

UNIVERSITY OF OTTAWA

# Services Marketing

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ADM 3322M – Marzena Cedzynski

**Kay Gan**

**Winter 2014**

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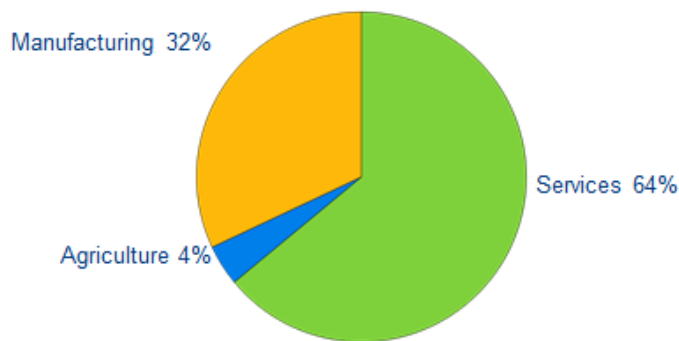
# Chapter 1: New Perspectives on Marketing in the Service Economy

## Why Study Services?

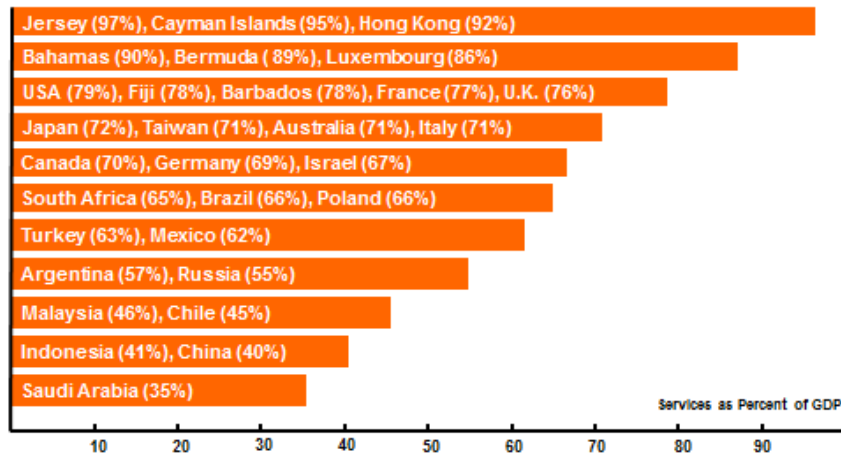
- Services dominate most economies and are growing rapidly:
  - Services account for more than **60% of GDP worldwide**
  - Almost all economies have a substantial service sector
  - Most **new employment** is provided by services
  - Strongest **growth area** for marketing
- Understanding services offers you a personal competitive advantage

## Services Dominate the Global Economy

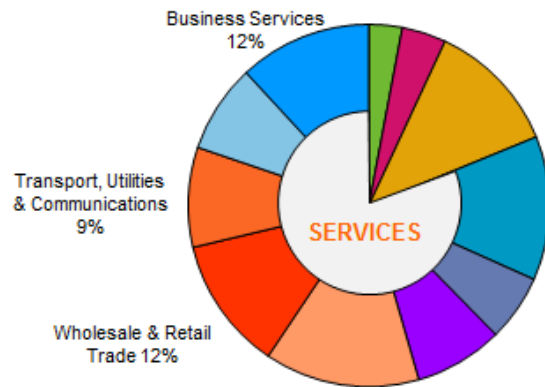
### Contribution of Service Industries to GDP Globally



## Estimated Size of Service Sector in Selected Countries



## Value Added by Service Industry Categories to US GDP



## NAICS: New Way to Classify & Analyze the Service Economy

- **NAICS – North American Industry Classification System**
  - Classifies industries in the economic statistic of USA, Canada and Mexico
  - Replaces of SIC codes in USA
  - Captures huge array of new service industries, each with its own NAICS code
- **NAPCS – North American Product Classification System**
  - Assigns codes to thousands of service products
  - Particularly useful for looking at rented goods and services

## NAICS Codes of Newer Service Industries Not Profiled by SIC

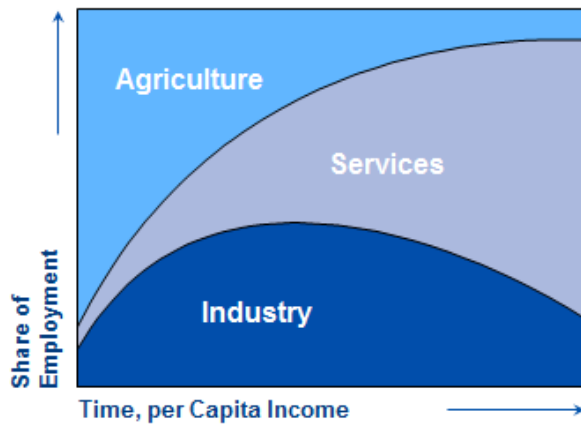
- Casino hotels
- Continuing Care Retirement Communities
- Diagnostic Imaging Centers
- Diet and Weight Reducing Centers
- Environmental Consulting
- Golf courses and Country Clubs
- Hazardous Waste Collection
- HMO Medical Centers
- Industrial Design Services
- Investment Banking and Securities Dealing
- Management Consulting Services
- Satellite Telecommunications
- Telemarketing Bureaus
- Temporary Help Services

## Why Study Services?

- Most new jobs are generated by services
  - Fastest growth expected in **knowledge-based** industries
  - Significant training and educational qualifications required, but employees will be **more highly compensated**

- Will service jobs be lost to lower-cost countries? Yes, some **service jobs can be exported**

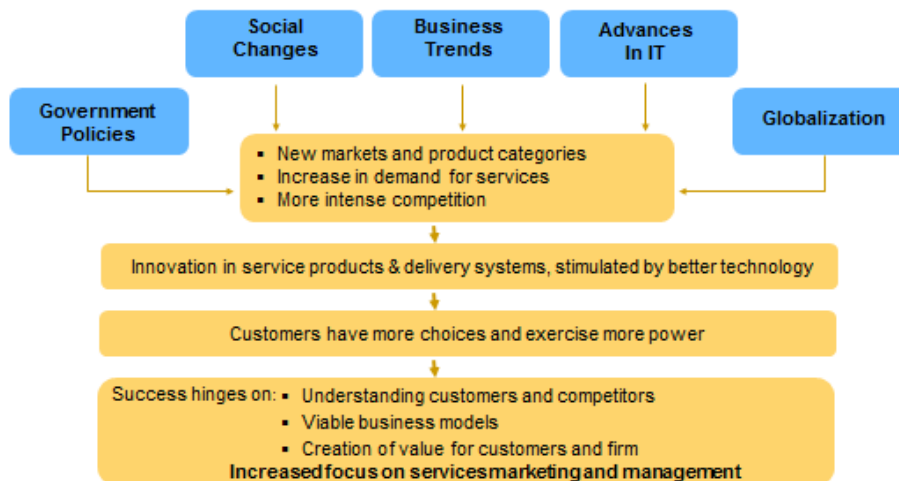
### Changing Structure of Employment as Economies Develop



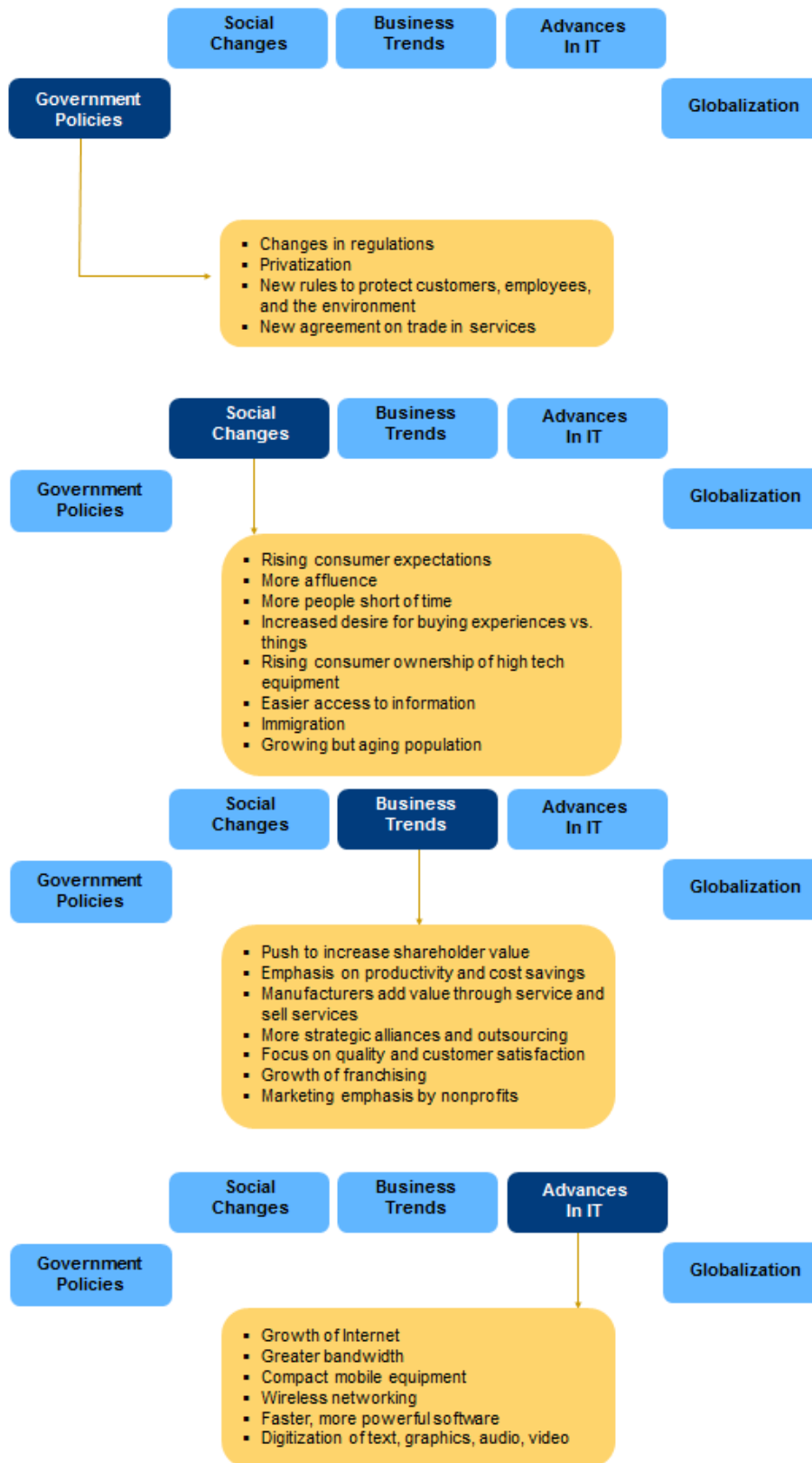
### Why Study Services?

- Powerful forces are **transforming** service markets
  - Government policies, social changes, business trends, advances in IT, internationalization
- Forces that reshape:
  - Demand
  - Supply
  - The competitive landscape
  - Customers' choices, power, and decision making

### Transformation of the Service Economy



## Factors Stimulating Transformation of the Service Economy





## What are Services?

- **The historical view**
  - Smith (1776): Services are different from goods because they are **perishable**
  - Say (1803): As services are **immaterial**, consumption **cannot be separated** from production
- **A fresh perspective: Benefits without Ownership**
  - Rental of goods:
    - a) *Payment made for using or accessing something – usually for a defined period of time – instead of buying it outright and*
    - b) *Allows participation in network systems that individuals and organizations could not afford*

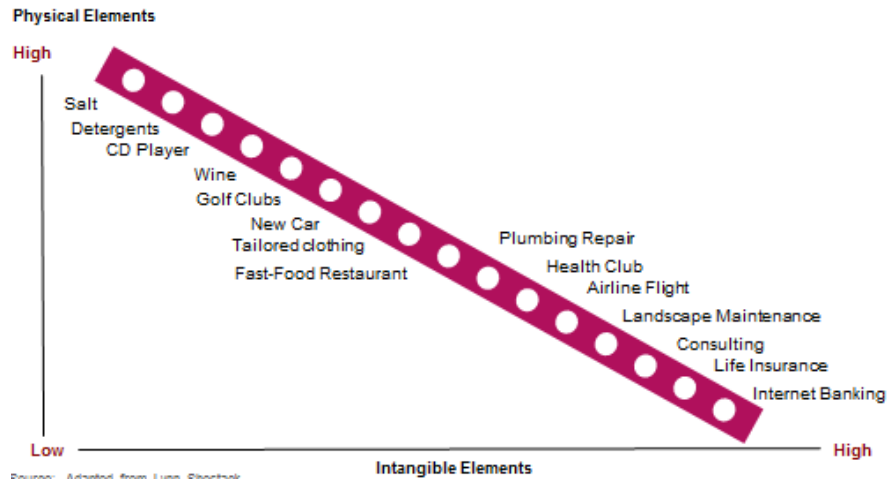
### Five broad categories within non-ownership framework of which two or more may be combined



## Definition of Services

- **Services**
  - Are **economic activities** offered by one party to another
  - Most commonly employ **time-based performances** to bring about desired results
- **In exchange for their money, time, and effort, service customers expect to obtain value from**
  - Access to goods, labor, facilities, environments, professional skills, networks, and systems;
  - Normally **do not take ownership** of any of the physical elements involved

## Value Creation is dominated by Intangible Elements



## Service Products vs. Customer Service & After-Sales Service

- A firm's market offerings are divided into core product elements and supplementary service elements
- Need to distinguish between:
  - Marketing **of** services – when service is the core product
  - Marketing **through** service – when good service increases the value of a core physical good
- Manufacturing firms are reformulating and enhancing existing added-value services to market them as stand-alone core products

## Service – A Process Perspective

- Differences exist amongst services depending on what is being processed
- Classification of services into
  - People processing
  - Possession processing
  - Mental stimulus processing
  - Information processing

## 4 Categories of Services

Nature of the Service Act	Who or What is the Direct Recipient of the Service?	
	People	Possessions
Tangible Actions	<b>People-processing</b> (services directed at people's bodies): <ul style="list-style-type: none"> <li>• Barbers</li> <li>• Health care</li> </ul>	<b>Possession-processing</b> (services directed at physical possessions): <ul style="list-style-type: none"> <li>• Refueling</li> <li>• Disposal / recycling</li> </ul>
Intangible Actions	<b>Mental stimulus processing</b> (services directed at people's mind): <ul style="list-style-type: none"> <li>• Education</li> <li>• Advertising / PR</li> </ul>	<b>Information processing</b> (services directed at intangible assets): <ul style="list-style-type: none"> <li>• Accounting</li> <li>• Banking</li> </ul>

### *People Processing*

- Customers must:
  - Physically enter the service factory
  - Cooperate actively with the service operation
- Managers should think about process and output from the **customer's perspective**
  - To identify benefits created and non-financial costs: Time, mental and physical effort

### *Possession Processing*

- Involvement is limited
- Less physical involvement
- Production and consumption are **separable**

### *Mental Stimulus Processing*

- Ethical standards required:
  - Customers might be manipulated
- Physical presence of recipients not required
- Core content of services is **information-based**
  - Can be 'inventoried'

### *Information Processing*

- Most **intangible form** of service
- May be transformed:
  - Into enduring forms of service output
- Line between information processing and mental stimulus processing may be unclear

## **Marketing Challenges Posed by Services**

### **Services Pose Distinctive Marketing Challenges**

- Marketing management tasks in the service sector differ from those in the manufacturing sector
- Eight common differences between services and goods but they do not apply equally to all services

***What are marketing implications of these differences?***

## Differences, Implications, and Marketing-Related Tasks

Difference	Implications	Marketing-Related Tasks
<ul style="list-style-type: none"> <li>Most service products cannot be inventoried</li> <li>Intangible elements usually dominate value creation</li> <li>Services are often difficult to visualize &amp; understand</li> <li>Customers may be involved in co-production</li> </ul>	<ul style="list-style-type: none"> <li>Customers may be turned away</li> <li>Harder to evaluate service &amp; distinguish from competitors</li> <li>Greater risk &amp; uncertainty perceived</li> <li>Interaction between customer &amp; provider; poor task execution could affect satisfaction</li> </ul>	<ul style="list-style-type: none"> <li>Use pricing, promotion, reservations to smooth demand; work with ops to manage capacity</li> <li>Emphasize physical clues, employ metaphors and vivid images in advertising</li> <li>Educate customers on making good choices; offer guarantees</li> <li>Develop user-friendly equipment, facilities &amp; systems; train customers, provide good support</li> </ul>

Difference	Implications	Marketing-Related Tasks
<ul style="list-style-type: none"> <li>People may be part of service experience</li> <li>Operational inputs and outputs tend to vary more widely</li> <li>Time factor often assumes great importance</li> <li>Distribution may take place through nonphysical channels</li> </ul>	<ul style="list-style-type: none"> <li>Behavior of service personnel &amp; customers can affect satisfaction</li> <li>Hard to maintain quality, consistency, reliability</li> <li>Difficult to shield customers from failures</li> <li>Time is money; customers want service at convenient times</li> <li>Electronic channels or voice communications</li> </ul>	<ul style="list-style-type: none"> <li>Recruit, train employees to reinforce service concept</li> <li>Shape customer behavior</li> <li>Redesign for simplicity and failure proofing</li> <li>Institute good service recovery procedures</li> <li>Find ways to compete on speed of delivery; offer extended hours</li> <li>Create user-friendly, secure websites and free access by telephone</li> </ul>

## Extended Marketing Mix for Services

### Services Require and Extended Marketing Mix

- Marketing can be viewed as:
  - A strategic and competitive thrust pursued by top management
  - A set of functional activities performed by line managers
  - A customer-driven orientation for the entire organization
- Marketing is **only function** to bring operating revenues into a business; all other functions are cost centers
- The “7Ps” of services marketing are needed to create viable **strategies for meeting customer needs profitably**

### The 7Ps of Services Marketing

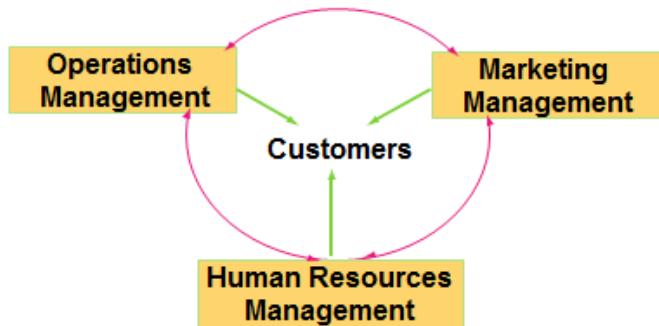
- Traditional Marketing Mix Applied to Services
  - Product (Ch4)
  - Place and Time (Ch5)
  - Price (Ch6)

- Promotion and Education (Ch7)
- Extended Marketing Mix for Services
  - Process (Ch8 & 9)
  - Physical Environment (Ch10)
  - People (Ch11)

## Integration of Marketing with Other Management Functions

Marketing to be integrated with Other Management Functions

**Three management functions play central and interrelated roles in meeting needs of service customers**



## Developing Effective Service Marketing Strategies

Overview of Framework



***Understanding Service Products, Consumers, and Markets***

- Chapter 1 New Perspectives on Marketing in the Service Economy
- Chapter 2 Consumer Behavior in a Services Context
- Chapter 3 Positioning Services in Competitive Markets

***Applying the 4 P's of Marketing to Services***

- Chapter 4 Developing Service Products: Core and Supplementary Elements
- Chapter 5 Distributing Services through Physical and Electronic Channels
- Chapter 6 Setting Prices and Implementing Revenue Management
- Chapter 7 Promoting Services and Educating Customers

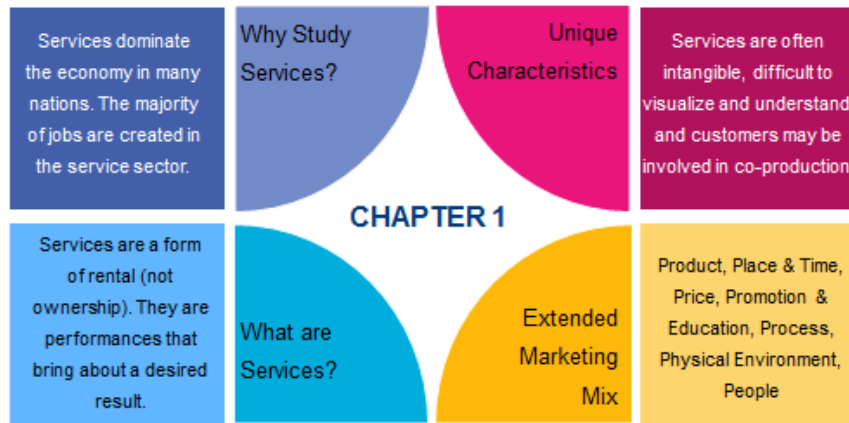
***The Extended Services Marketing Mix for Managing the Customer Interface***

- Chapter 8 Designing and Managing Service Processes
- Chapter 9 Balancing Demand and Productive Capacity
- Chapter 10 Crafting the Service Environment
- Chapter 11 Managing People for Service Advantage

***Implementing Profitable Service Strategies***

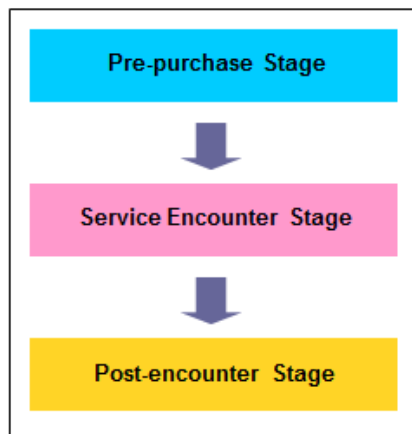
- Chapter 12 Managing Relationships and Building Loyalty
- Chapter 13 Complaint Handling and Service Recovery
- Chapter 14 Improving Service Quality and Productivity
- Chapter 15 Striving for Service Leadership

## Summary



## Chapter 2: Consumer Behavior in a Service Context

### Customer Decision Making: The Three-Stage Model of Service Consumption



#### Pre-Purchase Stage

- Customers seek solutions to aroused needs
- Evaluating a service may be difficult
- Uncertainty about outcomes increases perceived risk
- What risk reduction strategies can service suppliers develop?
- Understanding customers' service expectations
- Components of customer expectations
- Making a service purchase decision

#### Need Arousal

- Decision to buy or use a service is triggered by **need arousal**
- Triggers of need:
  - Unconscious minds (e.g., personal identity and aspirations)
  - Physical conditions (e.g., hunger)

- External sources
- Consumers are then motivated to find a solution for their need

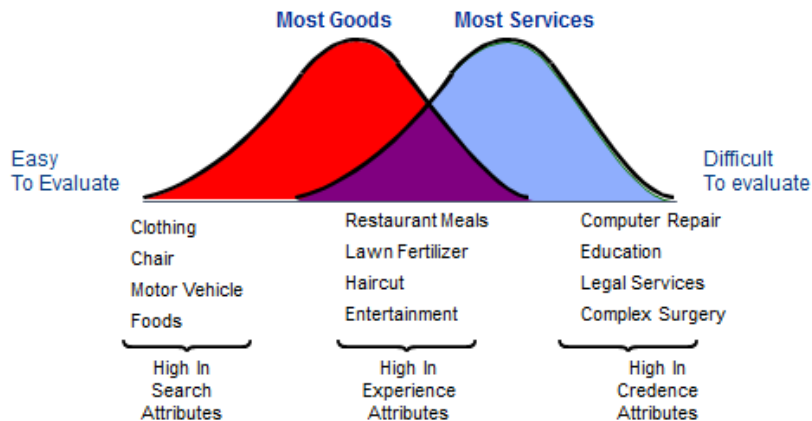
### Information Search

- Need arousal leads to attempts to find a solution
- **Evoked set** – a set of products and brands that a consumer considers during the decision-making process – that is derive from past experiences or external sources
- Alternatives then **need to be evaluated** before a final decision is made

### Evaluating Alternatives – Service Attributes

- Search attributes help customers evaluate a product before purchase
  - E.g., type of food, location, type of restaurant and price
- Experience attributes cannot be evaluated before purchase
  - The consumer will not know how much s/he will enjoy the food, the service, and the atmosphere until the actual experience
- Credence attributes are those that customers find impossible to evaluate confidently even after purchase and consumption
  - E.g., hygiene conditions of the kitchen and the healthiness of the cooking ingredients

### How Product Attributes Affect Ease of Evaluation



### Perceived Risks of Purchasing and Using Services

- **Functional** – unsatisfactory performance outcomes
- **Financial** – monetary loss, unexpected extra costs
- **Temporal** – wasted time, delays leading to problems
- **Physical** – personal injury, damage to possessions
- **Psychological** – fears and negative emotions
- **Social** – how others may think and react
- **Sensory** – unwanted impact on any of five senses

### How Might Consumers Handle Perceived Risk?

- Seek information from respected personal sources
- Compare service offerings and search for independent reviews and ratings via the Internet

- Relying on a firm with food reputation
- Looking for guarantees and warranties
- Visiting service facilities or going for trials before purchase and examining tangible cues or other physical evidence
- Asking knowledgeable employees about competing services

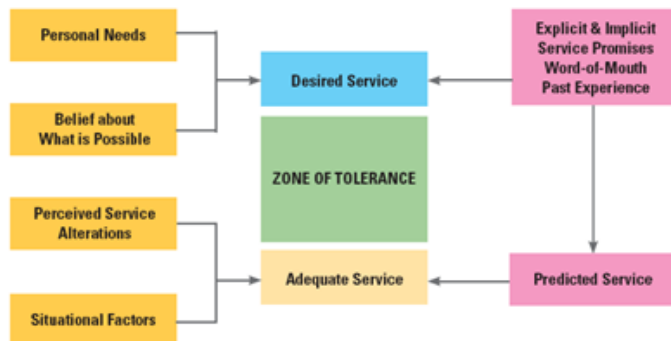
### Strategic Responses to Managing Customer Perceptions of Risk



### Understanding Customers' Service Expectations

- Customers evaluate service quality by **comparing** what they expect against what they perceive
  - Situational and personal factors also considered
- Expectations of good service vary from one business to another, and differently positioned service providers in same industry
- Expectations change over time

### Factors Influencing Customer Expectations of Service



### Components of Customer Expectations

- **Desired Service Level**
  - Wished-for level of service quality that customer believes can and should be delivered
- **Adequate Service Level**
  - Minimum acceptable level of service
- **Predicted Service Level**

- Service level that customer believes firm will actually deliver
- **Zone of Tolerance**
  - Acceptable range of variations in service delivery

### *Purchase Decision*

- **Purchase Decision:** possible alternatives are compared and evaluated, whereby the best option is selected
  - Simple if perceived risks are low and alternatives are clear
  - Complex when trade-offs increase
- Trade-offs are often involved
- After making a decision, the consumer moves into the service encounter stage

### *Service Encounter Stage*

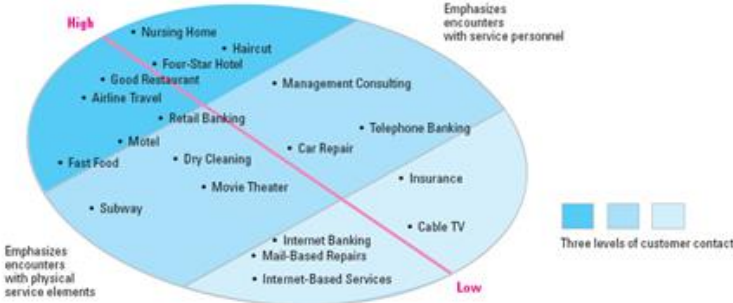
- Service encounters range from high-to-low contact
- Understanding the servuction system
- Theater as a metaphor for service delivery: An integrative perspective
  - Service facilities
  - Personnel
  - Role and script theories
- **Service encounter** – a period of time during which a customer interacts directly with the service provider
  - might be brief or extend over a period of time (e.g., a phone call or visit to the hospital)
- Models and frameworks:
  1. “Moments of Truth” – importance of managing touch points
  2. High/low contact model – extent and nature of contact points
  3. Servuction model – variations of interactions
  4. Theater metaphor – “staging” service performances

### *Moments of Truth*

“[W]e could say that the perceived quality is realized at the moment of truth, when the service provider and the service customer confront one another in the arena. At that moment they are very much on their own... It is the skill, the motivation, and the tools employed by the firm’s representative and the expectations and behavior of the client which together will create the service delivery process.”

