number of trained engineers, holding a stock of spares and backing off support arrangements with the PCB. One PCB manages and monitors the effectiveness of their distributors through use of a handbook that sets out the standards for both 'hard' issues such as repair turnaround times and also the 'softer' issues, such as engineers being dressed appropriately. Some interviewees stressed the need for distributors to be treated as though they were local offices of the PCB and were expected to maintain similar high standards.

In addition to a number of core services that the PCB will mandate the distributor to offer, many will also provide products and services appropriate to their customers.

Where the distributor is in a pivotal position with a customer and has relationships with competing PCBs, this can cause problems if the rival firm can influence the distributor to promote their products over another's - Buttle's (2004) point made earlier. One PCB in this position tries to enhance the power of some distributors with whom they have strong relationships in order to reduce the influence of others that may be closer to a competitor.

ii) Other PCBs and System Integrators

As PCBs move towards more of a consultative-based approach to selling so the need to work with other PCBs and systems integrations increases, as the 'solution' a customer is after may well not be deliverable by just one company. This is an important area for PCBs and the development of solutions in general since it is unlikely that the answer to the customer's problems will come from one company alone, even though literature in this area (e.g. Sawhney, 2006) makes little mention of the need to form effective partnerships with other suppliers.

One interviewee highlighted the difficulties that some PCBs might have in forming the correct relationships and identified two management styles; one dictatorial, primarily emphasising the needs of the PCB, whilst the other being more relationship-based, with this being the appropriate style where a consortium has been created to deliver the solution.

Several interviewees mentioned that it is now possible to be the lead supplier for one contract and a sub-contractor in the next, often with the same companies in the consortium – this was dubbed 'coopertition' by one interviewee! Flexibility is now a necessary part of a PCB's culture, to be able to lead or be led in a partnership as befits the needs of the customer. One PCB was even audited by the customer from the CEO through to the shop floor to identify the company's partnering behaviour.

Where a PCB has a well-developed service capability it may be able to position itself as a service vendor to a range of other PCBs, particularly if its product portfolio does not compete with theirs. If arrangements can be put in place for a number of leading product suppliers for a particular market, this could be a differentiator because as one interviewee noted although many companies claim to 'work with all the badges' in reality they will often only have strength in depth with one or two.

5. Conclusions

This is a 'work in progress' paper and as such this area of the paper has not been fully completed, although by the time of the IMP Conference the implications will be clearer.

This research has shown that when b2b PCBs enhance the role of services in their businesses, the importance of relationships both with their customers and other companies increases. Previous research on PCBs developing service capabilities has addressed to some extent the former but not particularly the latter, with this capability critical to the delivery of solutions.

As PCBs extend their service offerings to the core processes of their customers' businesses, relationships that may have been transactional in nature (i.e. a series of one-off transactions) become more intimate and long-term, with the risks and rewards higher for both parties. To achieve this position, PCBs need to adopt a more consultative sales approach and build on a track record of excellent service performance to engender trust in the relationship. However, if PCBs are not prepared to move their relationships with customers in this direction, they may be usurped by other companies that are, be they other PCBs or more traditional service companies. This is because many companies view strategic relationships with a few key suppliers as a way that they can reduce costs and risks and focus more time on growing their businesses. However, where PCBs still have strong differentiated product portfolios, services that support and enhance these may still be the best approach to service operations success.

Although this paper has focused on what has been described as a PCB's 'external capabilities', another area of the research has addressed the 'internal capabilities' together with issues concerning services strategy and organisation. One of the main developments from this work is the need for academics to consider all factors as being critical to providing success in the area of services, i.e. relationships are important but so are the PCB's internal resources and strategic direction.

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