**Richard Normann**

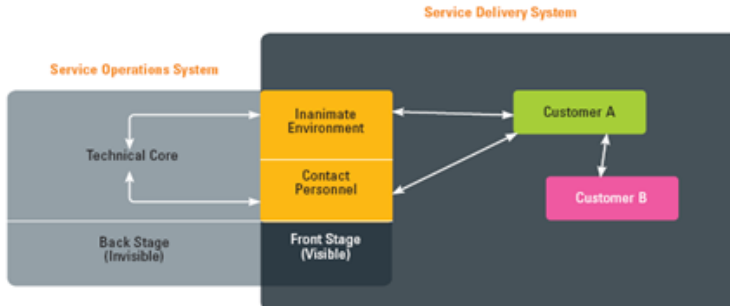
## Service Encounters Range from High-Contact to Low-Contact



## Distinctions between High-Contact and Low-Contact Services

- High-Contact Services
  - Customers visit service facility and remain throughout service delivery
  - Active contact
  - Includes most people-processing service
- Low-Contact Services
  - Little or no physical contact
  - Contact usually at arm's length through electronic or physical distribution channels
  - Facilitated by new technologies

## The Servuction System



## The Servuction System: Service Production and Delivery

- **Servuction System:** visible front stage and invisible backstage
- **Service Operations**
  - Technical core where inputs are processed and service elements created
  - Contact people
  - Inanimate environment
- **Service Delivery**
  - Where “final assembly” of service elements takes place and service is delivered
  - Includes customer interactions with operations and other customers

## *Theater as a Metaphor for Service Delivery*

"All the world's a stage and all the men  
and women merely players. They have  
their exits and their entrances and each  
man in his time plays many parts."

William Shakespeare  
As You Like It

Theatrical Metaphor: an Integrative Perspective

**Good metaphor as service delivery is a series of events that customers experience as a performance**



## *Implications of Customer Participation in Service Delivery*

- Greater need for information/training
  - Help customers to perform well, get desired results
- Customer should be given a **realistic service preview** in advance of service delivery
  - This allows them to have a clear idea of their expected role and their script in this whole experience
  - Manages expectations and emotions

## *Post-Encounter Stage*

- Evaluation of service performance
- Future intentions

## *Customer Satisfaction with Service Experience*

- **Satisfaction: attitude-like judgment** following a service purchase or series of service interactions
  - Whereby customers have expectations prior to consumption, observe service performance, compare it to expectations
- Satisfaction judgments are based on this comparison
  - Positive disconfirmation (better)
  - Confirmation (same)

- Negative disconfirmation (worse)

### *Customer Delight: Going beyond Satisfaction*

- Research shows that delight is a function of three components
  - Unexpectedly high levels of performance
  - Arousal (e.g., surprise, excitement)
  - Positive affect (e.g., pleasure, joy, or happiness)
- Strategic links exist between customer satisfaction and corporate performance
  - By creating more value for customers (increased satisfaction), the firm creates more value for the owners

**BEST PRACTICE IN ACTION 2.1**

**Progressive Insurance Delights Its Customers**

Progressive Insurance Corp. prides itself on providing extraordinary customer service—and its accomplishments in the area of claims processing are particularly impressive. To lower its costs and simultaneously improve customer satisfaction and retention, the company introduced its Immediate Response service, offering customers 24/7 access to claims handling. Adjusters work out of mobile claims vans rather than offices, and Progressive has a target of nine hours for an adjuster to inspect a damaged vehicle. In many instances, claims representatives actually arrive at the scene of an accident while the evidence is still fresh.

Consider the following scenario. The crash site in Tampa, Florida, is chaotic and tense. Two cars are damaged and, although the passengers aren't bleeding, they are shaken up and scared. Lance Edgy, a senior claim representative for Progressive Corp., arrives on the scene just minutes after the collision. He calms the victims and advises them on medical care, repair shops, police reports, and legal procedures. Edgy invites William McAllister, Progressive's policyholder, into an air-conditioned van equipped with comfortable chairs, a desk, and two cell phones. Even before the tow trucks have cleared away the wreckage, Edgy is able to offer his client a settlement for the market value of his totaled Mercury. McAllister, who did not appear to have been at fault in this accident, later stated in amazement: "This is great—someone coming right out here and taking charge. I didn't expect it at all."

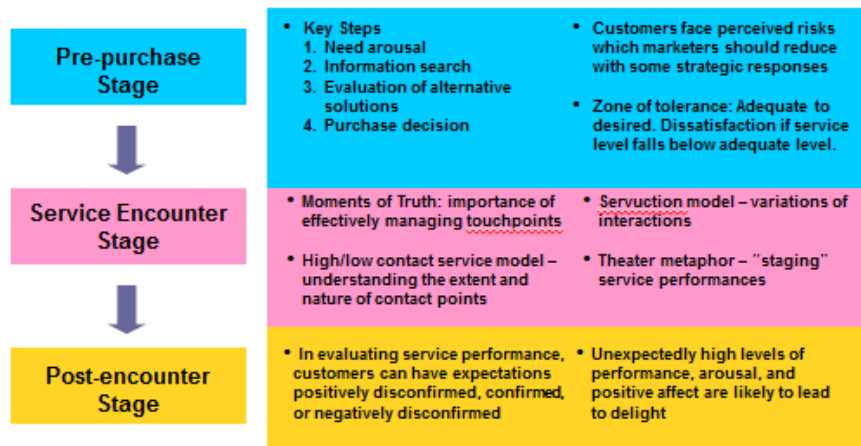
The shortened time cycle has advantages for Progressive, too. Costs are reduced, there's less likelihood that lawyers will become involved when settlement offers are made promptly, and it's easier to prevent fraud. Progressive continues to find new ways to delight its customers. Its website, [www.progressive.com](http://www.progressive.com), has been consistently rated as the top overall among internet-based insurance carriers by Gomez.com (an internet quality measurement firm), which places a priority on a site's educational, purchasing, and servicing capabilities. Progressive has also been cited for pleasantly surprising its customers with consumer-friendly innovations and extraordinary customer service.



Source: Ronald Hankoff, "Service Is Everybody's Business," *Fortune*, June 27, 1994, 50; Michael Hammer, "Deep Change: How Operational Innovation Can Transform Your Company," *Harvard Business Review* 82, April 2004, 84-95; [www.progressive.com](http://www.progressive.com), accessed December 12, 2005.

- Best Practice in Action 2.1: **Progressive Insurance** Delights Its Customers
  - Provided excellent customer service which allowed them to lower costs and also increase customer satisfaction and retention

## Summary



## Chapter 3: Developing Service Products – Core and Supplementary Elements

### Planning and Creating Service Products

#### Service Products

- A service product comprises of all elements of service performance, both tangible and intangible, that create value for customers
- Service products consist of:
  - **Core Product:** central component that supplies the principal, problem-solving benefits customers seek
  - **Supplementary Services:** augments the core product, facilitating its use and enhancing its value and appeal
  - **Delivery Processes:** used to deliver both the core product and each of the supplementary services

#### Designing a Service Concept

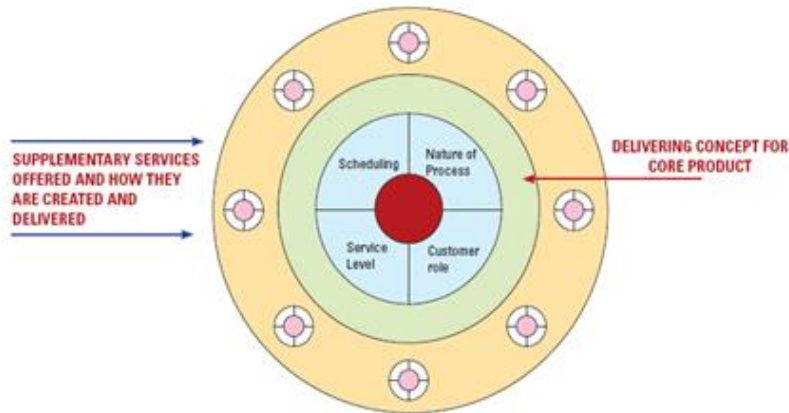
- Service concept design must address the following issues:
  - How the different service components are delivered to the customer
  - The nature of the customer’s role in those processes
  - How long delivery lasts
  - The recommended level and style of service to be offered

#### Documenting Delivery Sequence over Time

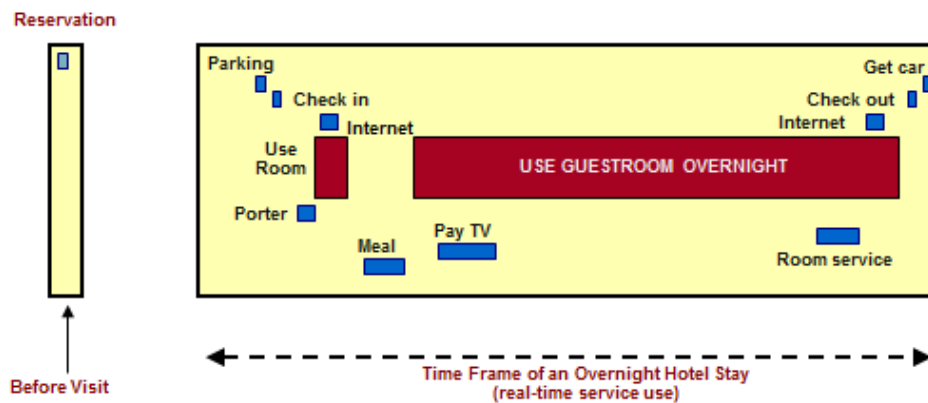
- Must address sequence in which customers will use each core and supplementary service
- Determine approximate length of time required for each step
- Information should reflect good understanding of customers, especially their:
  - Needs

- Habits
- Expectations

## Integration of Core Product, Supplementary Elements, and Delivery Process

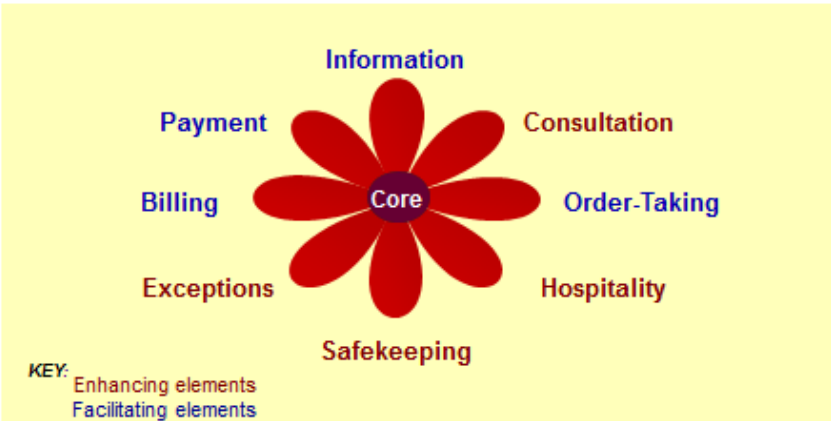


## Temporal Dimension to Augmented Product



## The Flower of Service

- There are two types of supplementary services
  - Facilitating: either needed for service delivery, or help in the use of the core product
  - Enhancing: add extra value for the customer
- In a well-managed service organization, the petals and core are fresh and well-formed
- Market positioning strategy helps to determine which supplementary services should be included



### Facilitating Services – Information

- Directions to service site
- Schedules/service hours
- Prices
- Reminders
- Warnings
- Conditions of sale/service
- Notification of changes
- Documentation
- Confirmation of reservations
- Summaries of account activities
- Receipts and tickets

### Facilitating Service – Order-Taking

#### Applications

- Memberships in clubs/programs
- Subscription services (e.g., utilities)
- Prerequisite based services (e.g., financial credit, college enrollment)

#### Order Entry

- On-site order fulfillment
- Mail/telephone/e-mail/web order

#### Reservations and Check-in

- Seats/tables/rooms
- Vehicles or equipment rental
- Professional appointments

### **Facilitating Services – Billing**

- Periodic statements of account activity
- Invoices for individual transactions
- Verbal statements of amount due
- Self-billing (computed by customer)
- Machine display of amount due

### **Facilitating Services – Payment**

#### **Self-Service**

- Insert card, cash or token into machine
- Electronic funds transfer
- Mail a check
- Enter credit card number online

#### **Direct to Payee or intermediary**

- Cash handling or change giving
- Check handling
- Credit/charge/debit card handling
- Coupon redemption

#### **Automatic Deduction from Financial Deposits**

- Automated systems (e.g., machine-readable tickets that operate entry gate)
- Human system (e.g., toll collectors)

### **Enhancing Services – Consultation**

- Customized advice
- Personal counseling
- Tutoring/training in product use
- Management or technical consulting

### **Enhancing Services – Hospitality**

- Greeting
- Food and beverages
- Toilets and washrooms
- Waiting facilities and amenities
- Lounges, waiting areas, seating
- Weather protection
- Magazines, entertainment, newspapers
- Transport
- Security

## Enhancing Services – Safekeeping

### Caring for Possessions Customer Bring with them

- Child care, pet care
- Parking for vehicles, valet parking
- Coat rooms
- Baggage handling
- Storage space
- Safe deposit boxes
- Security personnel

### Caring for Goods Purchased (or Rented) by Customers

- Packaging
- Pickup
- Transportation and delivery
- Installation
- Inspection and diagnosis
- Cleaning
- Refueling
- Preventive maintenance
- Repair and renovation

## Enhancing Services – Exceptions

### Special Requests in Advance of Service Delivery

- Children’s needs
- Dietary requirements
- Medical or disability needs
- Religious observances

### Handling Special Communications

- Complaints
- Compliments
- Suggestions

### Problem Solving

- Warranties and guarantees
- Resolving difficulties that arise from using the product
- Resolving difficulties caused by accidents, service failures
- Assisting customers who have suffered an accident or a medical emergency

## Restitution

- Refunds and compensation
- Free repair of defective goods

## Managerial Implications

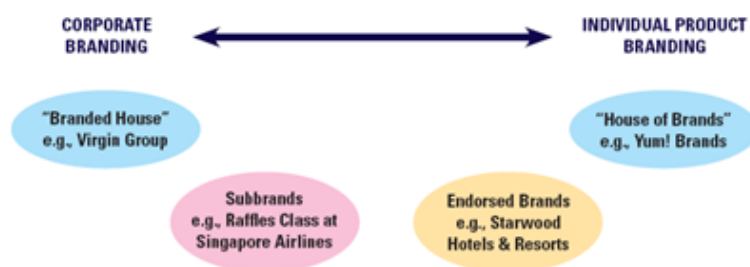
- Core products do not have to have supplementary elements
- Nature of product helps determine supplementary services offered to enhance value
- People-processing and high contact services have more supplementary services
- Different levels of service can add extra supplementary services for each upgrade in service level
- Low-cost, no-frills basis firms needs fewer supplementary elements

## Branding Service Products and Experiences

### Service Products, Product Lines, and Brands

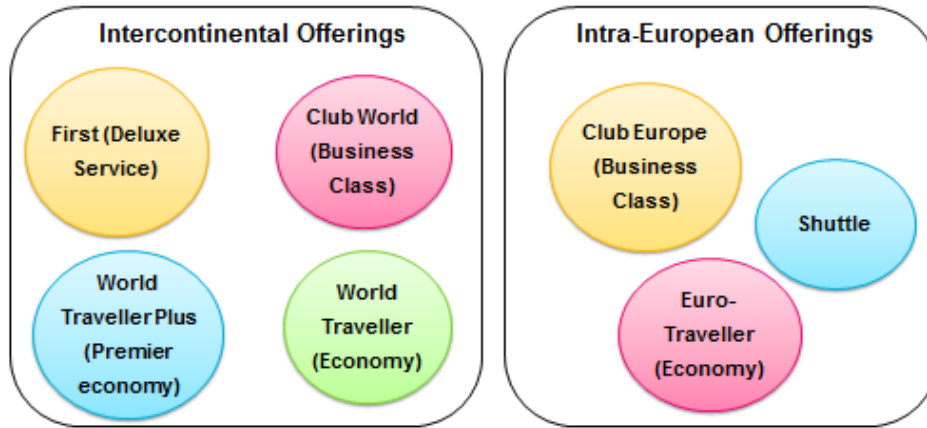
- **Service Product:** a defined and consistent “**bundle of output**”
  - Supported by supplementary services (assembly of elements that are built around the core product)
  - Differentiated by bundle of output
- **Product Line:** most service organizations offer a **line of products** rather than just a single product
- There are three broad alternatives for product lines:
  - Single brand to cover all products and services
  - A separate, stand-alone brand for each offering
  - Some combination of these two extremes

### Spectrum of Branding Alternatives



### Example: British Airways Sub brands

British Airways offers seven distinct air travel products



### Offering a Branded Experience

Branding can be employed at corporate and product levels

- Corporate brand:
  - Easily recognized,
  - Holds meaning to customers,
  - Stands for a particular way of doing business
- Product brand:
  - Helps firm communicate **distinctive experiences** and benefits associated with a **specific service concept**

### Moving Towards a Branded Experience



## Offering a Branded Experience

"The brand promise or value proposition is not a tag line, an icon, or a color or a graphic element, although all of these may contribute.

It is, instead, **the heart and soul of the brand.**"

Don Schultz

## New Service Development

### A Hierarchy of New Service Categories



### Reengineering Service Processes

- Service processes affect customers and also cost, speed, and productivity
- Reengineering – analyzing and redesigning processes to achieve faster and better performance
- Examination of processes can lead to creation of alternative delivery methods:
  - Add or eliminate supplementary services
  - Re-sequence delivery of service elements
  - Offer self-service options

### Physical Goods as a Source of New Service Ideas

- Goods and services may become competitive substitutes if they offer the same key benefits
- Provides an alternative to owning the physical good that can attain the desired outcome
- Any new good may create need for after-sales services now and be a source of future revenue stream

## Creating Services as Substitutes for Physical Good

	Own a Physical Good	Rent Use of Physical Good
Perform Work Oneself	<ul style="list-style-type: none"><li>▪ Drive Own Car</li><li>▪ Use Own Computer</li></ul>	<ul style="list-style-type: none"><li>▪ Rent a Car and Drive it</li><li>▪ Rent Use of Computer</li></ul>
Hire Someone to Do Work	<ul style="list-style-type: none"><li>▪ Hire a Chauffeur to Drive</li><li>▪ Hire a Typist to Type</li></ul>	<ul style="list-style-type: none"><li>▪ Hire a Taxi or Limousine</li><li>▪ Send Workout to a Secretarial Service</li></ul>

## Achieving Success in Developing New Services

- Services are not immune to high failure rates that plague new manufactured products
- In developing new services:
  - Core product is often secondary importance, many innovations are in supplementary services or service delivery
  - Ability to maintain quality of the total service offering is key
  - Accompanying marketing support activities are vital
  - Market knowledge is of utmost importance

## Success Factors in New Service Development

- Market synergy
  - Good fit between new product and firm's image
  - Advantage in meeting customers' needs
  - Strong support from firm during and after launch
  - Understands customer purchase decision behavior
- Organizational factors
  - Strong inter-functional cooperation and coordination
  - Internal marketing to educate staff on new product and its importance
- Market research factors
  - Scientific studies conducted early in development process
  - Product concept well defined before undertaking field studies

## Summary

- Creating services involve:
  - Designing the core product, supplementary services, and their delivery processes
- Flower of service includes **core products** and two types of supplementary services: facilitating and enhancing
  - **Facilitating services** include information, order taking, billing, and payment
  - **Enhancing services** include consultation, hospitality, safekeeping, and exceptions

## Chapter 7: Positioning Services in Competitive Markets

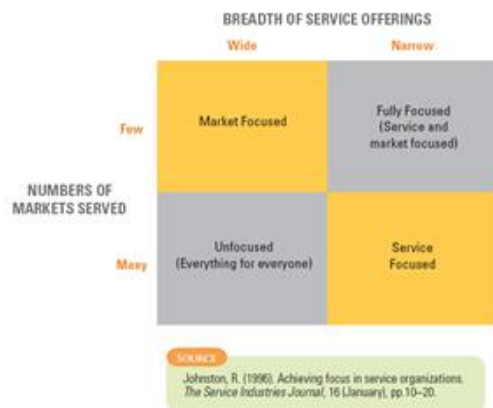
### Focused Strategies for Services

#### Standing Apart from the Competition

“A business must set itself apart from its competition. To be successful it must identify and promote itself as the best provider of attributes that are important to target customers.”

George S. Day

#### Basic Focus Strategies for Services



#### Considerations for using Focused Strategies

Fully focused: Limited range of services to narrow and specific market

- Opportunities
  - Developing recognized expertise in a well-defined niche may provide protection against would-be competitors
  - Allows firms to charge premium prices
- Risks
  - Market is too small to generate needed volume
  - Demand may be displaced by generic competition from alternative products
  - Purchasers in chosen segment may be susceptible to economic downturn
- Market focused
  - Narrow market segment with wide range of services
  - Need to make sure firms have operational capability to do and deliver each of the different services selected
  - Need to understand customer purchasing practices and preferences
- Service focused
  - Narrow range of services to fairly broad market

- As new segments are added, firm needs to develop knowledge and skills in serving each segment
- Unfocused
  - Broad markets with wide range of services
  - Many service providers fall into this category
  - Danger – becoming a “jack of all trades and master of none”

## Market Segmentation

- Firms vary widely in their abilities to serve different types of customers
- A market segment is composed of a group of buyers sharing common characteristics, needs, purchasing, behavior, and consumption patterns
- Target segments should be selected with reference to
  - Firm’s ability to match or exceed competing offerings directed at the same segment
  - Not just profit potential

## Service Attributes and Levels

### Developing Right Service Concept for a Specific Segment

- Use research to identify and prioritize which attributes of a given service are important to specific market segments
- Individuals may set different priorities according to:
  - Purpose of using the service
  - Who makes decision
  - Timing of use
  - Whether service is used alone or with a group
  - Composition of that group

### Important vs. Determinant Attributes

- Consumers usually choose between alternative service offerings based on perceived differences between them
- Attributes that distinguish competing services from one another are not necessarily the most important ones
- Determinant attributes determine buyers’ choices between competing alternatives
  - Service characteristics that are important to purchases
  - Customers see significant differences between competing alternatives on these attributes

### Establishing Service Levels

- Make decisions on service levels – level of performance firm plans to offer on each attribute
  - Easily quantified attributes are easier to understand – e.g., vehicle speed, physical dimensions
  - Qualitative attributes subject to individual interpretation – e.g., physical comfort, noise levels

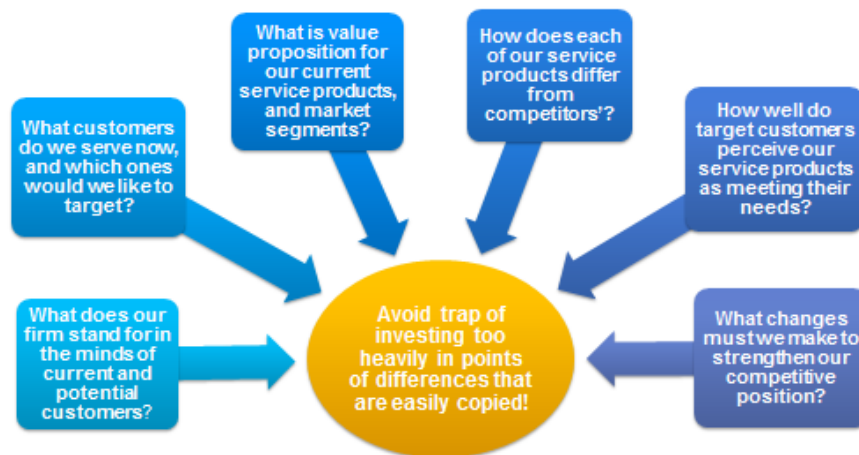
- Can often segment customers according to willingness to trade off price versus service level:
  - Price-insensitive customers willing to pay relatively high price for high levels of service
  - Price-sensitive customers look for inexpensive service with relatively low performance

## Positioning Distinguishes a Brand from its Competitors

### Four Principles of Positioning Strategy

- Must establish position for firm or product in minds of customers
- Position should be distinctive, providing one simple, consistent message
- Position must set firm/product apart from competitors
- A company cannot be all things to all people – must focus its efforts

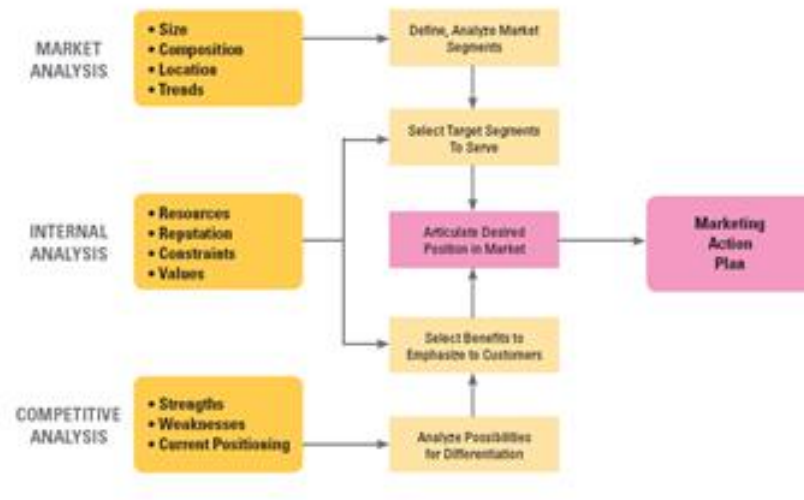
### Principles of Positioning



### Developing an Effective Positioning Strategy

- Positioning links market analysis and competitive analysis to internal corporate analysis
- Market Analysis
  - Focus on overall level and trend of demand and geographic locations of demand
  - Look into size and potential of different market segments
  - Understand customer needs and preferences and how they perceive the competition
- Internal Corporate Analysis
  - Identify organization's resources, limitations, goals, and values
  - Select limited number of target segments to serve
- Competitor Analysis
  - Understand competitors' strengths and weaknesses
  - Anticipate responses to potential positioning strategies

## Market, Internal, and Competitive Analyses



### Anticipating Competitive Response

- Competitors might pursue same market position
  - Independently do same positioning analysis and arrive at similar conclusions
  - Threatened by new strategy, take steps to reposition own service
  - New entrants plays “follow the leader”
- Conduct internal corporate analysis for challengers and analyze possible effects of alternative moves
  - Impact of price cut on demand, market share, and profits
  - Responses of different segments to changes in service attributes

### Using Positioning Maps to Analyze Competitive Strategy

#### Using Positioning Maps to Plot Competitive Strategy

- Great tool to visualize competitive positioning and map developments of time
- Useful way to represent consumers perceptions of alternative products graphically
- Typically confined to two attributes, but 3-D models can be used to portray positions on three attributes simultaneously
- Information about a product can be obtained from market data, derived from ratings by representative consumers, or both

### Positioning of Hotels in Belleville: Price vs. Service Level



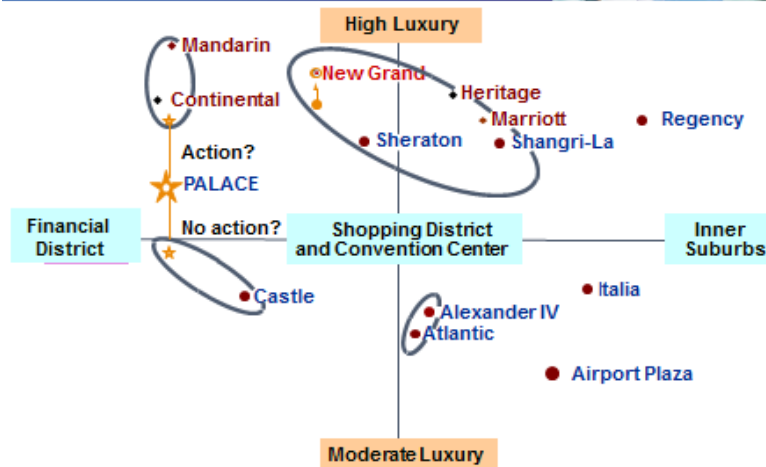
### Positioning of Hotels in Belleville: Location vs. Physical Luxury



### Positioning After New Construction: Price vs. Service Level



## Positioning After New Construction: Location vs. Physical Luxury



### Positioning Maps Help Managers to Visualize Strategy

- Research provides input to development of positioning maps – challenge is to ensure that
  - Attributes employed in maps are important to target segments
  - Performance of individual firms on each attribute accurately reflects perceptions of customer in target segments
- Predictions can be made of how positions may change in light of future developments
- Charts and maps can facilitate “visual awakening” to threats and opportunities, suggest alternative strategic directions

## Changing Competitive Positioning

### Repositioning

- Firm may have to make significant change in existing position
  - Revising service characteristics; redefining target market segments; abandoning certain products; withdrawing from certain market segments
- Improving negative brand perceptions may require extensive **redesign** of core product
- Repositioning introduces new dimensions into positioning equation that other firms cannot immediately match

### Summary

- Focus strategies:
  - Fully focused
  - Service focused
  - Market focused
  - Unfocused
- Market Segmentation – buyers share common characteristics, needs, purchasing behavior & consumption patterns
- Service attributes – determinant attributes are often the ones most important to customers
- Positioning links:

- Market Analysis
- Internal Analysis
- Competitive Analysis
- Positioning maps are useful for plotting competitive strategy:
  - Identify potential competitive responses
  - Help executives to visualize strategy

## Chapter 5: Distributing Services through Physical and Electronic Channels

### Distribution in a Services Context

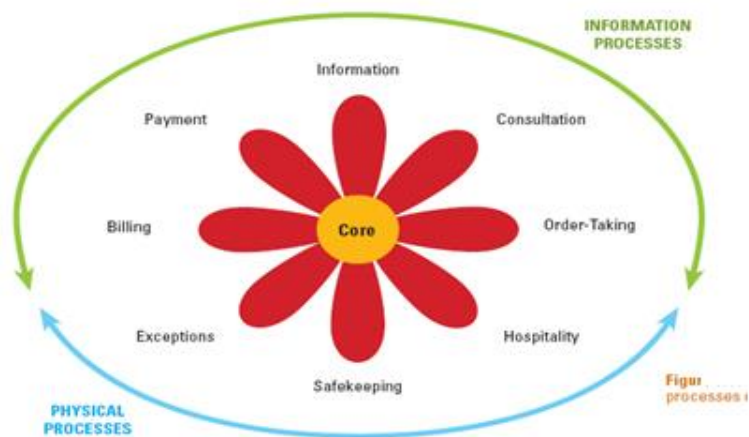
The three interrelated elements of distribution are:

- Information and promotion flow
  - To get customer interested in buying the service
- Negotiation flow
  - To sell the right to use a service
- Product flow
  - To develop a network of local sites

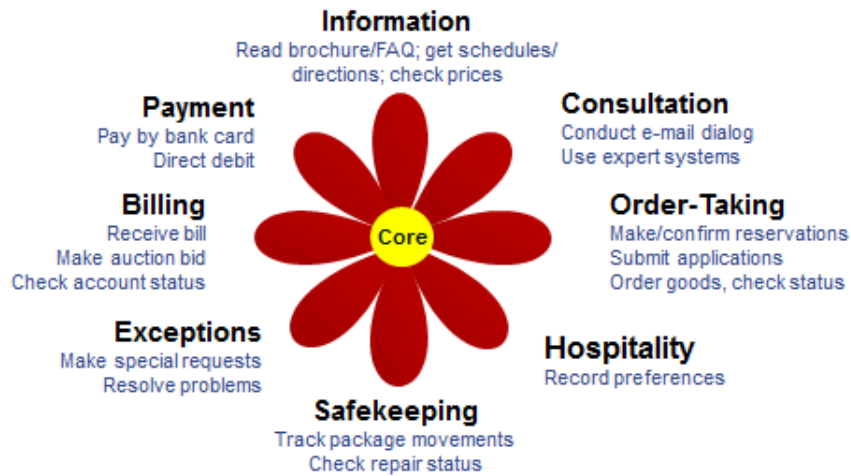
### Distinguishing between Distribution of Supplementary and Core Services

- Most core services require physical locations
- Many supplementary services are informational; can be distributed widely and cost-effectively via other means
  - Telephone
  - Internet

### Information and Physical Processes of Augmented Service Products



## Using Websites for Service Delivery



## Options for Service Delivery

### Distribution Options for Serving Customers

- Customers visit service site
  - Convenience of service factory locations and operational schedules important when customer has to be physically present
- Service providers go to customers
  - Unavoidable when object of service is immovable
  - More expensive and time-consuming for service provider
- Service transaction is conducted remotely
  - Achieved with help of logistics and telecommunications

### Six Options for Service Delivery

Type of Interaction between Customer and Service Organization	Availability of Service Outlets	
	Single Site	Multiple Sites
Customer goes to service organization	Theater Hair salon	Bus service Fast-food chain
Service organization comes to customer	House painting Mobile car wash	Mail delivery Banking branch network
Customer and service organization transact remotely (mail or electronic communications)	Credit card company Local TV station	Broadcast network Telephone company

### Channel Preferences Vary Among Customers

- For complex and high-perceived risk services, people tend to rely on personal channels
- Individuals with greater confidence and knowledge about a service/channel tend to use impersonal and self-service channels
- Customers with social motives tend to use personal channels
- Convenience is a key driver of channel choice

## Place and Time Decisions

### Place Decisions of Service Delivery

- Cost, productivity, and access to labor are key determinants to locating a service facility
- Location constraints
  - Operational requirement (e.g., airports)
  - Geographic factor (e.g., ski resorts)
  - Need for economies of scale (e.g., hospitals)
- Ministores
  - Creating many small service factories to maximize geographic coverage
  - Separating front and back stages of operation
  - Purchasing space from another provider in complementary field
- Locating in Multipurpose Facilities
  - Proximity to where customers live or work
    - Service Stations
    - Service Perspectives 5.2

### Time of Service Delivery

- Traditionally, schedules were restricted
  - Service availability limited to daytime, 40-50 hours a week
- Today
  - For flexible, responsive service operations: 24/7 service, all around the world

## Delivering Services in Cyberspace

### Service Delivery Innovations Facilitated by Technology

- Technological Innovations
  - Development of “smart” mobile telephones and PDAs, and presence of WiFi
  - Voice-recognition technology
  - Websites
  - Smart cards
    - Store detailed information about customer
    - Act as electronic purse containing digital money
- Electronic channels can be offered together with physical channels, or replace physical channels

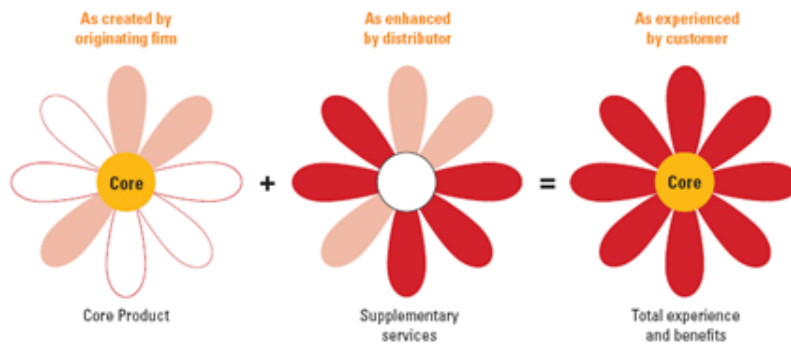
### E-Commerce: Move to Cyberspace

- What are the factors that encourage you to use virtual stores?
  - Convenience
  - Ease of search
  - Broader selection
  - Potential for better prices
  - 24-hour service with prompt delivery
- Recent developments: websites, customer management (CRM) systems, and mobile telephony

- Integrating mobile devices into the service delivery infrastructure can be used as means to:
  - Access services
  - Alert customers to opportunities/problems
  - Update information in real time

## Role of Intermediaries

### Splitting Responsibilities for Service Delivery



### Challenges for original supplier

- Act as guardian of overall process
- Ensure that each element offered by intermediaries fits overall service concept

## Franchising

- Franchisor provides training, equipment, and support marketing activities
- Franchisees invest time and finance, and follow copy and media guidelines of franchisor
- Advantages:
  - Expand delivery of effective service concept without a high level of monetary investment
  - Franchisees are motivated to ensure good customer service and high-quality service operations
- Disadvantages of franchising
  - Loss of control over delivery system and how customer experience actual service
  - Effective quality control is difficult
  - Conflict between franchisees may arise especially as they gain experience
- Alternative: license another supplier to act on the original supplier's behalf to deliver core product
  - Trucking companies
  - Banks selling insurance products

## Challenge of Distribution in Large Domestic Markets

- Distributing services (i.e., physical logistics) faces challenges due to:
  - Distances involved

- Multiple time zones
- Multiculturalism
- Differences in laws and tax rates

## Distributing Services Internationally

### Factors Favoring Adoption of Transnational Strategies

Transnational strategy involves integration of strategy formulation and its implementation across all countries in which company elects to do business

- Market Drivers
  - Common customer needs across countries
  - Corporate customers seek to standardize and simplify suppliers used in different countries – ad agencies, logistics suppliers, Big 4 accounting firms
- Government Drivers
  - Favorable trade policies, compatible technical standards, common marketing regulations
- Competition Drivers
  - Competitors from overseas, interdependence of countries
  - Firms may be obliged to follow competitors into new markets to protect own positions elsewhere
- Technology Drivers
  - Advances in information technology – miniaturization and mobility of equipment, digitization of voice
- Cost Drivers
  - Economies of scale
  - Lower operating costs

### How Service Processes Affect International Market Entry

- People processing services require direct contact with customers
  - Export service concept
    - Acting alone or in partnership with local suppliers
      - E.g., chain restaurants, hotels, car rental firms
  - Import customers
    - Inviting customers from overseas to firm's home country
      - E.g., hospitals catering to "medical tourism"
  - Transport customers to new locations
    - Passenger transportation (air, sea, rail, road)
- Possession processing involves services to customer's physical possessions
  - Repair and maintenance, freight transport
- Information-based services include mental processing services and information processing services
  - Export the service to a local service factory

- Hollywood film shown around the world
- Import customers
- Export the information via telecommunications and transform it locally
  - Data can be downloaded via CDs or DVDs

### Impact of Globalization Drivers on Various Service Categories

Globalization Drivers	People Processing	Possession Processing	Information Based
Competition	Simultaneity of production and consumption limits leverage of foreign competitive advantage, but management systems can be globalized.	Technology drives globalization of competitors with technical edge.	Highly vulnerable to global dominance by competitors with monopoly or competitive advantage in information.
Market	People differ economically and culturally, so needs for service and ability to pay may vary.	Level of economic development impacts demand for services to individually owned goods.	Demand for many services is derived to a significant degree from economic and educational levels.

Globalization Drivers	People Processing	Possession Processing	Information Based
Technology	Use of IT for delivery of supplementary services may be a function of ownership and familiarity with technology.	Need for technology-based service delivery systems depends on possessions requiring service and the cost trade-offs in labor substitution	Ability to deliver core services through remote terminals may be a function of investment in computerization, etc.
Cost	Variable labor rates may impact pricing in labor-sensitive services.	Variable labor rates may favor low-cost locations.	Major cost elements can be centralized and minor cost elements localized.
Government	Social policies (e.g., health) vary widely and may affect labor cost, etc.	Policies may decrease/increase cost and encourage/discourage certain activities	Policies may impact demand and supply and distort pricing

### Barriers to International Trade in Services

- Passage of free-trade legislation is important facilitator of transnational operations
  - Notable developments: NAFTA, Latin American economic blocs, EU
- Despite efforts of WTO and GATT, barriers still exist:
  - Restrictions on international airline operating rights
  - Heavy taxation
  - Legal restrictions
  - Lack of broadly agreed upon accounting standards
  - Cultural issues

## Summary

- Distribution relates to both core and supplementary services and embraces three interrelated elements
  - Information and promotion flow, negotiation flow, product flow
- Channel options include:
  - Customer visit the service site
  - Service providers go to their customers
  - Service transaction is conducted remotely
- Place and time decision include where services should be delivered in bricks-and-mortar context, when it should be delivered
- Delivery in cyberspace is facilitated by technology; e-commerce allows 24-hour delivery, saving time and effort
- Intermediaries play roles in distributing services
- Service processes (people-processing services, possession-processing services, and information-based services) affect international market entry via the drivers:
  - Market drivers
  - Competition drivers
  - Technology drivers
  - Cost drivers
  - Government drivers

## Chapter 6: Setting Prices and Implementing Revenue Management

### Effective Pricing is Central to Financial Success

#### What Makes Service Pricing Strategy Different and Difficult?

- Harder to calculate financial costs of creating a service process or performance than manufactured good
- Variability of inputs and outputs:
  - How can firms define a “unit of service” and establish basis for pricing?
- Importance of time factor – same service may have more value to customers when delivered faster
- Customers find service pricing difficult to understand, risky, and sometimes even unethical

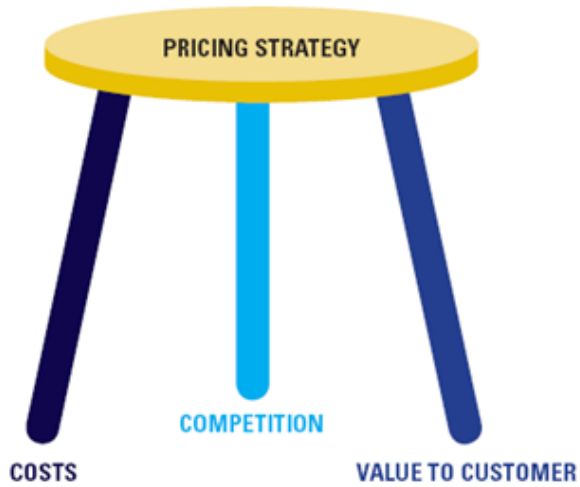
#### Objectives for Pricing of Services

- Revenue and Profit Objectives
  - Seek profit
  - Cover costs
- Patronage and User-Based Objectives
  - Build demand
    - Demand maximization

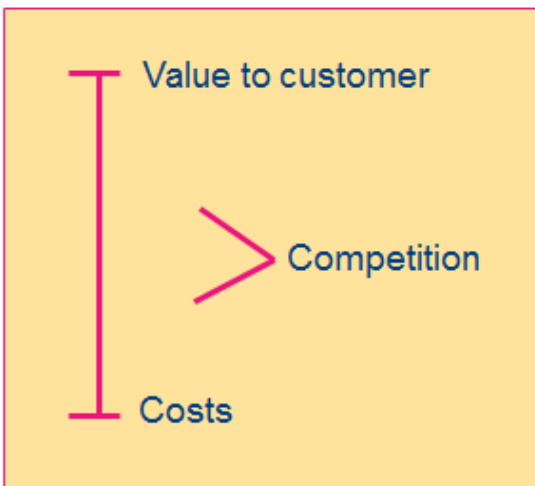
- Full capacity utilization
- Build a user base
  - Stimulate trial and adoption of new service
  - Build market share/large user base

## Pricing Strategy as Represented by the Pricing Tripod

### The Pricing Tripod



### Floor and Ceiling of Price



## Three Main Approaches to Pricing

Cost-Based Pricing	Value-Based Pricing	Competition-Based Pricing
<ul style="list-style-type: none"><li>• Set prices relative to financial costs</li><li>• Activity-Based Costing</li><li>• Pricing implications of cost analysis</li></ul>	<ul style="list-style-type: none"><li>• Relate price to value perceived by customer</li></ul>	<ul style="list-style-type: none"><li>• Monitor competitors' pricing strategy</li><li>• Dependent on the price leader</li></ul>

### *Cost-Based Pricing: Traditional vs. Activity-Based Costing*

- Traditional costing approach
  - Emphasized expense categories (arbitrary overheads allocation)
  - May result in reducing value generated for customers
- ABC management systems
  - Link resource expenses to variety and complexity of goods/services produced
  - Yields accurate cost information

**BUT, customers care about value to themselves, not what service production costs the firm**

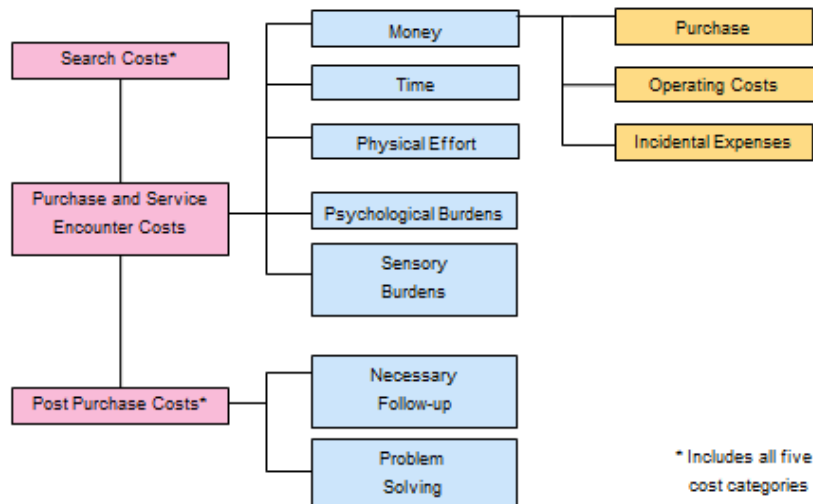
### *Value-Based Pricing: Understanding Net Value*

- Net Value = Perceived Benefits to Customers (Gross Value) – All Perceived Outlays (Money, Time, Mental/Physical Effort)
- Consumer surplus: difference between price paid and amount customer would have been willing to pay in absence of other options
- Competing services are then evaluated via comparison of net value

### *Value-Based Pricing: Strategies for Enhancing Net Value*

- Enhance gross value – benefits delivered
  - Add benefits to core product
  - Enhance supplementary service
  - Manage perceptions of benefits delivered
- Reduce costs incurred by
  - Reducing monetary costs of acquisition and usage
  - Cutting amount of time required to evaluate, buy, use service
  - Lowering effort associated with purchase and use

### Defining Total User Cost



### Competition-Based Pricing

- Price competition increases due to:
  - Increasing competition
  - Increase in substituting offers
  - Wider distribution of competitor
  - Increasing surplus capacity in the industry
- However under these circumstances, price competition can decrease:
  - High non-price-related costs of using alternatives
  - Personal relationships matter
  - Switching costs are high
  - Time and location specificity reduces choice
  - Managers should examine all related financial and non-monetary costs

## Competitive-Based Pricing

Which clinic would you patronize if you needed a chest x-ray (assuming that all three clinics offer good technical quality)?		
Clinic A	Clinic B	Clinic C
<ul style="list-style-type: none"><li>• Price \$65</li><li>• Located 1 hour away by car or transit</li><li>• Next available appointment is in 3 weeks</li><li>• Hours: Monday – Friday, 9am – 5pm</li><li>• Estimated wait at clinic is about 2 hours</li></ul>	<ul style="list-style-type: none"><li>• Price \$125</li><li>• Located 15 min away by car or transit</li><li>• Next available appointment is in 1 week</li><li>• Hours: Monday – Friday, 8am – 10pm</li><li>• Estimated wait at clinic is about 30 to 45 minutes</li></ul>	<ul style="list-style-type: none"><li>• Price \$185</li><li>• Located next to your office building (or college)</li><li>• Next available appointment is in 1 day</li><li>• Hours: Monday – Saturday, 8am – 10pm</li><li>• By appointment – estimated wait at clinic is about 0 to 15 minutes</li></ul>

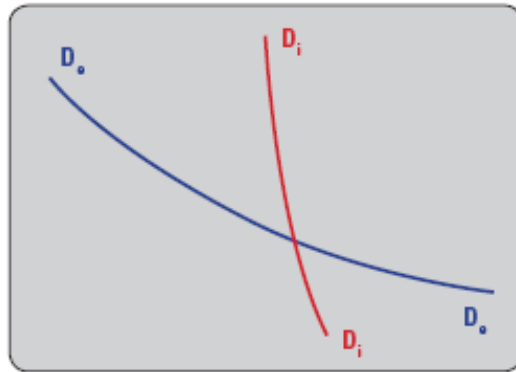
## Revenue Management: What it is and how it works

### Maximizing Revenue from Available Capacity at a Given Time

- Most effective in the following conditions:
  - High fixed cost structure
  - Relatively fixed capacity
  - Perishable inventory
  - Variable and uncertain demand
  - Varying customer price sensitivity
- Revenue management (RM) is price customization
  - Charge different value segments different prices for same product based on price sensitivity
- RM uses mathematical models to examine historical data and real time information to determine
  - What prices to charge within each price bucket
  - How many service units to allocate to each bucket
- Rate fences deter customers willing to pay more from trading down to lower prices (minimize consumer surplus)

## Price Elasticity

PRICE PER UNIT  
OF SERVICE



QUANTITY OF UNITS DEMANDED

$$\text{Price Elasticity} = \frac{\text{Percentage change in demand}}{\text{Percentage change in price}}$$

$D_e$  : Demand is *price elastic*. Small changes in price lead to big changes in demand

$D_i$  : Demand for service is *price inelastic*. Big changes have little impact on demand

## Key Categories of Rate Fences: Physical (Product-Related) Fences

### Product-Related Fences

Rate Fences	Examples
Basic Product	<ul style="list-style-type: none"> <li>• Class of travel (Business/Economy Class)</li> <li>• Size and furnishing of a hotel room</li> <li>• Seat location in a theatre</li> </ul>
Amenities	<ul style="list-style-type: none"> <li>• Free breakfast at a hotel, airport pick-up, etc.</li> <li>• Free golf cart at a golf course</li> </ul>
Service Level	<ul style="list-style-type: none"> <li>• Priority wait listing</li> <li>• Increase in baggage allowances</li> <li>• Dedicated service hotlines</li> <li>• Dedicated account management team</li> </ul>

## Key Categories of Rate Fences: Non-Physical Fences

### Transaction Characteristics

Rate Fences	Examples
Time of booking or reservation	<ul style="list-style-type: none"> <li>• Requirements for advance purchase</li> <li>• Must pay full fare two weeks before departure</li> </ul>
Location of booking or reservation	<ul style="list-style-type: none"> <li>• Passengers booking air tickets for an identical route in different countries are charged different prices</li> </ul>
Flexibility of ticket usage	<ul style="list-style-type: none"> <li>• Fees/penalties for canceling or changing a reservation (up to loss of entire ticket price)</li> <li>• Non-refundable reservation fees</li> </ul>

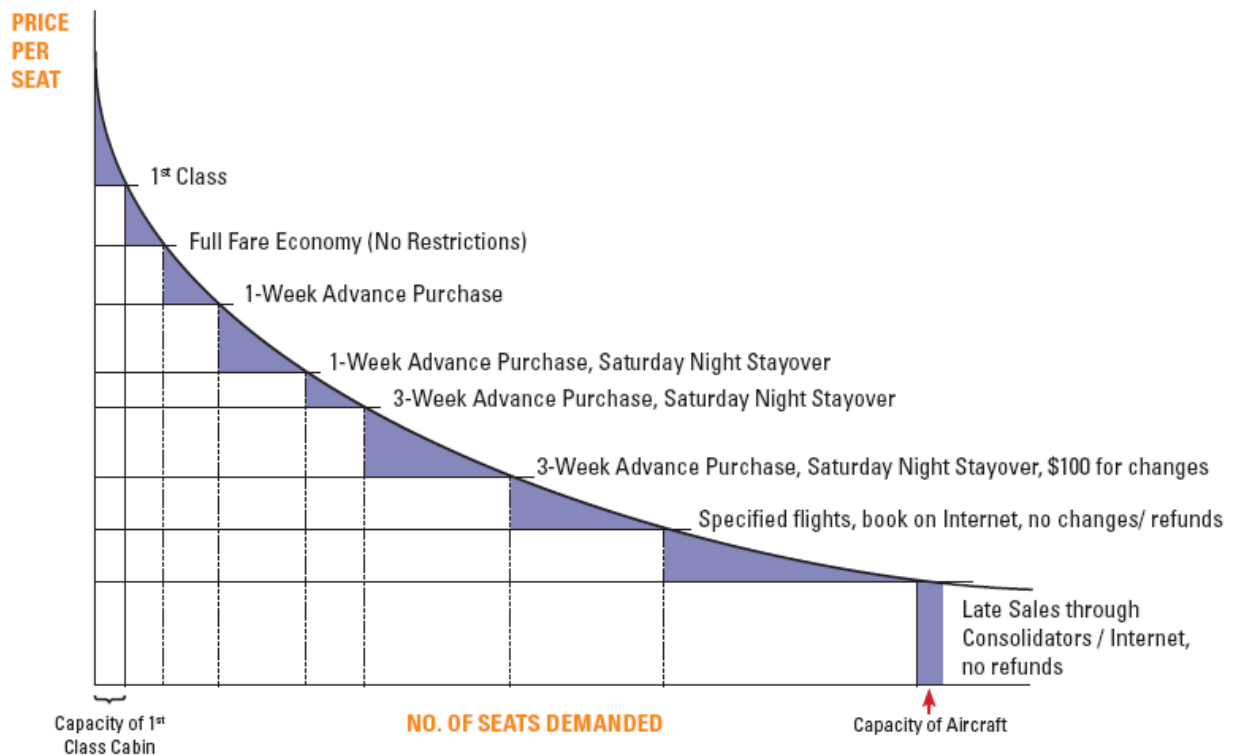
### Consumption Characteristics

Rate Fences	Examples
Time or duration of use	<ul style="list-style-type: none"> <li>• Early bird special in restaurant before 6pm</li> <li>• Must stay over on Sat for airline, hotel</li> <li>• Must stay at least five days</li> </ul>
Location of consumption	<ul style="list-style-type: none"> <li>• Price depends on departure location, especially in international travel</li> <li>• Prices vary by location (between cities, city centre vs. edges of city)</li> </ul>

### Buyer Characteristics

Rate Fences	Examples
Frequency or volume of consumption	<ul style="list-style-type: none"> <li>• Member of certain loyalty tier with the firm get priority pricing, discounts or loyalty benefits</li> </ul>
Group membership	<ul style="list-style-type: none"> <li>• Child, student, senior citizen discounts</li> <li>• Affiliation with certain groups (e.g., Alumni)</li> </ul>
Size of customer group	<ul style="list-style-type: none"> <li>• Group discounts based on size of group</li> </ul>

### Relating Price Buckets and Fences to Demand Curve



\* Dark areas denote amount of consumer surplus (goal of segmented pricing is to reduce this)

## Ethical Concerns in Service Pricing

### Ethical Concerns in Pricing

- Many services have complex pricing schedules
  - Hard to understand
  - Difficult to calculate full costs in advance of service
- Unfairness and misrepresentation in price promotions
  - Misleading advertising
  - Hidden charges
- Too many rules and regulations
  - Customers feel constrained, exploited
  - Customers unfairly penalized when plans change

### Designing Fairness into Revenue Management

- Design clear, logical, and fair price schedules and fences
- Use high published prices and present fences as opportunities for discounts
- Communicate consumer benefits of revenue management
- Use bundling to “hide” discounts
- Take care of loyal customers
- Use service recovery to compensate for overbooking

## Putting Service Pricing into Practice

### Pricing Issues: Putting Strategy into Practice



### Putting Service Pricing into Practice

#### *How much to charge?*

- Pricing tripod provides a useful starting point
- A specific figure must be set for the price
- Need to consider the pros and cons, and ethical issues

### *What basis for pricing?*

- Completing task
- Admission to a service performance
- Time based
- Monetary value of service delivered (e.g., commission)
- Consumption of physical resources (e.g., food and beverages)

### *Who should collect payment?*

- Service provider or specialist intermediaries
- Direct or non-direct channels

### *Where should payment be made?*

- Conveniently located intermediaries
- Mail/bank transfer

### *When should payment be made?*

- In advance
- Once service delivery has been completed

### *How should payment be made?*

- Cash
- Token
- Stored value card
- Electronic fund transfer
- Charge Card (Debit/Credit)
- Vouchers

### *How to communicate prices?*

- Relate the price to that of competing products
- Ensure price is accurate and intelligible

## **Summary**

- Pricing objectives can include
  - Generating revenues and profit, building demand, and developing user base
- Three main foundations to pricing a service
  - Cost-based pricing
  - Competition-based pricing
  - Value-based pricing
- Firm must be aware of competitive pricing but may be harder to compare for services than for goods
- Revenue management
  - Maximizes revenue from a given capacity at a point in time
  - Manage demand and set prices for each segment closer to perceived value

- Use of rate fences
- Ethical issues in pricing
  - Complex pricing schedules
  - Unfairness and misrepresentation in advertising
  - Hidden charges
  - Too many rules and regulations

## Chapter 8: Designing and Managing Service Processes

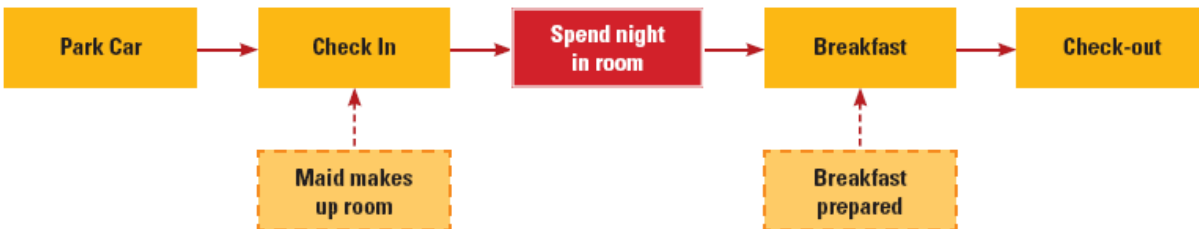
### Flowcharting Customer Service Processes

#### Flowcharting Service Delivery Helps to Clarify Product Elements

- Technique for displaying the nature and sequence of the different steps in delivery service to customers
- Offers way to understand total customer service experience
- Shows how nature of customer involvement with service organizations varies by type of service:
  - People processing
  - Possession processing
  - Mental Stimulus processing
  - Information processing

#### Flowcharts for People and Possession Processing Services

##### PEOPLE PROCESSING - STAY AT MOTEL

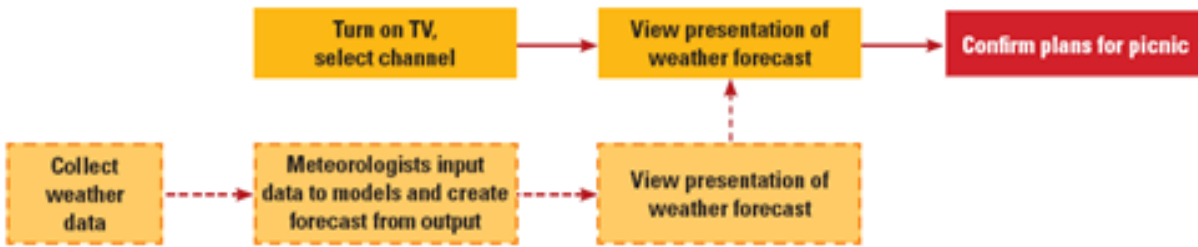


##### POSSESSION PROCESSING - REPAIR A DVD PLAYER



## Flowcharts for Mental Stimulus and Information Processing Services

### MENTAL STIMULUS PROCESSING - WEATHER FORECAST



### INFORMATION PROCESSING - HEALTH INSURANCE



## Blueprinting Services to Create Valued Experiences and Productive Operations

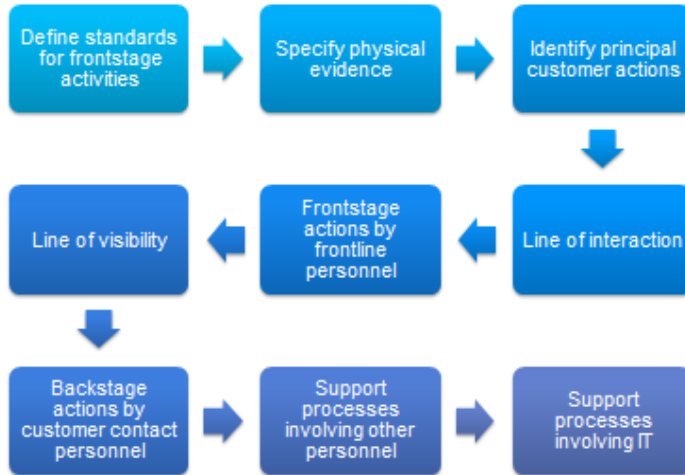
### Developing a Blueprint

- Developing a Blueprint
  - Identify key activities in creating and delivering service
  - Define “big picture” before “drilling down” to obtain a higher level of detail
- Advantages of Blueprinting
  - Distinguish between “frontstage” and “backstage”
  - Clarify interactions and support by backstage activities and systems
  - Identify potential fail points; take preventive measures; prepare contingency
  - Pinpoint stages where customers commonly have to wait

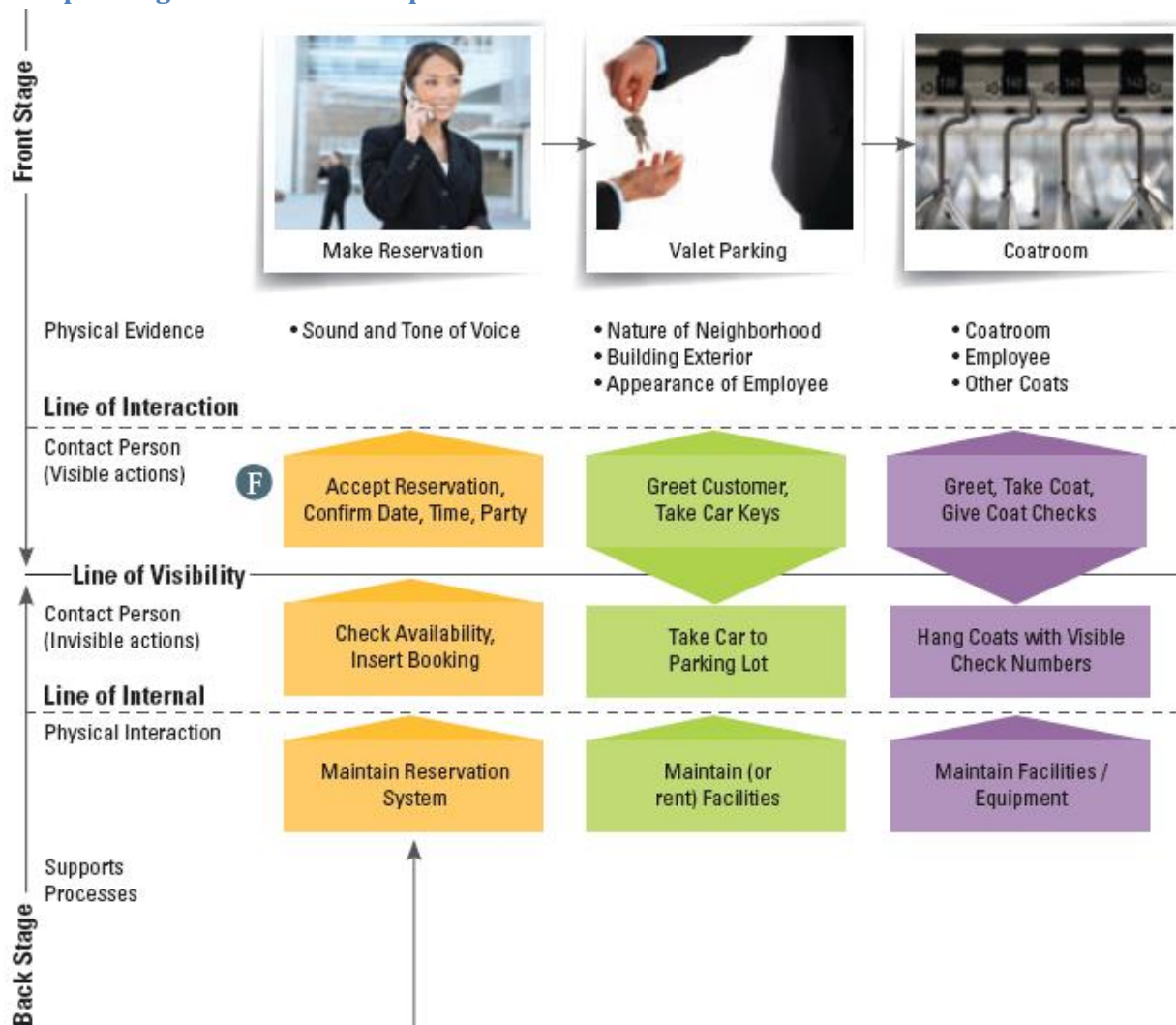
### Key Components of a Service Blueprint

#### Objectives:

- Identify fail points & risks of excessive waits
- Set service standards
- Fail-proof process



### Blueprinting the Restaurant Experience: Act 1



### Blueprinting the Restaurant Experience: A Three-Act Performance

- **Act 1:** Prologue and Introductory Scenes

- **Act 2: Delivery of Core Product**
  - Cocktails, seating, order food and wine, wine service
  - Potential fail points: menu information complete? Menu intelligible? Everything on the menu actually available?
  - Mistakes in transmitting information a common cause of quality failure
  - Customers may not only evaluate quality of food and drink, but how promptly it is served or serving staff attitudes
- **Act 3: The Drama Concludes**
  - Remaining actions should move quickly and smoothly, with no surprises at the end
  - Customer expectations: accurate, intelligible and prompt bill, payment handled politely, guest are thanks for their patronage

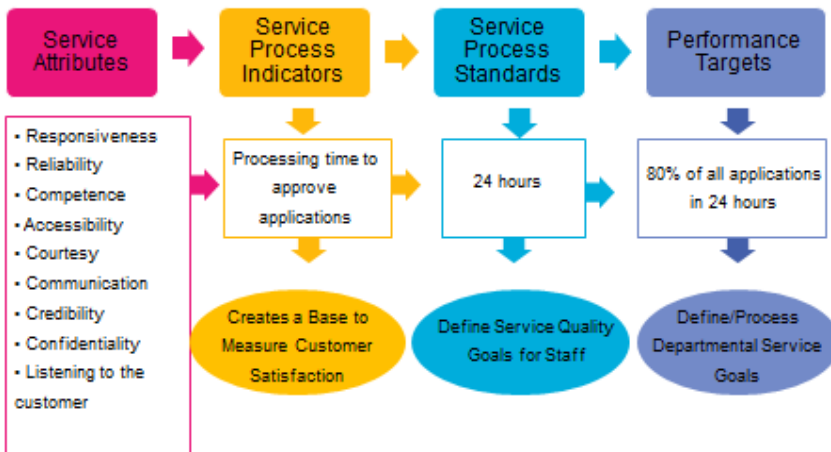
### Improving Reliability of Processes through Fail-Proofing

- Identify fail points
- Analysis of reasons for failure reveals opportunities for failure-proofing to reduce/eliminate future errors
- Need fail-safe methods for both employees and customers

### Setting Service Standards and Targets

- Service providers set standards for each step sufficiently high to satisfy and even delight customers
  - Include time parameters, script and prescriptions for appropriate style and demeanor
  - Must be expressed in ways that permit objective measurement
- Performance targets – specific process and team performance targets for which staff are responsible for
- Evaluate based on distinction between standards and targets
- First impression is important
  - Affects customer’s evaluations of quality during later stages of service delivery as customer perceptions of service experiences tend to be cumulative
- For low-contact service, a single failure committed front stage is relatively more serious than in a high-contact service

## Setting Standards and Targets for Customer Service Processes



## Redesigning Service Processes

### Why Redesign?

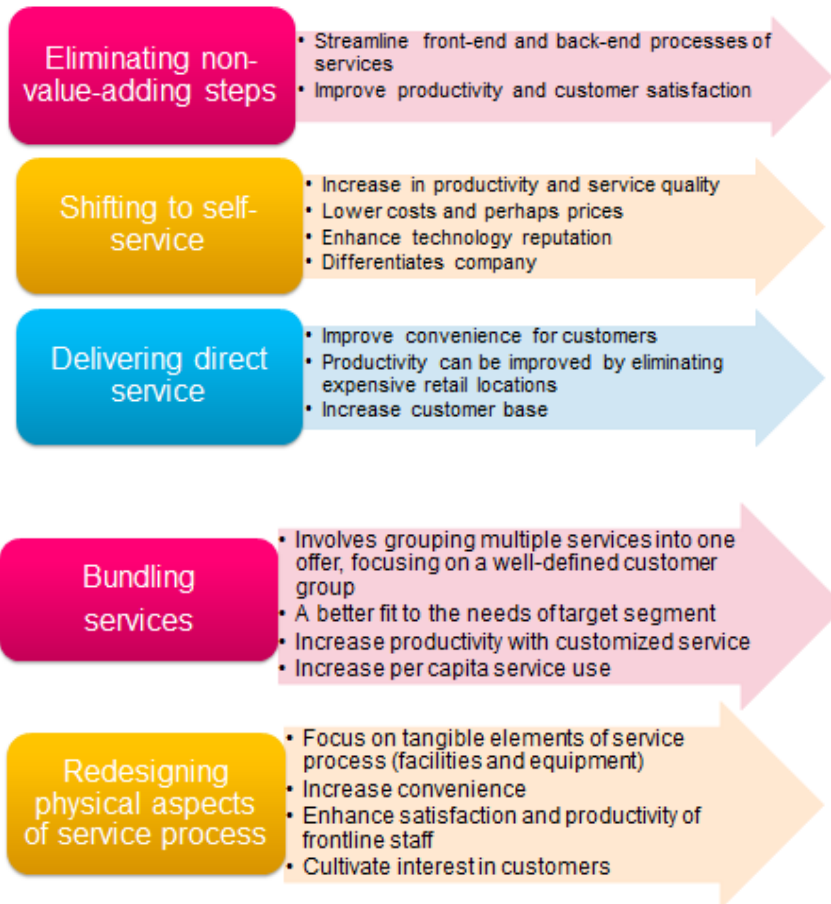
- Revitalizes process that has become outdated
- Changes in external environment make existing practices obsolete and require redesign or underlying processes
- Rusting occurs internally
  - Natural deterioration of internal processes; creeping bureaucracy; evolution of spurious, unofficial standards
  - Symptoms:
    - Extensive information exchange
    - Data that is not useful
    - High ratio of checking control activities to value-adding activities

"Institutions are like steel beams—they tend to rust. What was once smooth and shiny and nice tends to become rusty."

Mitchell T. Rabkin, MD,  
former president of Boston's Beth Israel Hospital

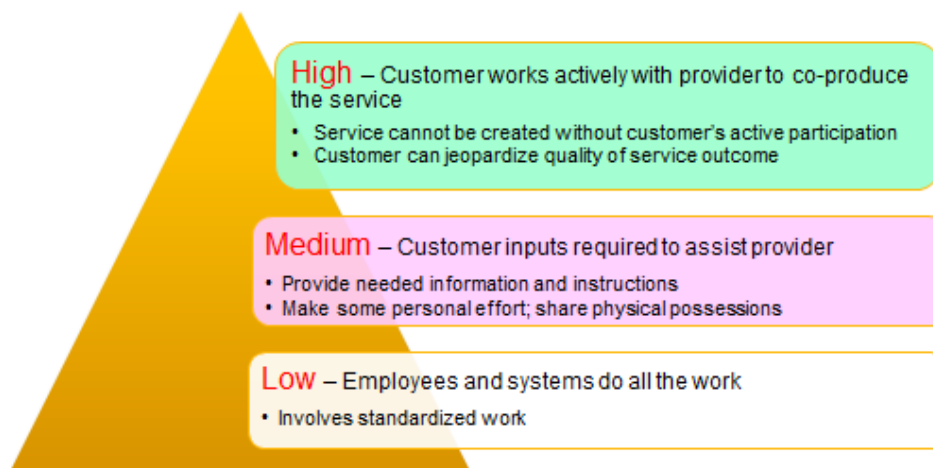
- Redesign aims to achieve these performance measures:
  - Reduced number of service failures
  - Reduced cycle time from customer initiation of a service process to its completion
  - Enhanced productivity
  - Increase customer satisfaction

## Process Redesign: Approaches and Potential Benefits



## The Customer as Co-Producer

### Levels of Customer Participation



### Customers as Partial Employees

- Customers can influence productivity and quality of service processes and outputs

- Customers not only bring expectations and needs but also need to have relevant service production competencies
- For the relationship to last, both parties need to cooperate with each other

### Managing Customers



### Self-Service Technologies

#### Self-Service Technologies (SSTs)

- SSTs are **the ultimate form** of customer involvement where customers undertake specific activities using facilities or systems provided by service supplier
  - Customer’s time and effort replace those of employees
- Information-based services lend selves particularly well to SSTs
  - Used in both supplementary services and delivery of core product

**Many companies and government organizations seek to divert customers from employee contact to Internet-based self-service**

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Time and Cost savings</li> <li>• Flexibility</li> <li>• Convenience of location</li> <li>• Greater control over service delivery</li> <li>• High perceived level of customization</li> </ul>	<ul style="list-style-type: none"> <li>• Anxiety and stress experienced by customers who are uncomfortable with using them</li> <li>• Some see service encounters as social experience and prefer to deal with people</li> </ul>

#### What Aspects of SSTs Please or Annoy Customers?

People love SSTs when...	People hate SSTs when...
<ul style="list-style-type: none"> <li>• SST machines are conveniently located and accessible 24/7 – often as close as the nearest computer!</li> <li>• Obtaining detailed information and</li> </ul>	<ul style="list-style-type: none"> <li>• SSTs fail – system is down, PIN numbers not accepted, etc.</li> <li>• Customers themselves mess up – forgetting passwords; failing to provide</li> </ul>

completing transactions can be done faster than through face-to-face or telephone contact

information as requested; simply hitting wrong buttons

**Key weakness:** few firms incorporate service recovery systems such that customer are still forced to make telephone calls or personal visits

### Putting SSTs to Test by Asking a Few Simple Questions

- Does the SST work reliably?
  - Firms must ensure that SSTs are dependable and user-friendly
- Is the SST better than interpersonal alternatives?
  - Customers wills tick to conventional methods is SST doesn't create benefits for them
- If it fails, what systems are in place to recover?
  - Always provide systems, structures, and technologies that will enable prompt service recovery when things fail

### Managing Customer's Reluctance to Change

- Increasing customer's participation level in a service can be difficult
- Marketing communications to be used to:
  - Prepare customer for change
  - Explain the rationale and benefits
  - What customers need to do differently in the future

### Summary

- Service blueprinting can be used to design a service and create a satisfying experience for customers.
- Blueprinting a restaurant (or other service) can be a three-act performance
  - Prologue and introductory scenes
  - Delivery of the core product
  - Conclusion of the drama
- Service standards and targets are different and can be used to evaluate performance
- Service process redesign reduces service failure and enhances productivity
- When the customer is a co-producer, issues to consider are
  - Levels of customer participation
  - Self-service technologies (SST)
  - Psychological factors in customer co-production
  - Aspects of SST that please of annoy customers

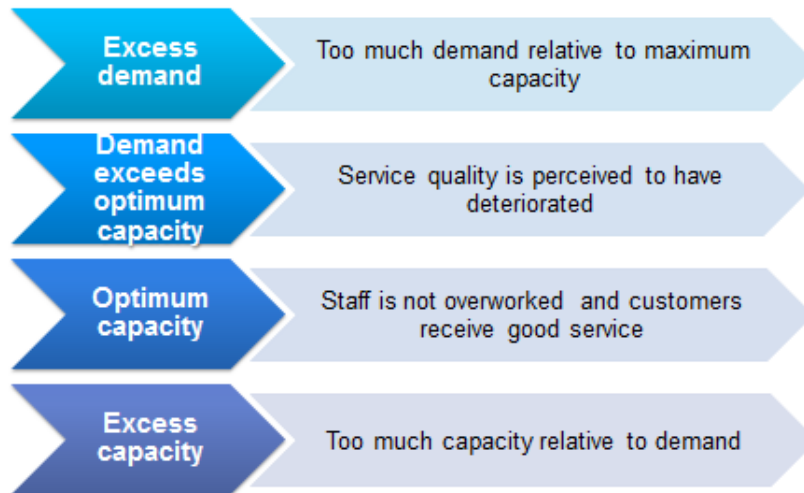
# Chapter 9: Balancing Demand and Productive Capacity

## Fluctuations in Demand Threaten Service Productivity

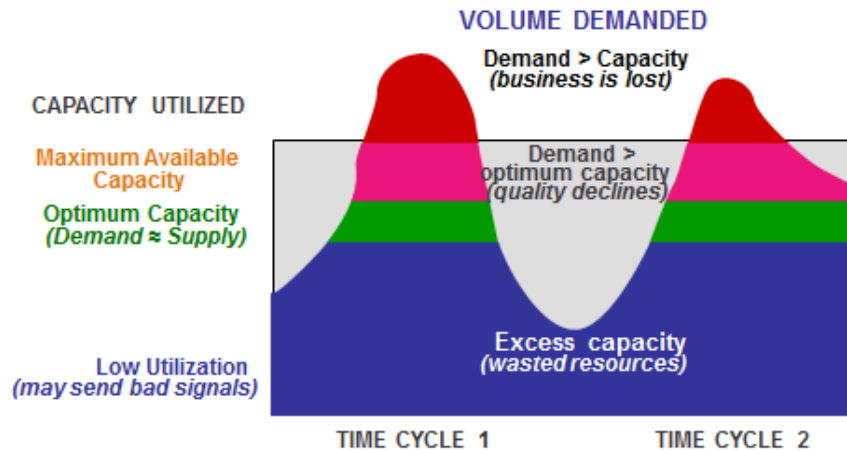
### Defining Productive Capacity

- Productive capacity can take several forms in services
  - Physical facilities designed to contain customers
  - Physical facilities designed for storing or processing goods
  - Physical equipment used to process people, possessions, or information
  - Labor
  - Infrastructure
- Financial success in capacity-constrained business is a function of management's ability to use productive capacity as **efficiently** and **profitably** as possible

### From Excess Demand to Excess Capacity



### Variations in Demand Relative to Capacity



### Addressing Problem of Fluctuating Demand

Two basic approaches of which most firms use a mix of:

- Adjust level of capacity to meet demand
  - Need to understand productive capacity and how it varies on an incremental basis
- Manage level of demand
  - Use marketing strategies to smooth out peaks, fill in valleys
  - Inventorying demand until capacity becomes available

## Managing Capacity

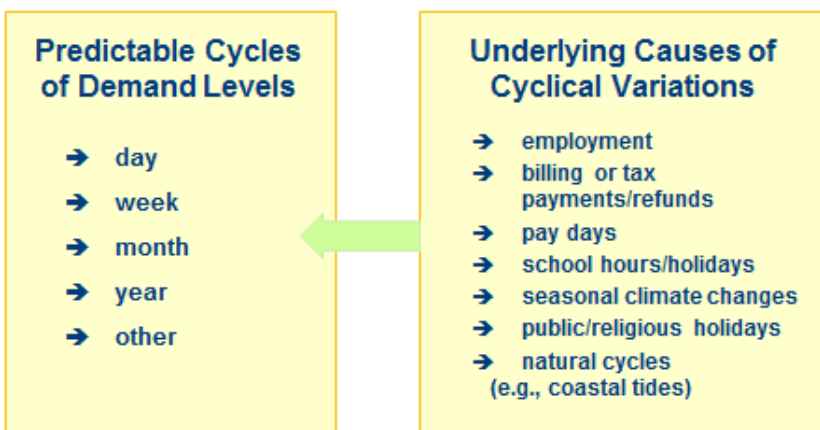
- Enables more people to be served at same level of capacity
- Stretch and shrink:
  - Offer inferior extra capacity at peaks (e.g., bus/train standees)
  - Use facilities for longer/shorter periods
  - Reduce amount of time spent in process by minimizing slack time
- Adjusting capacity to match demand
  - Rest during low demand
  - Cross-train employees
  - Use part-time employees
  - Customers perform self-service
  - Ask customers to share
  - Create flexible capacity
  - Rent/share facilities and equipment

## Analyze Patterns of Demand

### Demand Varies by Market Segment

- Understand why customers from specific market segments select this service
- Keep good records of transactions to analyze demand patterns
  - Sophisticated software can help to track customer consumption patterns
- Record weather conditions and other special factors that might influence demand

### Predictable Demand Patterns and their Underlying Causes



## Causes of Seemingly Random Changes in Demand Levels

Question: Which of these events can be predicted?

1. Weather
2. Health problems
3. Accidents, Fires, Crime
4. Natural disasters

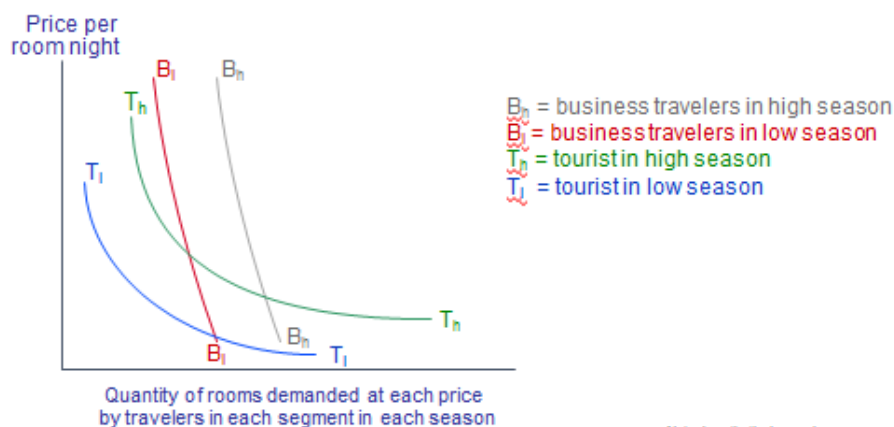
## Managing Demand

- Take no action
  - Let demand find its own levels
- Interventionist approach
  - Reduce demand in peak periods
  - Increase demand when there is excess capacity
- Inventorying demand until capacity becomes available
  - Formal wait and queuing system
  - Reservation system

## Marketing Mix Elements to Shape Demand Patterns

- Use price and other nonmonetary costs to manage demand
- Change product elements
- Modify place and time of delivery
  - No change
  - Vary times when service is available
  - Offer service to customers at a new location
- Promotion and education

## Hotel Room Demand Curves by Segment and Season



## Inventory Demand through Waiting Lines and Queuing Systems

### Waiting is a Universal Phenomenon

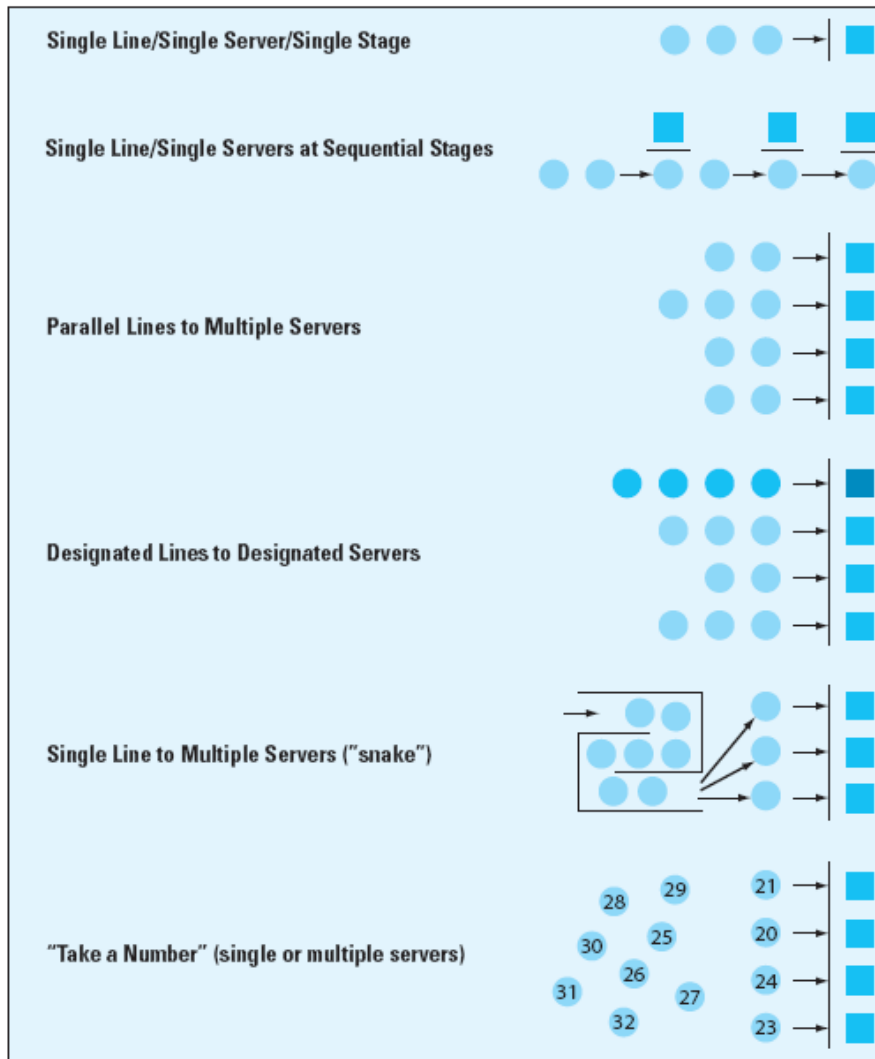
- An average person may spend up to 30 minutes/day waiting in line – equivalent to over one week per year
- Nobody likes to wait
- It's boring, time-wasting, and sometimes physically uncomfortable

### Why do Waiting Lines Occur?

- Because number of arrivals at a facility exceeds capacity of system to process them at a specific point in the process
- Queues are basically a symptom of unresolved capacity management problems
- Not all queues take form of a physical waiting line in a single location
  - Queues may be physical but geographically dispersed
  - Some are virtual (e.g., phone)

### Managing Waiting Lines

- Rethink design of queuing system
- Install a reservation system
- Tailoring the queuing system to different market segments
- Manage customer behavior and perceptions of wait
- Redesign processes to shorten transaction time



### Queuing Systems can be tailored to Market Segments

- Urgency of job
  - Emergencies vs. non-emergencies
- Duration of service transaction
  - Number of items to transact
  - Complexity of task
- Payment of premium price
- Importance of customer
  - Frequent users/high volume purchasers vs. others

## Customer Perceptions of Waiting Time

### Ten Propositions on Psychology of Waiting Lines

Feels longer than	
Unoccupied time	Occupied time
Solo waits	Group waits
Physically uncomfortable waits	Comfortable waits
Pre- and post-process waits	In-process waits
Unexplained waits	Explained waits
Unfamiliar waits	Known, finite waits
Unfair waits	Fair waits
Anxious waits	Calm waits
Monotonous waits	Valued waits

## Inventory Demand through Reservations System

### Benefits of Reservations

- Saves customers from having to wait in line
- Helps to control and manage the demand (e.g., leave time for emergency jobs)
- Pre-sells the service and can be used to prepare and educate the customer for the service encounter
- Data captured helps organizations to understand their demand patterns and to plan their operations and staffing levels

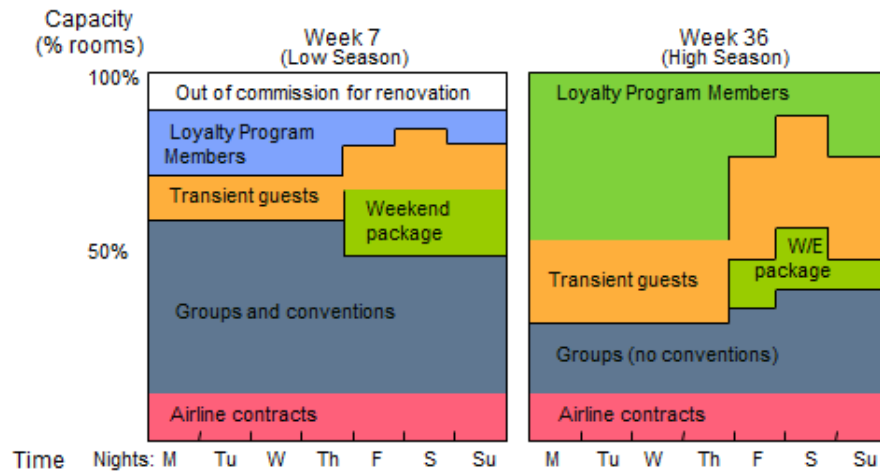
### Characteristics of Well-Designed Reservations System

- Fast and user-friendly for customers and staff
- Responsive to customer queries and needs
- Offers options for self-service (e.g., through an online reservation system)
- Accommodates preferences (e.g., room with a view)
- Deflects demand from unavailable first choices to alternative times and locations

### Reservations Strategies should focus on Yield

- Yield analysis helps managers recognize **opportunity cost** of allocating capacity to one customer/segment when another segment might yield a higher rate later
- Decisions need to be based on good information
  - Detailed records of past usage
  - Current market intelligence and good marketing sense
  - Realistic estimate of the chances of obtaining higher rated business
- When firms overbook to increase yield
  - Victims of overbooking should be compensated to preserve the relationship

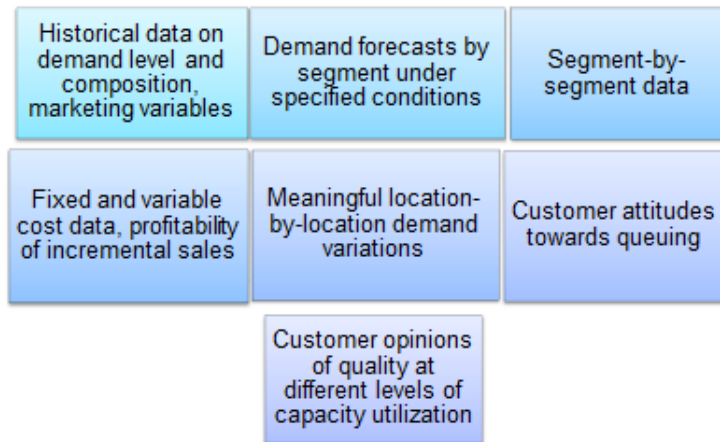
## Setting Hotel Room Sales Targets by Segment and Time Period



## Creating Alternative Use for Otherwise Wasted Capacity

- Use capacity for service differentiation
- Reward your best customers and build loyalty
- Customer and channel development
- Reward employees
- Barter free capacity

## Information Needed for Demand and Capacity Management Strategies



## Summary

- At any moment in time, a fixed-capacity service may face
  - Excess demand
  - Demand exceeding optimum capacity
  - Excess capacity
- To balance demand and capacity, a firm can:
  - Manage capacity
  - Take no action and let demand find its own levels

- Reduce demand in peak periods
- Increase demand when there is excess capacity
- Inventory demand using wait & queuing, and reservation systems
- Capacity can be managed through:
  - Stretching or shrinking capacity levels
  - Adjusting capacity to match demand
  - Creating flexible capacity
- Demand can be managed through
  - Analysis of patterns
  - To be reshaped by marketing strategies
- Waiting is a universal phenomenon. Waits can be reduced by:
  - Rethinking and redesigning the queuing system
  - Managing customers' behavior and their perceptions of the wait installing an effective reservation system focused on yield

## Chapter 10: Crafting the Service Environment

### What is the Purpose of Service Environments?

#### Purpose of Service Environments

- Shape customers' experience and their behaviors
- Support image, positioning, and differentiation
- Part of the value proposition
- Facilitate service encounter and enhance productivity

#### Shape Customers' Experience and their Behaviors

- Message-creating medium
  - Symbolic cues to communicate the distinctive nature and quality of the service experience
- Attention-creating medium
  - Make servicescape stand out from competition and attract customers from target segments
- Effect-creating medium
  - Use colors, textures, sounds, scents, and spatial design to enhance desired service experience

## Support Image, Position, and Differentiation



Orbit Hotel and Hostel, Los Angeles



Four Seasons Hotel, New York

## Servicescape as Part of Value Proposition

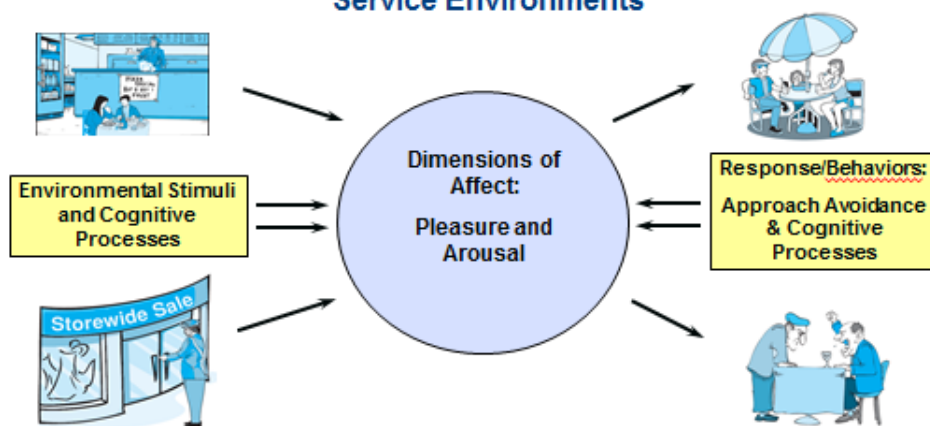
- Physical surroundings help shape appropriate feelings and reactions in customers and employees
  - E.g., Disneyland, Denmark's LEGOLAND
- Servicescape form a core part of the value proposition
  - Las Vegas: repositioned itself to a somewhat more wholesome fun resort, visually striking entertainment center
  - Florida-based Muvico: builds extravagant movie theatres and offers plush amenities. *"What sets you apart is how you package it"* (Muvico's CEO, Hamid Hashemi)

The power of servicescape is being discovered

## Understanding Consumer Responses to Service Environments

### The Mehrabian-Russell Stimulus-Response Model

#### Feelings Are a Key Driver of Customer Responses to Service Environments



### Insights from Mehrabian-Russell Stimulus-Response Model

It is simple yet fundamental model of how people respond to environments that illustrates:

- The environment, its conscious and unconscious perceptions, and interpretation influence how people feel in that environment
- Feelings, rather than perceptions/thoughts drive behavior
- Typical outcome variable is 'approach' or 'avoidance' of an environment, but other possible outcomes can be added to model

### The Russell Model of Affect



### Insights from Russell's Model of Affect

- Emotional responses to environments can be described along two main dimensions:
  - Pleasure: subjective, depending on how much individual likes or dislikes environment
  - Arousal: how stimulated individual feels, depends largely on information rate or load of an environment
- Separates cognitive emotions from emotional dimensions
- Advantage: simple, direct approach to customers' feelings
  - Firms can set targets for affective states

### Drivers of Affect

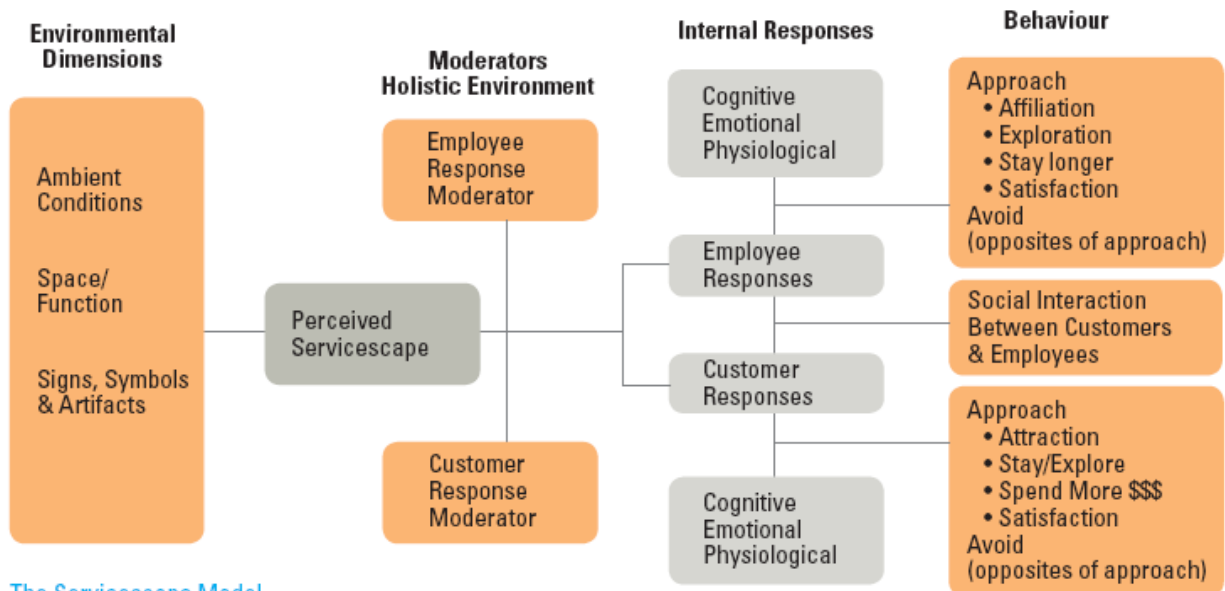
- Caused by perceptions and cognitive processes of any degree of complexity
- Determines how people feel in a service setting
- If higher levels of cognitive processes are triggered, the interpretation of this process determines people's feelings
- The more complex a cognitive process becomes, the more powerful its potential impact on affect

### Behavioral Consequence of Affect

- Pleasant environments result in approach, whereas unpleasant ones result in avoidance
- Arousal amplifies the basic effect of pleasure on behavior
  - If environment is pleasant, increasing arousal can generate excitement, leading to a stronger positive consumer response
  - If environment is unpleasant, increasing arousal level will move customers into the "distressed" region

- Feelings during service encounters are important driver of customer loyalty

## An Integrative Framework: The Servicescape Model



### 7 The Servicescape Model.

- Identifies the main dimensions in a service environment and views them holistically
- Internal customer and employee responses can be categorized into cognitive, emotional, and psychological responses, which lead to overt behavioral responses towards the environment
- Key to effective design is how well each individual dimensions fits together with everything else

## Dimensions of the Service Environment

### Main Dimensions in Servicescape Model

- Ambient Conditions
  - Characteristics of environment pertaining to our five sense
- Spatial Layout and Functionality
  - Spatial layout
    - Floorplan
    - Size and shape of furnishings
  - Functionality: ability of those items to facilitate performance
- Signs, Symbols, and Artifacts
  - Explicit or implicit signals to:
    - Help consumers find their way

### Ambient Conditions

- Ambient conditions are perceived both separately and holistically, and include:
  - Lighting and color schemes
  - Size and shape perceptions
  - Sounds such as noise and music

- Temperature
  - Scents
- Clever design of these conditions can elicit desired behavioral responses among consumers

### Music

- In service settings, music can have powerful effect on perceptions and behaviors, even if played at barely audible levels
- Structural characteristics of music – such as tempo, volume, and harmony – are perceived holistically
  - Fast tempo music and high volume music increase arousal levels
  - People tend to adjust their pace, either voluntarily or involuntarily, to match tempo of music
- Careful selection of music can deter wrong type of customers

### Scent

- An ambient smell is one that pervades an environment
  - May or may not be consciously perceived by customers
  - Not related to any particular product
- Scents have distinct characteristics and can be used to solicit emotional, physiological, and behavioral responses
- In service settings, research has shown that scents can have significant effect on customer perceptions, attitudes, and behaviors

### *Aromatherapy: Effects of Selected Fragrances on People*

Fragrance	Aroma Type	Aromatherapy Class	Traditional Use	Potential Psychological Effect on People
Eucalyptus	Camphoraceous	Toning, stimulating	Deodorant, antiseptic, soothing agent	Stimulating and energizing
Lavender	Herbaceous	Calming, balancing, soothing	Muscle relaxant, soothing agent, astringent	Relaxing and calming
Lemon	Citrus	Energizing, uplifting	Antiseptic, soothing agent	Soothing energy levels
Black pepper	Spicy	Balancing, soothing	Muscle relaxant, aphrodisiac	Balancing people's emotions

### Color

- Colors can be defined into three dimensions:
  - Hue is the pigment of the color
  - Value is the degree of lightness or darkness of the color
  - Chroma refers to hue-intensity, saturation, or brilliance
- People are generally drawn to warm color environments

- Warm colors encourage fast decision making and are good for low-involvement decisions or impulse buys
- Cool colors are preferred for high-involvement decisions

### *Common Associations and Human Responses to Colors*

Color	Degree of Warmth	Nature Symbol	Common Association and Human Responses to Color
Red	Warm	Earth	High energy and passion; can excite and stimulate emotions, expressions, and warmth
Orange	Warmest	Sunset	Emotions, expressions, and warmth
Yellow	Warm	Sun	Optimism, clarity, intellect, and mood-enhancing
Green	Cool	Growth, grass and trees	Nurturing, healing and unconditional love
Blue	Coolest	Sky and Ocean	Relaxation, serenity and loyalty
Indigo	Cool	Sunset	Mediation and spirituality
Violet	Cool	Violet flower	Spirituality, reduces stress, can create an inner feeling of calm

### *Signs, Symbols, and Artifacts*

- Communicates the firm’s image and helps customers find their way
  - First time customers will automatically try to draw meaning from the signs, symbols, and artifacts
- Challenge is to guide customer through the delivery process
  - Unclear signals from a servicescape can result in anxiety and uncertainty about how to proceed and obtain the desired service

## Putting it all Together

### Selection of Environmental Design Elements

- Consumers perceive service environments holistically
  - No dimension of design can be optimized in isolation, because everything depends on everything else
  - Holistic characteristic of environments makes designing service environment an art

### Tools to Guide Servicescape Design

- Keen observation of customers’ behavior and responses
- Feedback and ideas from frontline staff and customers
- Photo audit – Mystery Shopper to take photographs of service experience
- Field experiments can be used to manipulate specific dimensions in an environment and the effects observed
- Blueprinting or service mapping – extended to include physical evidence in the environment

## Summary

- Service environment:
  - Shapes customers’ experiences and behavior

- Facilitates service encounters and enhances productivity
- Mehrabian-Russell stimulus-response model and Russell’s model of affect help us understand customer responses to service environments
- Main dimensions of servicescape model:
  - Ambient conditions – music, scent, color, etc.
  - Spatial layout and functionality
  - Sign, symbols, and artifacts
- When putting it all together, firms should
  - Design with a holistic view
  - Design from a customer’s perspective
  - Use tools to guide servicescape design

## Chapter 11: Managing People for Service Advantage

### Service Employees are Crucially Important

#### Service Personnel: Source of Customer Loyalty & Competitive Advantage

- Customer’s perspective: encounter with service staff is most important aspect of service
- Firm’s perspective: frontline is an important source of differentiation and competitive advantage
- Frontline is an important driver of customer loyalty
  - Anticipating customer needs
  - Customizing service delivery
  - Building personalized relationship

#### Frontline in Low-Contact Services

- Many routine transactions are now conducted without involving frontline staff, e.g.,
  - ATMs (Automated Teller Machines)
  - IVE (Interactive Voice Response) systems
  - Websites for reservations/ordering, payment, etc.
- However, frontline employees remain crucially important
- “Moments of Truths” drive customer’s perception of the service firm

### Factors Contributing to the Difficulty of Frontline Work

#### Boundary Spanning Roles

- Boundary spanners link the organization to outside world
- Multiplicity of roles often results in service staff having to pursue both operational and marketing goals
- Consider management expectations of service staff:
  - Delight customers
  - Be fast and efficient in executing operational tasks
  - Do selling, cross selling, and up-selling

- Enforce pricing schedules and rate integrity

### Role Stress in Frontline Employees

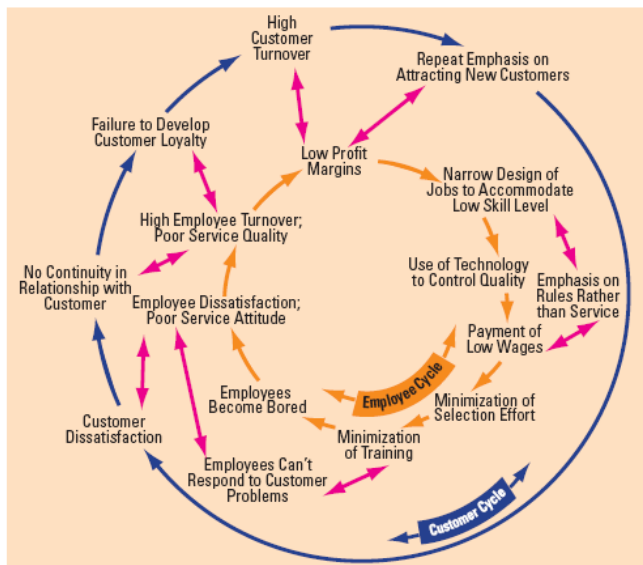
- Organization vs. Client: Dilemma whether to follow company rules or to satisfy customer demands
  - This conflict is especially acute in organizations that are not customer-oriented
- Person vs. Role: conflicts between what jobs require and employee’s own personality and beliefs
  - Organizations must instill ‘professionalism’ in frontline staff
- Client vs. Client: conflicts between customers that demand service staff intervention

### Emotional Labor

- “The act of expressing socially desired emotions during service transactions”
  - Performing emotional labor in response to society’s or management’s display rules can be stressful
  - Good HR practice emphasized selective recruitment, training, counseling, strategies to alleviate stress

## Cycles of Failure, Mediocrity, and Success

### Cycles of Failure



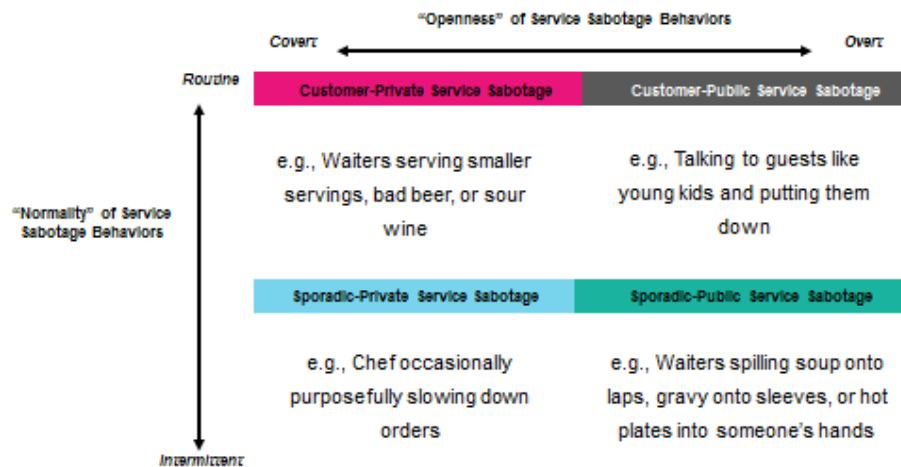
**SOURCE**

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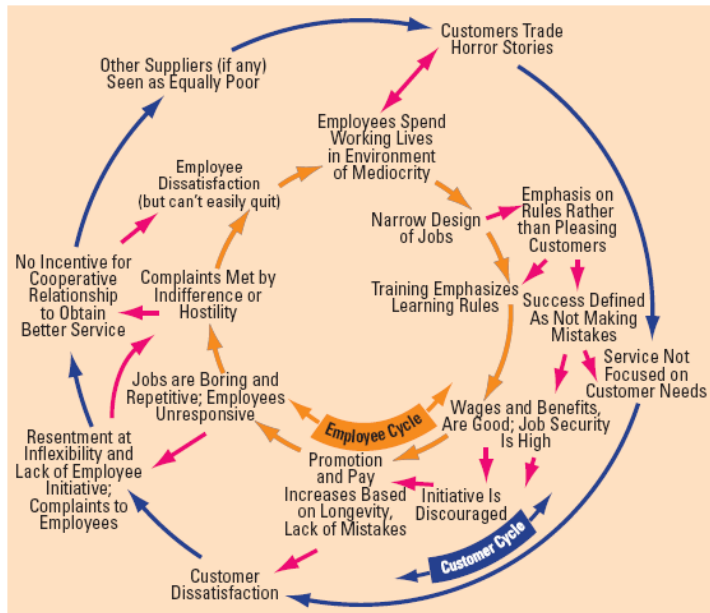
- The employee cycle of failure
  - Narrow job design for low skill levels
  - Emphasis on rules rather than service
  - Use of technology to control quality
  - Bored employees who lack ability to respond to customer problems

- Customers are dissatisfied with poor service attitude
- Low service quality
- High employee turnover
- The customer cycle of failure
  - Repeated emphasis on attracting new customers
  - Customers dissatisfied with employee performance
  - Customers always served by new faces
  - Fast customer turnover
  - Ongoing search for new customers to maintain sales volume
- Cost of short-sighted policies are ignored:
  - Constant expense of recruiting, hiring, and training
  - Lower productivity of inexperienced new workers
  - Higher costs of winning new customers to replace those lost – more need for advertising and promotional discounts
  - Loss of revenue stream from dissatisfied customers who turn to alternatives
  - Loss of potential customers who are turned off by negative word-of-mouth

## Service Sabotage



## Cycle of Mediocrity

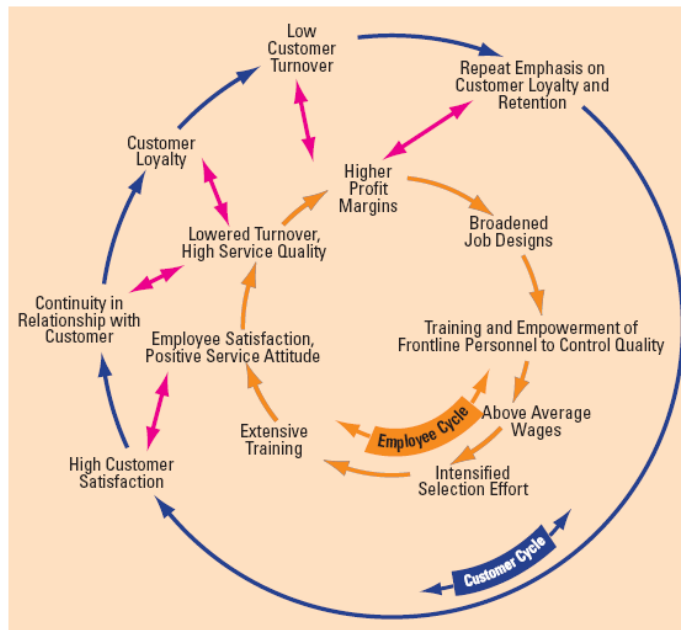


### SOURCE

Christopher Lovelock (1995). *Managing services: The human factor*. In W.J. Glynn and J.G. Barnes. *Understanding Service Management* (p. 228). Chichester, UK: John Wiley.

- Most commonly found in large, bureaucratic organizations that are frustrating to deal with
- Service delivery is oriented towards
  - Standardized service
  - Operational efficiencies
  - Promotions with long service
  - Rule-based training
  - Narrow and repetitive jobs
  - Successful performance measured by absence of mistakes
- Little incentive for customers to cooperate with organizations to achieve better service
- Complaints are often made to already unhappy employees
- Customers often stay because of lack of choice

## Cycle of Success



### SOURCE

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- Longer-term view of financial performance; firm seeks to prosper by investing in people
- Attractive pay and benefits attract better job applicants
- More focused recruitment, intensive training, and higher wages make it more likely that employees are:
  - Happier in their work
  - Proved higher quality, customer-pleasing service
- Broadened job descriptions with empowerment practices enable frontline staff to control quality, facilitate service recovery
- Regular customers more likely to remain loyal because they:
  - Appreciate continuity in service relationships
  - Have higher satisfaction due to higher quality

# Human Resources Management – How to get it right

## The Service Talent Cycle



## Hire the Right People

The old saying 'People are your most important asset' is wrong.

The **RIGHT** people are your most important asset.

Jim Collins

## Be the Preferred Employer

- Create a large pool: "Compete for Talent Market Share"
- Select the right people:
  - Different jobs are best filled by people with different skills, styles, or personalities
  - Hire candidates that fit firm's core values and culture
  - Focus on recruiting naturally warm personalities for customer-contact jobs

## Tools to Identify Best Candidates

- Employ multiple, structured interview
  - Use structured interview built around job requirements
  - Use more than one interviewer to reduce "similar to me" biases
- Observe behavior
  - Hire based on observed behavior, not words you hear
  - Best predictor of future behavior is past behavior
  - Consider group hiring sessions where candidates are given group tasks
- Conduct personality tests
  - Willingness to treat co-workers and customers with courtesy, consideration, and tact
  - Perceptiveness regarding customer needs

- Ability to communicate accurately and pleasantly
- Give applicants a realistic preview of the job
  - Chance for candidates to “try on the job”
  - Assess how candidates respond to job realities
  - Allow candidates to self-select themselves out of the job
  - Manage new employees’ expectation of job

### **Train Service Employees**

#### **Service employees need to learn:**

- Organizational culture, purpose, and strategy
  - Promote core values, get emotional commitment to strategy
  - Get managers to teach “why”, “what”, and “how” of job
- Interpersonal and technical skills
- Product/service knowledge
  - Staff’s product knowledge is a key aspect of service quality
  - Staff must explain product features and position products correctly

### **Is Empowerment Always Appropriate?**

- Empowerment is most appropriate when:
  - Firm’s business strategy is based on personalized, customized service, and competitive differentiation
  - Emphasis on extended relationship rather than short-term transactions
  - Use of complex and non-routine technologies
  - Service failures are non-routine
  - Business environment is unpredictable
  - Managers are comfortable letting employees work independently for benefit of firm and customers
  - Employees seek to deepen skills and have good interpersonal and group process skills

### **Control vs. Involvement**

- Empowerment systematically redistributes the following:
  - Information about operating results and measures of competitive performance
  - Knowledge/skills that enable employees to understand and contribute to organizational performance
  - Power to influence work procedures and organizational direction (e.g., quality circles, self-managing teams)
  - Rewards based on organizational performance (e.g., bonuses, profit sharing, stock ownership)
- The Control model concentrates these elements at the top of the organization whereas the Involvement model pushes these features throughout the organization

## Levels of Employee Involvement



## Build High-Performance Service Delivery Teams

- The Power of Teamwork in Services
  - Facilitate communication among team members and knowledge sharing
  - Higher performance targets
  - Pressure to perform is high
- Creating Successful Service Delivery Teams
  - Emphasis on cooperation, listening, coaching, and encouraging one another
  - Understand how to air differences, tell hard truths, ask tough questions
  - Management needs to set up a structure to steer teams toward success

## Motivate and Energize the Frontline

- Use full range of available rewards effectively, including:
  - Job content
    - People are motivated knowing they are doing a good job
  - Feedback and recognition
    - People derive a sense of identity and belonging to an organization from feedback and recognition
  - Goal accomplishment
    - Specific, difficult but attainable, and accepted goals are strong motivators

## Role of Labor Unions

- Challenge is to work jointly with unions, reduce conflicts, and create a service climate
- Labor unions and service excellence are sometimes seen as incompatible, yet many of the world's most successful service businesses are highly unionized (e.g., Southwest Airlines)
- Management consultation and negotiation with union representatives are essential if employees are to accept new ideas

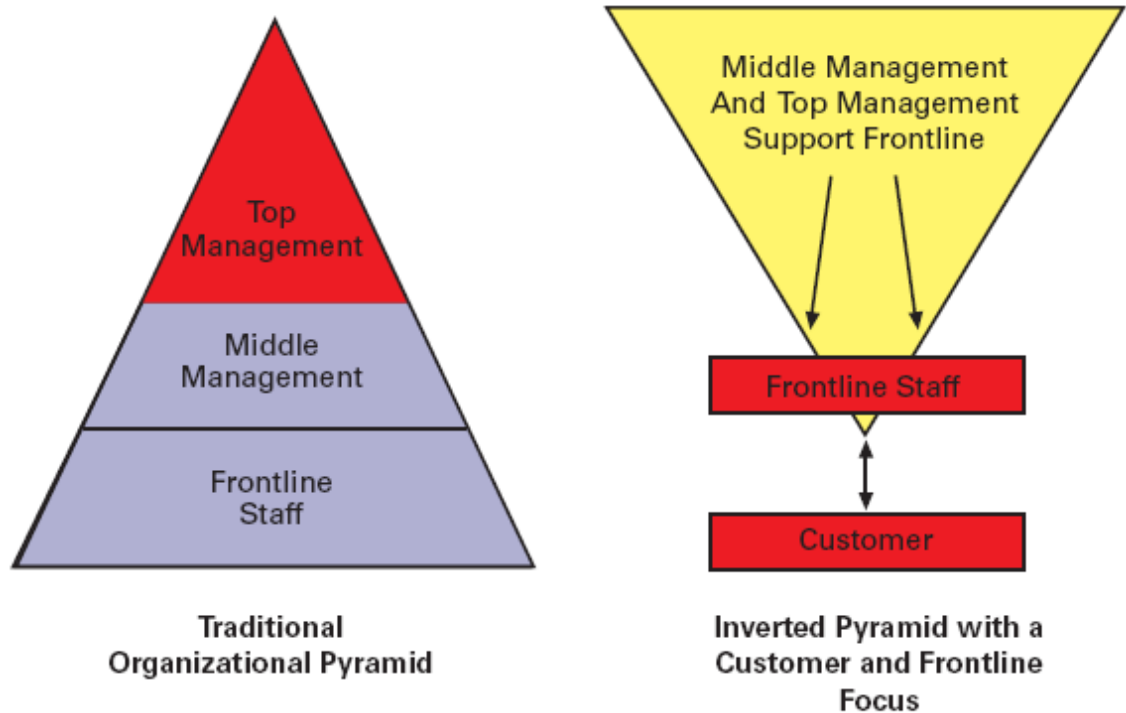
## Service Leadership and Culture

- Charismatic/transformational leadership:
  - Change frontline personnel's values and goals to be consistent with the firm
  - Motivate staff to perform at their best
- Service culture can be defined as:
  - Shared perceptions of what is important
  - Shares values and beliefs of why they are important

**A strong service culture focuses the entire organization on the frontline, with the top management informed and actively involved**

## The Inverted Organizational Pyramid

Summar



Legend:  $\updownarrow$  = Service encounters, or "Moments of Truth"

## Internal Marketing

- Necessary in large service businesses that operate in widely dispersed sites
- Effective internal marketing helps to:
  - Ensure efficient and satisfactory service delivery
  - Achieve harmonious and productive working relationship
  - Build employee trust, respect, and loyalty

## Summary

- Service employees are crucially important to firm's success
  - Source of customer loyalty and competitive advantage
- Frontline work is difficult and stressful; employees are boundary spanners, undergo emotional labor, face a variety of conflicts
- Understand cycles of failure, mediocrity, and success
- Know how to get HRM aspect right
  - Hire the right people
  - Identify the best candidate
  - Train service employees actively
  - Empower the frontline
  - Build high-performance service delivery teams
  - Motivate and energize people
  - Unions have a role to play
- Understand role of service culture and service leadership in sustaining service excellence

## Chapter 12: Managing Customer Relationship & Building Loyalty

### The Search for Customer Loyalty

#### How Much Profit a Customer Generates Over Time



#### SOURCE

Based on reanalysis of data from Reichheld, FR., Sasser Jr., W.E., (1990). Zero defections: quality comes from services. *Harvard Business Review*, 68 (September–October), pp. 105–111.

## Why Customers are More Profitable over Time

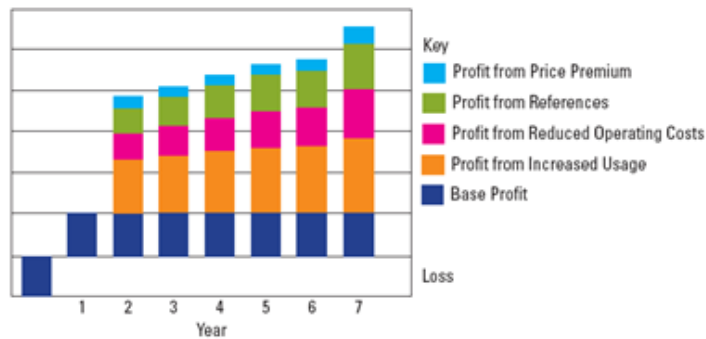


Figure 12.3 Why customers become profitable over time.

### SOURCE

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## Why is Customer Loyalty Important to a Firm's Profitability?

- Customers become more profitable the longer they remain with a firm:
  - Increased purchase and/or account balances
    - Customers/families purchase in greater quantities as they grow
  - Reduced operating costs
    - Fewer demands from suppliers and operating mistakes as customer becomes experienced
  - Referrals to other customers
    - Positive word-of-mouth saves firms from investing money in sales and advertising
  - Price premiums
    - Long-term customers willing to pay regular price
    - Willing to pay higher price during peak periods

## Assessing the Value of a Loyal Customer

- Must not assume that loyal customers are always more profitable than those making one-time transactions
  - Costs
    - Not all types of services incur heavy promotional expenditures to attract a new customer
    - Walk-in traffic more important at times
  - Revenue
    - Large customers may expect price discounts in return for loyalty
    - Revenues don't necessarily increase with time for all types of customers
- Profit impact of a customer varies according to stage of service in product life cycle
  - E.g., referrals and negative word-of-mouth have a higher impact in early stages
- Tasks:
  - Determine costs and revenues for customers from different market segments at different points in their customer lifecycles

- Predict future profitability

### Measuring Customer Equity: Lifetime Value of Each Customer

- Acquisition revenues less costs
  - Revenues (application fee + initial purchase)
  - Costs (marketing + credit check + account set up)
- Projected annual revenues and costs
  - Revenues (annual fee + sales + service fees + value referrals)
  - Costs (account management + cost of sales + write-offs)
- Value of referrals
  - Percentage of customers influenced by other customers
  - Other marketing activities that drew the firm to an individual's attention
- Net Present Value
  - Sum anticipated annual values (future profits)
  - Suitably discounted each year into the future

### Gap between Actual and Potential Customer Value

- What is actual purchasing behavior of customers in each target segment?
- What would be impact on sales and profits if they:
  - Buy all services offered by the firm,
  - Use these to the exclusion of any purchases from competitors,
  - Pay full price?
- How long, on average, do customers remain with firm?
- What impact would it have if they remained customers for life?

### Why Are Customers Loyal? (Service Insights 12.1)

- Customers stay loyal when we create value for them
- Value can be created for customers through:
  - Confidence
    - Confidence in correct performance
    - Ability to trust the provider
    - Lower anxiety when purchasing
    - Knowing what to expect and receive
  - Social benefits
    - Mutual recognition and friendship
  - Special treatment
    - Better price
    - Discounts not available to most customers
    - Extra services
    - Higher priority when there is a wait

## Understanding the Customer-Firm Relationship

### Transactional Marketing

- Transactional Marketing
  - One transaction or a series of transactions does not necessarily constitute a relationship
  - Requires mutual recognition and knowledge between the parties

### Relationship Marketing

- Marketing that creates **extended relationship** with customers
- Database Marketing:
  - Includes market transaction and information exchange
  - Technology is used to
    1. Identify and build database of current and potential customers
    2. Deliver differentiated messages based on customers' characteristics
    3. Track each relationship to monitor cost of acquiring that customer and lifetime value of resulting purchases
- Interaction Marketing:
  - Face-to-face interaction between customers and supplier's representatives
  - Value is added by people and social processes
  - Increasing use of technologies make maintaining relationships with customers a challenge
    - e.g., self-service technology, interactive website, call centers
- Network Marketing:
  - Common in B2B context
  - Companies commit resources to develop positions in a network

### Relationship with Customers

#### Type of Relationship between the Service Organization and its Customers

Nature of Service Delivery	Membership Relationship	No Formal Relationship
<b>Continuous</b>	<ul style="list-style-type: none"><li>• Cable TV</li><li>• Insurance Policy</li><li>• College enrollment</li></ul>	<ul style="list-style-type: none"><li>• Radio Station</li><li>• Police</li><li>• Lighthouse</li></ul>
<b>Discrete Transactions</b>	<ul style="list-style-type: none"><li>• Subscriber phone</li><li>• Theater subscription</li><li>• Warranty repair</li></ul>	<ul style="list-style-type: none"><li>• Pay Phone</li><li>• Movie Theatre</li><li>• Public Transport</li></ul>

## The Wheel of Loyalty

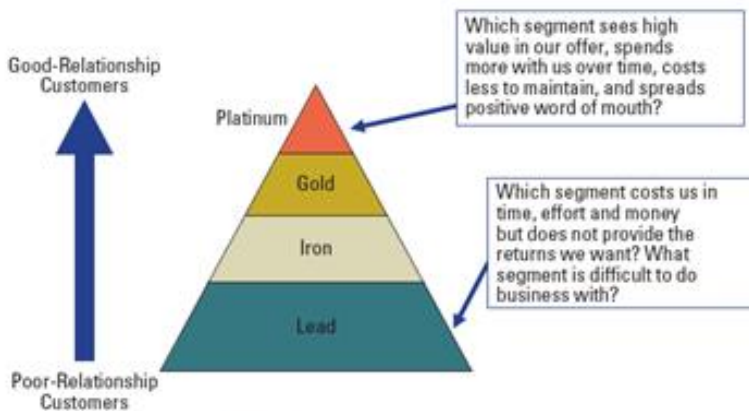


## Building a Foundation for Loyalty

### Targeting the Right Customers

- Target the right customer
  - How do customer needs relate to operations elements?
  - How can service personnel meet expectations of different customers?
  - Can company match or exceed competing services that are directed at same types of customers?
- Focus on number of customers served and value of each customer
  - Some customers more profitable than others in the short term
  - Others may have room for long-term growth
- “Right customers” are not always high spenders
  - Can be a large group of people that no other supplier is serving well

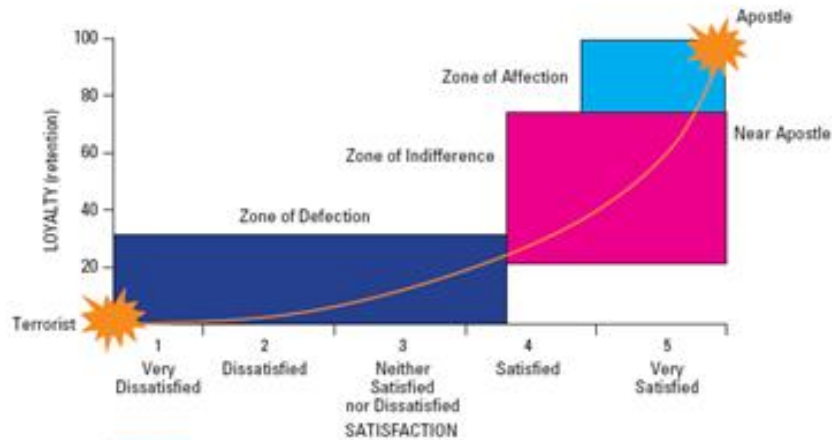
## Effective Tiering of Service – The Customer Pyramid



**SOURCE**

Zeithaml, V. A., Rust, R. T., & Lemon, K. N. (2001). The customer pyramid: Creating and serving profitable customers. *California Management Review*, 43(4), (Summer), pp. 118–142.

## The Customer Satisfaction – Loyalty Relationship



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### SOURCE

Reprinted by permission of Harvard Business Review. From why satisfied customers defect. By Jones, T. D. & Sasser Jr., W. E. (November-December), p. 91. Copyright © 1995 by the Harvard Business School Publishing Corporation; all rights reserved.

## Strategies for Building Loyalty Bonds with Customers

### Strategies for Developing Loyalty Bonds with Customers

- Deepening the relationship
  - Bundling/Cross-selling services makes switching a major effort that customer is unwilling to undertake
  - Customers benefit from consolidating their purchasing of various services from the same provider
    - One-stop-shopping, potentially higher service levels
    - Higher service tiers, etc.
- Reward Based Bonds: Incentives that offer rewards based on frequency of purchase, value of purchase, or combination of both
  - Financial bonds
    - Discounts on purchases, loyalty program rewards (e.g., frequent flyer miles), cash-back programs
  - Non-financial rewards
    - Priority to loyalty program members for waitlists and queues in call centers; higher baggage allowances, priority upgrading
  - Intangible rewards
    - Special recognition and appreciation, tiered loyalty programs
- Reward-based loyalty programs are relatively easy to copy and rarely provide a sustained competitive advantage
- Social Bonds
  - Based on personal relationships between providers and customers
  - Harder to build and imitate and thus, better chance of retention in the long term
- Customization Bonds

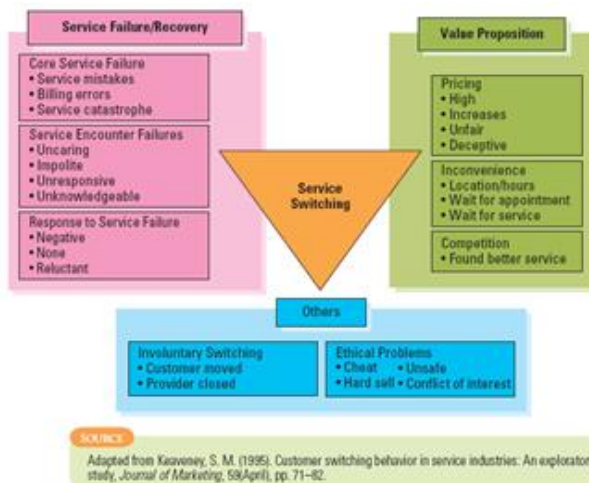
- Customized service for loyal customers
  - E.g., Starbucks
- Customers may find it hard to adjust to another service provider who cannot customize service
- Structural Bonds
  - Mostly seen in B2B settings
  - Align customers' way of doing things with supplier's own processes
    - Joint investments in projects and sharing of information, processes and equipment
  - Can be seen in B2C environment too
    - Airlines – SMS check-in, SMS E-mail alerts for flight arrival and departure times
  - Difficult for competition to draw customers away when they have integrated their way of doing things with existing supplier

## Strategies for Reducing Customer Defections

### Analyze Customer Defections and Monitor Declining Accounts

- Understand reasons for customer switching
- Churn Diagnostics
  - Analysis of data warehouse information on churned and declining customers
  - Exit interviews:
    - Ask a short set of questions when customer cancels account; in-depth interviews of former customers by third party agency
  - Churn Alert Systems:
    - Monitor activity in individual customer accounts to predict impending customer switching
    - Proactive detention efforts – send voucher, customer service representatives calls customer

### What Drives Customers to Switch?



## Addressing Key Churn Drivers

- Delivery quality
- Minimize inconvenience and non-monetary costs
- Fair and transparent pricing
- Industry specific drivers
  - Cellular phone industry: handset replacement a common reason for subscribers discontinuing services – offer proactive handset replacement programs
- Reactive measures
  - Save teams

## Other Ways to Reduce Churn

- Implement Effective Complaint Handling and Service Recovery Procedures
- Increase Switching Costs
  - Natural switching costs
    - E.g., Changing primary bank account – many related services tied to account
  - Can be created by instituting contractual penalties for switching
    - Must be careful not to be perceived as holding customers hostage
    - High switching barriers and poor service quality likely to generate negative attitudes and word of mouth

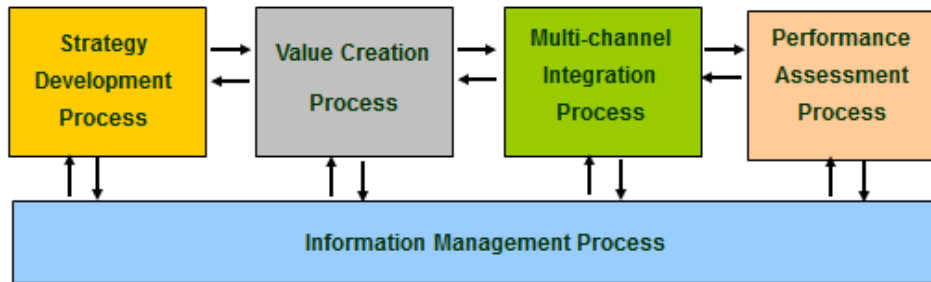
## CRM: Customer Relationship Management

### Objectives of CRM Systems

- Data collection
  - Customer data such as contact details, demographics, purchasing history, service preferences
- Data analysis
  - Data captured in analyzed and categorized
  - Used to tier customer base and tailor service delivery accordingly
- Sales force automation
  - Sales leads, cross-sell and up-sell opportunities effectively identified and processed
  - Track and facilitate entire sales cycle
- Marketing automation
  - Mining of customer data enables the firm to target its market
  - Goal to achieve one-to-one marketing and cost savings
  - Results in increasing the ROI on its marketing expenditure
  - Enables the assessment of the effectiveness of marketing campaigns through the analysis of responses
- Call center automation
  - Call center staff have customer information at their fingertips resulting in improved service levels to customers

- Caller ID and account numbers allow call centers to identify the customer tier the caller belongs to, and to tailor the service accordingly

### Integrated Framework for CRM Strategy



#### CRM: Strategy Development

- Responsibility to top management
- Used to guide the development for the customer strategy
- Assessment of business strategy

#### CRM: Value Creation

- Translates business and customer strategies into specific value propositions for both customers and firm
  - Customers benefit from priority, tiered services, loyalty rewards, and customization
  - Company benefits from reduced customer acquisition and retention costs, and increased share-of-wallet
- Dual creation of value: customers need to participate in CRM to reap value from firm's CRM initiatives

#### CRM: Multi-Channel Integration

- Serve customers well across many potential interfaces
- Offer a unified interface that delivers customization and personalization

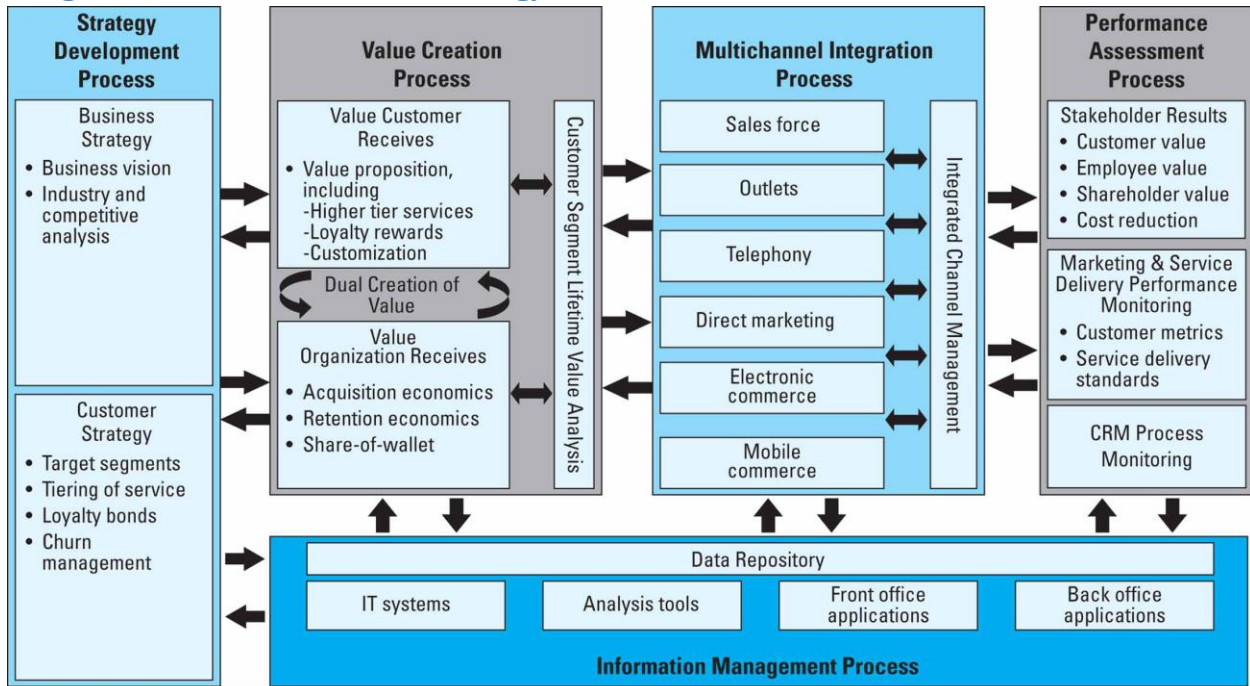
#### CRM: Performance Assessment

- Is CRM system creating value for key stakeholders?
- Are marketing and service standards objectives being achieved?
- Is CRM system meeting performance standards?

#### CRM: Information Management

- Collect customer information from all channels
- Integrate it with other relevant information
- Make useful information available to the frontline
- Create and manage data repository, IT systems, analytical tools, specific application packages

## Integrated Framework for CRM Strategy



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## Common Failures in CRM Implementation

- Service firms often equate installing CRM systems with having a customer relationship strategy
- Common reasons for failures
  - Viewing CRM as a technology initiative
  - Lack of customer focus
  - Insufficient appreciation of customer lifetime value (CLV)
  - Inadequate support from top management
  - Failure to reengineer business processes
  - Underestimating the challenges in data integration

## Defining a CRM Strategy

- How should our value proposition change to increase customer loyalty?
- How much customization or one-to-one marketing and service delivery is appropriate and profitable?
- What is incremental profit of increasing share-of-wallet with current customers? How much does this vary by customer tier and/or segment?
- How much time and resources can we allocate to CRM right now?
- If we believe in customer relationship management, why haven't we taken more steps in that direction in the past?
- What can we do today to develop customer relationships without spending on technology?

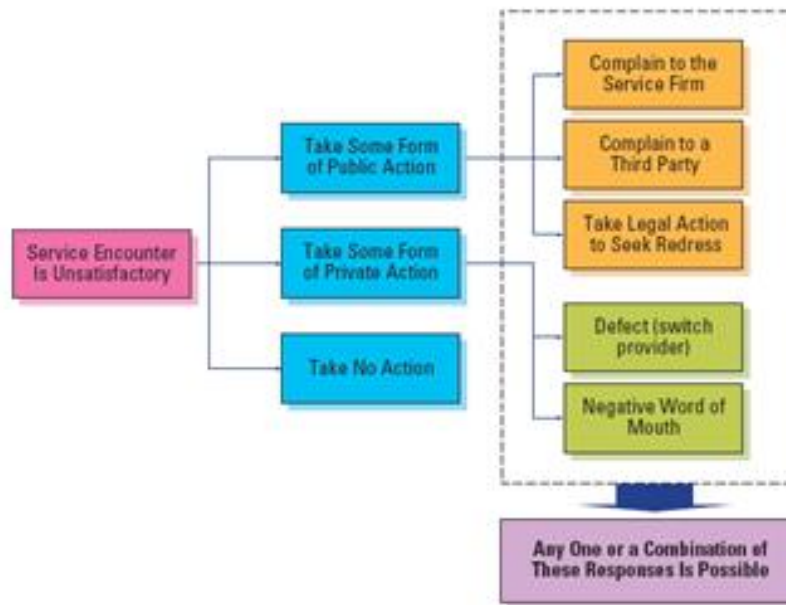
## Summary

- Customer loyalty is an important driver of profitability so firms need to assess lifetime customer value and narrow gap between actual and potential value
- Building a foundation of loyalty involves
  - Good fit between customer needs and capabilities
  - Tiering services effectively
  - Obtaining customer satisfaction through service quality
- Customer loyalty bonds include
  - Reward-based, social, customization, and structural bonds
  - Created through membership and loyalty programs
- Strategies for reducing customer defections include
  - Analyzing customer defections and monitoring declining accounts
  - Addressing key churn drivers, increasing switching costs
  - Implementing effective complaint-handling and service recovery procedures
- A successful CRM program requires understanding of common failures while including the following processes
  - Strategy development process
  - Value creation process
  - Multichannel integration process
  - Performance assessment process

## Chapter 13: Complaint Handling and Service Recovery

### Customer Complaining Behavior

#### Customer Response Categories to Service Failures



#### Understanding Customer Responses to Service Failure

- Why do customers complain?
  - Obtain compensation
  - Vent their anger
  - Help to improve the service
  - Altruistic reasons
- What proportion of unhappy customers complain?
- Why don't unhappy customers complain?
- Who is most likely to complain?
- Where do customers complain?
- What do customers expect once they have made a complaint?
  - Procedural, interactional, and outcome justice

## Three Dimensions of Perceived Fairness in Service Recovery



## Customer Responses to Effective Service Recovery

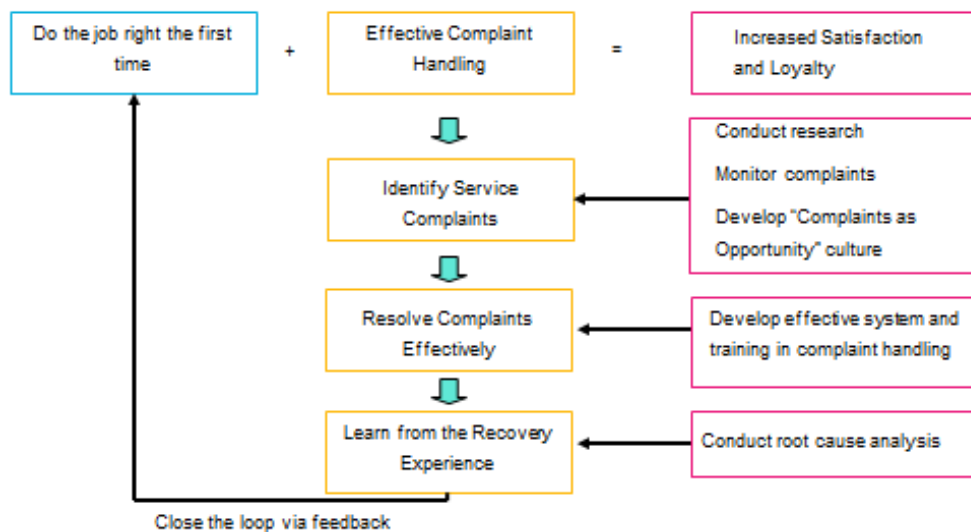
### Service Recovery

- Service Recovery
  - Plays a crucial role in achieving customer satisfaction by testing a firm’s commitment to satisfaction and service quality
  - Impacts customer loyalty and future profitability
  - Severity and “recoverability” of failure (e.g., spoiled wedding photos) may limit firm’s ability to delight customer with recovery efforts
- Service Recovery Paradox: Customers who experience a service failure that is satisfactorily resolved may be more likely to make future purchases than customers without problems
  - If second service failure occurs, the paradox disappears

**Best Strategy: Do it Right the First Time**

## Principles of Effective Service Recovery Systems

### Components of an Effective Service Recovery System



## Strategies to Reduce Customer Complaint Barriers

Complaint Barriers for Dissatisfied Customers	Strategies to Reduce These Barriers
<b>Inconvenience</b> <ul style="list-style-type: none"> <li>• Hard to find the right complaint procedure</li> <li>• Effort involved in complaining</li> </ul>	<b>Make Feedback Easy and Convenient</b> <ul style="list-style-type: none"> <li>• Put customer service hotline numbers, e-mail and postal addresses on all customer communications materials</li> </ul>
<b>Doubtful Pay Off</b> <ul style="list-style-type: none"> <li>• Uncertain if action will be taken by the firm to address the problem</li> </ul>	<b>Assure that Feedback is Taken Seriously</b> <ul style="list-style-type: none"> <li>• Have service recovery procedures in place, communicate this to customers</li> <li>• Feature service improvements based on customer feedback</li> </ul>
<b>Unpleasantness</b> <ul style="list-style-type: none"> <li>• Fear of being treated rudely</li> <li>• Hassle, embarrassment</li> </ul>	<b>Make Feedback Experience Positive</b> <ul style="list-style-type: none"> <li>• Thank customers for their feedback</li> <li>• Train frontline employees not to hassle</li> <li>• Allow anonymous feedback</li> </ul>

## How to Enable Effective Service Recovery

- Methods: (See *Service Perspectives 13.1*)
  - Be proactive – on the spot, before customer complain
  - Plan recovery procedures
  - Teach recovery skills to relevant personnel
  - Empower personnel to use judgment and skills to develop recovery solutions
- Rules of Thumb for Adequate Compensation:
  - What is positioning of our firm?
  - How severe was the service failure?
  - Who is the affected customer?

## Service Guarantees

### Service Guarantees Help Promote and Achieve Service Loyalty

- Force firms to focus on what customers want
- Set clear standards
- Highlight cost of service failures
- Help firm identify and overcome fail points
- Reduce the risk of purchase decision and build long-term loyalty

### How to Design Service Guarantees

- Unconditional
- Easy to understand and communicate
- Meaningful to the customer
- Easy to invoke
- Easy to collect on
- Credible

## Types of Service Guarantees

Single attribute-specific guarantee	Multi-attribute-specific guarantee	Full-satisfaction guarantee	Combined guarantee
<ul style="list-style-type: none"> <li>• Explicit minimum performance standard on one important attribute is guaranteed (e.g., delivery by noon the next day)</li> </ul>	<ul style="list-style-type: none"> <li>• Explicit minimum performance standard on a few important attributes is guaranteed</li> </ul>	<ul style="list-style-type: none"> <li>• All service aspects are guaranteed to be delivered to the full satisfaction of the customer with no exceptions or conditions attached</li> </ul>	<ul style="list-style-type: none"> <li>• All service aspects are guaranteed (as for full-satisfaction guarantee)</li> <li>• Explicit minimum performance standards on important attributes are guaranteed (as for multi-attribute-specific guarantee)</li> </ul>

### Is it Always Suitable to Introduce a Guarantee?

- It may not be appropriate to introduce guarantees when
  - Companies have a strong reputation for service excellence
  - Company does not have good quality level
  - Quality cannot be controlled because of external forces
  - Consumers see little financial, personal, or physiological risk associated with the purchase

## Discouraging Abusive and Opportunistic Customer Behavior

### Addressing the Challenge of Jaycustomers

- Jaycustomer: a customer who behaves in a thoughtless or abusive fashion, causing problems for the firm, its employees, and other customers
- More potential for mischief in service businesses, especially when many customers are present
- No organization wants an ongoing relationship with an abusive customer

### Seven Types of Jaycustomers

#### *The Cheat:*

- Thinks of various ways to cheat the firm

#### *The Thief:*

- No intention of paying – sets out to steal or pay less
  - Services lend themselves to clever schemes to avoid payment

- E.g., bypassing electricity meters, circumventing TV cables, riding free on public transportation
- Firms must take preventive actions against thieves, but make allowances for honest but absent-minded customers

### *The Rulebreaker*

- Rules guide customers safely through the service encounter
  - Government agencies may impose rules for health and safety reasons
  - Some rules protect other customers from dangerous behavior
    - E.g., ski patrollers issue warnings to reckless skiers by attaching orange stickers on their lift tickets
- Ensure company rules are necessary, should not be too much or inflexible

### *The Belligerent*

- Should loudly, maybe mouthing insults, threats, and curses
  - Service personnel are often abused even when they are not to be blamed
  - Confrontations between customers and service employees can easily escalate
- Firms should ensure employees have skills to deal with difficult situations

### *Family Feuders*

- People who get into arguments with other customers – often members of their own family

### *The Vandal*

- Service vandalism includes pouring soft drinks into bank cash machines, slashing bus seats, breaking hotel furniture
  - Sources: bored and drink young people, and unhappy customers who feel mistreated by service providers take revenge
  - Prevention is the best cure

### *The Deadbeat*

- Customers who fail to pay (as distinct from “thieves” who never intended to pay in the first place)
  - Preventive action is better than cure – e.g., insisting on prepayment; asking for credit card number when order is taken
  - Customers may have good reasons for not paying
    - If the client’s problems are only temporary ones, consider long-term value of maintaining the relationship

### **Consequences of Dysfunctional Customer Behavior**

- Employees:
  - Mood or temper negatively affected
  - Long-term psychological damage
  - Staff morale will fall, affecting productivity
- Other customers:

- Positive – rally to support an employee who is perceived to be abused
- Negative – contagious bad behavior might escalate the situation

### Dealing with Customer Fraud

- Treating all customer with suspicion is likely to alienate them
  - TARP found only 1-2% of customer base engages in premeditated fraud – so why treat the remaining 98% of honest customer as potential crooks?
  - But, records need to be kept to investigate repeat claimers
- Insights from research on guarantee cheating:
  - Amount of a guarantee payout had no effect on customer cheating
  - Repeat-purchase intention reduced cheating intent
  - Customers are reluctant to cheat if service quality is high

### Summary

- When customer are dissatisfied, they can
  - Take some form of public action, private action, or no action
- Firms then need to understand customer complaining behaviors and motivations to handle the complaint along the three dimensions of fairness
- Effective service recovery can lead to customer loyalty via the service recovery paradox
  - It does not always hold true – better to get it right the first time
- Guiding principles for effective service recovery include
  - Make it easy for customers to give feedback
  - Enable effective service recovery
  - Focusing on how generous compensation should be
  - Dealing with complaining customer
- Service guarantees are power tools in delivering satisfaction but discretion should be used
- To discourage abuse and opportunistic behavior, we need to deal with customer fraud

## Chapter 14: Improving Service Quality and Productivity

### Integrating Service Quality and Productivity Strategies

- Quality and productivity create value for customers and companies
- Quality focuses on the benefits created for customers; productivity addresses financial costs incurred by firm
- Importance of productivity:
  - Keep costs down to improve profits and/or reduce prices
  - Enable firms to spend more on improving customer service and supplementary services
  - Secure firm's future through increase spending on R&D
  - May impact service experience

## What is Service Quality?

### Different Perspectives of Service Quality

#### Transcendent:

- Quality = Excellence. Recognized only through experience

#### Manufacturing-based:

- Quality is in conformance to the firm's developed specifications

#### User-based:

- Quality lies in the eyes of the beholder

#### Value-based:

- Quality is a trade-off between price and value

### Dimensions of Service Quality

#### Tangibles

- Appearance of physical elements

#### Reliability

- Dependable and accurate performance

#### Responsiveness

- Promptness; helpfulness

#### Assurance

- Competence, courtesy, credibility, security

#### Empathy

- Easy access, good communication, understanding of customer

# The Gaps Model

## Six Service Quality Gaps

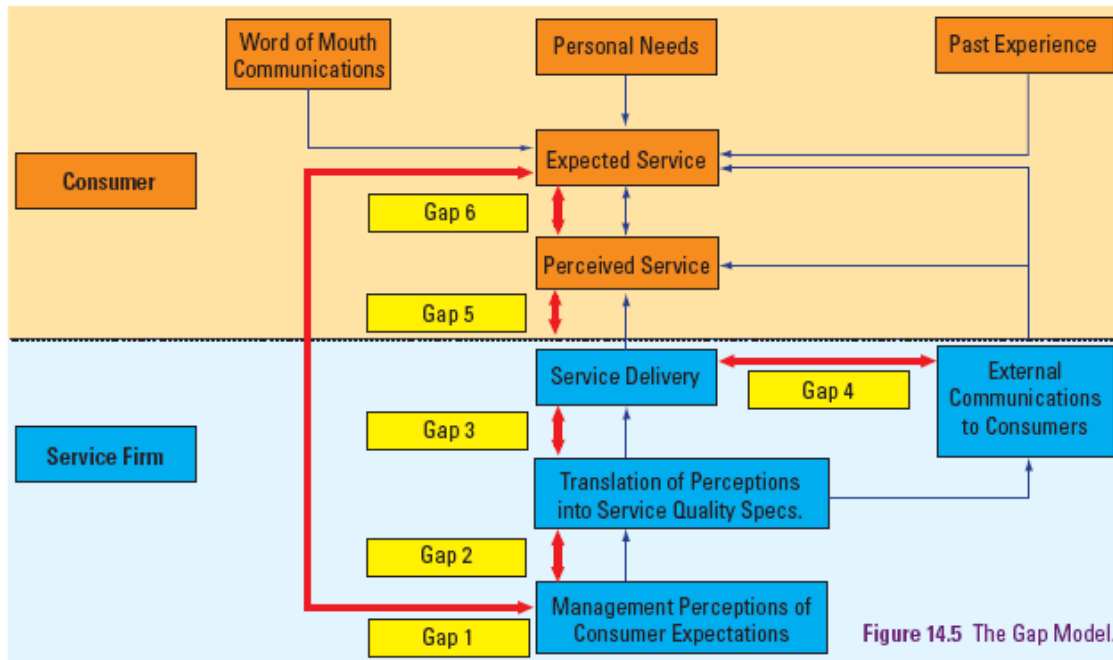


Figure 14.5 The Gap Model.

**SOURCE**

Adapted from the original 5-gaps model developed by Parasuraman, A., Zeithaml, V. A., & Berry, L. L. (1985). A conceptual model of service quality and its implications for future research. *Journal of Marketing* 49, (Fall), pp. 41–50; Zeithaml, V. A., Bitner, M. J., & Gremler, D. (2006). *Services Marketing: Integrating Customer Focus Across the Firm* (p. 46.). NY: McGraw Hill/Irwin. A further gap (Gap 5) was added by Christopher Lovelock (1994), *Product Plus* (p. 112). NY: McGraw Hill.

## Suggestions for Closing the Six Service Quality Gaps

Types of Quality Gap	Proposed Solutions
<b>Gap 1—The Knowledge Gap</b>	<p><i>Educate Management About What Customers Expect</i></p> <ul style="list-style-type: none"> <li>• Sharpen market research procedures, including questionnaire and interview design, sampling, and field implementation, and repeat research studies once in a while</li> <li>• Implement an effective customer feedback system that includes satisfaction research, complaint content analysis and customer panels</li> <li>• Increase interactions between customers and management</li> <li>• Facilitate and encourage communication between front-line employees and management</li> </ul>
<b>Gap 2—The Policy Gap</b>	<p><i>Establish the Right Service Processes and Specify Standards</i></p> <ul style="list-style-type: none"> <li>• Get the customer service processes right:               <ul style="list-style-type: none"> <li>○ Use a rigorous, systematic, and customer-centric process for designing and redesigning customer service processes.</li> <li>○ Standardize repetitive work tasks to ensure consistency and reliability by substituting hard technology for human contact and improving work methods (soft technology).</li> </ul> </li> <li>• Develop tiered service products that meet customer expectations:               <ul style="list-style-type: none"> <li>○ Consider premium, standard and economy-level products to allow customers to self-segment according to their needs, or</li> <li>○ Offer customers different levels of service at different prices</li> </ul> </li> <li>• Set, communicate and reinforce measurable customer-oriented service standards for all work units:               <ul style="list-style-type: none"> <li>○ Establish for each step in service delivery a set of clear service quality goals that are challenging, realistic and explicitly designed to meet customer expectations.</li> <li>○ Ensure that employees understand and accept goals, standards, and priorities</li> </ul> </li> </ul>

Types of Quality Gap	Proposed Solutions
<b>Gap 3—The Delivery Gap</b>	<p><i>Ensure that Performance Meets Standards and that Customers Understand the Quality Level Delivered</i></p> <ul style="list-style-type: none"> <li>• Ensure that customer service teams are motivated and able to meet service standards:               <ul style="list-style-type: none"> <li>○ Improve recruitment with a focus on employee-job fit; select employees for the abilities and skills needed to perform their job well.</li> <li>○ Train employees on the technical and soft skills needed to perform their assigned tasks effectively, including interpersonal skills, especially for dealing with customers under stressful conditions.</li> <li>○ Clarify employee roles and ensure that employees understand how their jobs contribute to customer satisfaction; teach them about customer expectations, perceptions and problems.</li> <li>○ Build cross-functional service teams that can offer customer-centric service delivery and problem resolution.</li> <li>○ Empower managers and employees in the field by pushing decision-making power down the organization.</li> <li>○ Measure performance; provide regular feedback and reward customer service team performance as well as individual employees and managers on attaining quality goals.</li> </ul> </li> <li>• Install the right technology, equipment, support processes and capacity:               <ul style="list-style-type: none"> <li>○ Select the most appropriate technologies and equipment for enhanced performance.</li> <li>○ Ensure that employees working on internal support jobs provide good service to their own internal customer, the front-line personnel.</li> <li>○ Balance demand against productive capacity.</li> </ul> </li> <li>• Manage customers for service quality:               <ul style="list-style-type: none"> <li>○ Educate customers so that they can perform their roles and responsibilities in service delivery effectively.</li> </ul> </li> </ul>

Types of Quality Gap	Suggest Solutions
<b>Gap 4—The Communications Gap</b>	<p><i>Close the Internal Communications Gap by ensuring that Communications Promises are Realistic and Correctly understood by Customers</i></p> <ul style="list-style-type: none"> <li>• Educate managers responsible for sales and marketing communications about operational capabilities: <ul style="list-style-type: none"> <li>○ Seek inputs from front-line employees and operations personnel when new communications programs are being developed.</li> <li>○ Let service providers preview advertisements and other communications before customers are exposed to them.</li> <li>○ Get sales staff to involve operations staff in face-to-face meetings with customers.</li> <li>○ Develop internal educational and motivational advertising campaigns to strengthen understanding and integration among the marketing, operations, and human resource functions, and to standardize service delivery across different locations.</li> </ul> </li> <li>• Ensure that communications content sets realistic customer expectations.</li> <li>• Be specific with promises and manage customers' understanding of communication content: <ul style="list-style-type: none"> <li>○ Pretest all advertising, brochures, telephone scripts and web site content prior to external release to see if target audience interpret them as the firm intends (if not, revise and retest). Make sure that the advertising content reflects those service characteristics that are most important to customers. Let them know what is not possible and why.</li> <li>○ Identify and explain in real time the reasons for shortcomings in service performance, highlighting those that cannot be controlled by the firm.</li> <li>○ Document beforehand the tasks and performance guarantees that are included in an agreement or contract. After the completion of the work, explain what work was performed in relation to a specific billing statement.</li> </ul> </li> </ul>

Types of Quality Gap	Suggest Solutions
<b>Gap 5—The Perception Gap</b>	<p><i>Tangibilize and Communicate the Service Quality Delivered</i></p> <ul style="list-style-type: none"> <li>• Make service quality tangible and communicate the service quality delivered: <ul style="list-style-type: none"> <li>○ Develop service environments and physical evidence cues that are consistent with the level of service provided.</li> <li>○ For complex and credence services, keep customers informed during service delivery on what is being done, and give briefings after the delivery so that customers can appreciate the quality of service they received.</li> <li>○ Provide physical evidence (e.g. for repairs, show customers the damaged components that were removed).</li> </ul> </li> </ul>
<b>Gap 6—The Service Gap</b>	<p>Close Gaps 1 to 5 to consistently meet Customer Expectations Gap 6 is the accumulated outcome of all the preceding gaps. It will be closed when Gaps 1 to 5 have been addressed.</p>

## Measuring and Improving Service Quality

### Measure of Service Quality

Soft Measures	Hard Measures
<ul style="list-style-type: none"> <li>• Not easily observed, must be collected by talking to customers, employees or others</li> <li>• Provide direction, guidance and feedback to employees on ways to achieve</li> </ul>	<ul style="list-style-type: none"> <li>• Can be counted, timed, or measured through audits</li> <li>• Typically operational processes or outcomes</li> </ul>

- customer satisfaction
- Can be quantified by measuring customer perceptions and beliefs
- E.g., SERVQUAL, surveys, and customer advisory panel
- Standards often set with reference to percentage of occasions on which a particular measure is achieved

## Learning from Customer Feedback

### Key Objectives of Customer Feedback Systems

- Assessment and benchmarking of service quality and performance
- Customer-driven learning and improvements
- Creating a customer-oriented service culture

### Customer Feedback Collection Tools



### Strengths and Weaknesses of Customer Feedback Collection Tools

COLLECTION TOOLS	LEVEL OF MEASUREMENT				REPRESENTATIVE/ RELIABLE	POTENTIAL FOR SERVICE RECOVERY	FIRST HAND LEARNING	COST EFFECTIVENESS
	FIRM	PROCESS	TRANSACTION SPECIFIC	ACTIONABLE				
Total Market Survey (Incl. Competitors)	●	○	○	○	●	○	○	○
Annual Survey on Overall Satisfaction	●	◐	○	○	●	○	○	○
Transactional Survey	●	●	◐	◐	●	○	○	○
Service Feedback Cards	◐	●	●	◐	◐	●	◐	●
Mystery Shopping	○	◐	●	●	○	○	◐	○
Unsolicited Feedback (e.g., complaints)	○	◐	●	●	○	●	◐	●
Focus Group Discussions	○	◐	●	●	○	◐	●	◐
Service Reviews	○	◐	●	●	○	●	●	◐

### Analysis, Reporting, and Dissemination of Customer Feedback

- Relevant feedback tools and collecting customer feedback should be channeled back to the relevant parties to take action

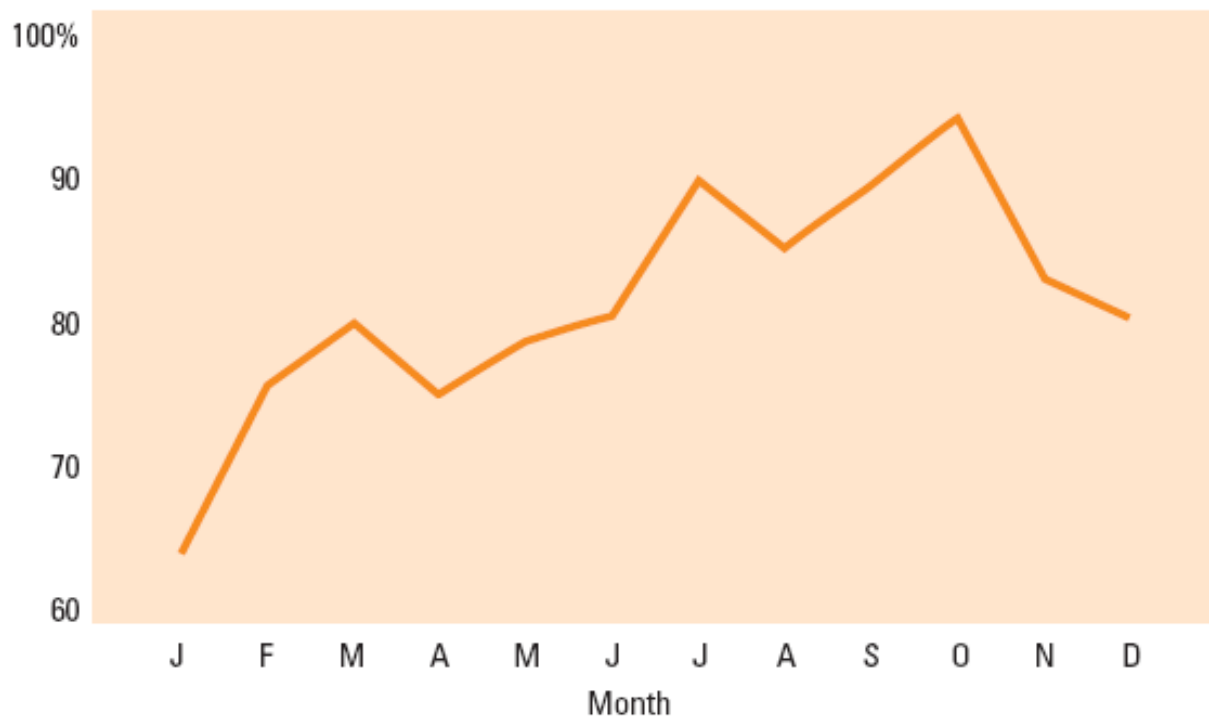
- Three common types of performance reports
  - Monthly Service Performance Update
  - Quarterly Service Performance Review
  - Annual Service Performance Report

## Hard Measures of Service Quality

- Service quality indexes
  - Embrace key activities that have an impact on customers
- Control charts to monitor a single variable
  - Offer a simple method of displaying performance over time against specific quality standards
  - Enable easy identification of trends
  - Are only good if data on which they are based are accurate
- FedEx: one of the first service companies to understand the need for an index of service quality that embraced all the key activities that affect customers

## Control Chart for Departure Delays

Flights Departing Within 15 Minutes of Schedule

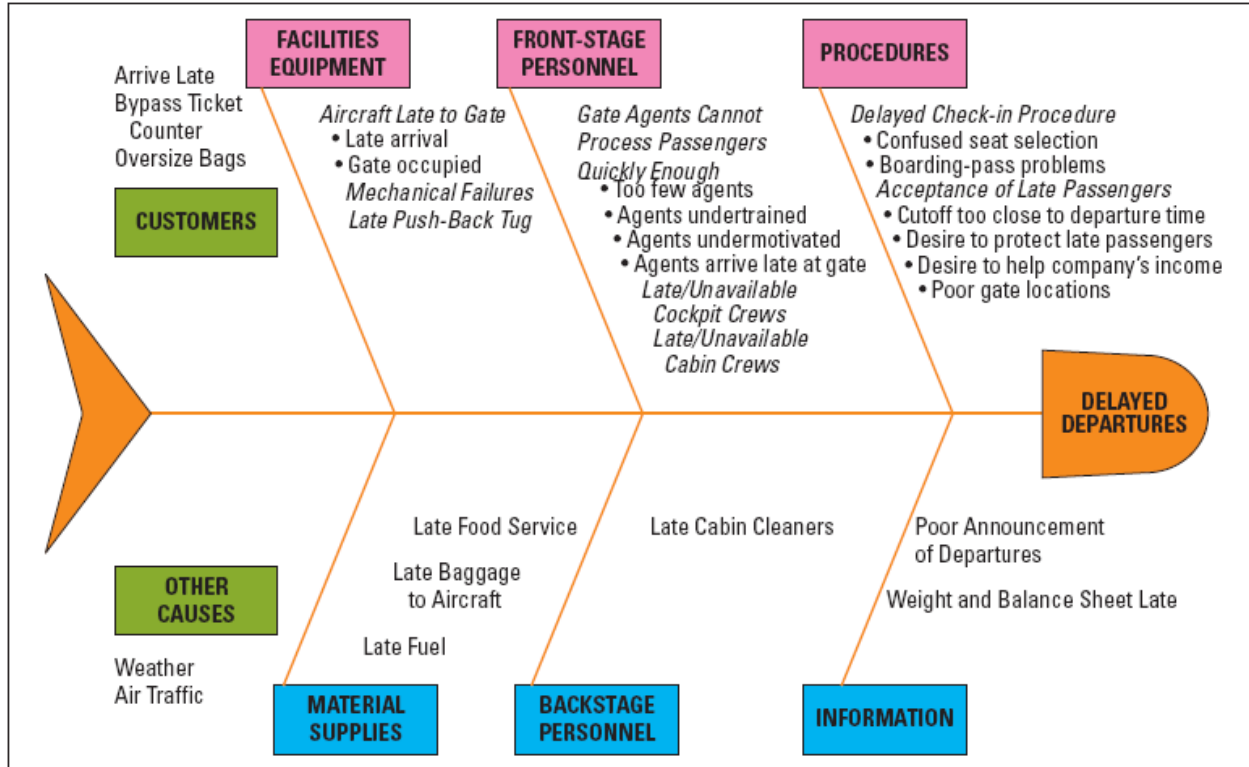


## Tools to Analyze and Address Service Quality Problems

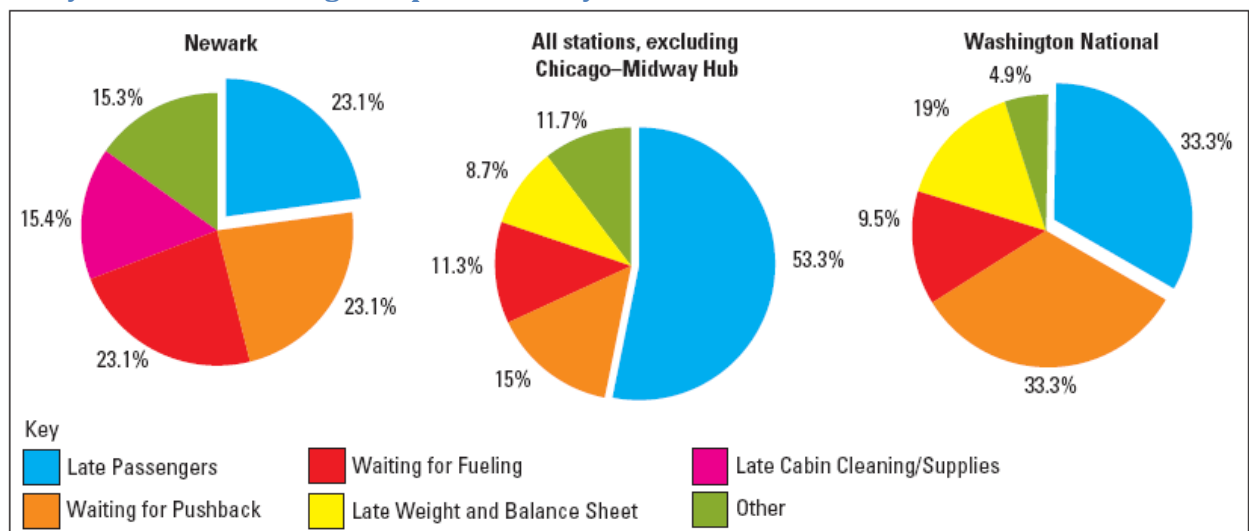
- Fishbone diagram
  - Cause-and-effect diagram to identify potential causes of problems
- Pareto Chart

- Separating the trivial from the important. Often, a majority of problems are caused by a minority of causes (i.e., the 80/20 rule)
- Blueprinting
  - Visualization of service delivery, identifying points where failures are most likely to occur

### Cause-and-Effect Chart for Flight Departure Delays



### Analysis of Causes of Flight Departure Delays



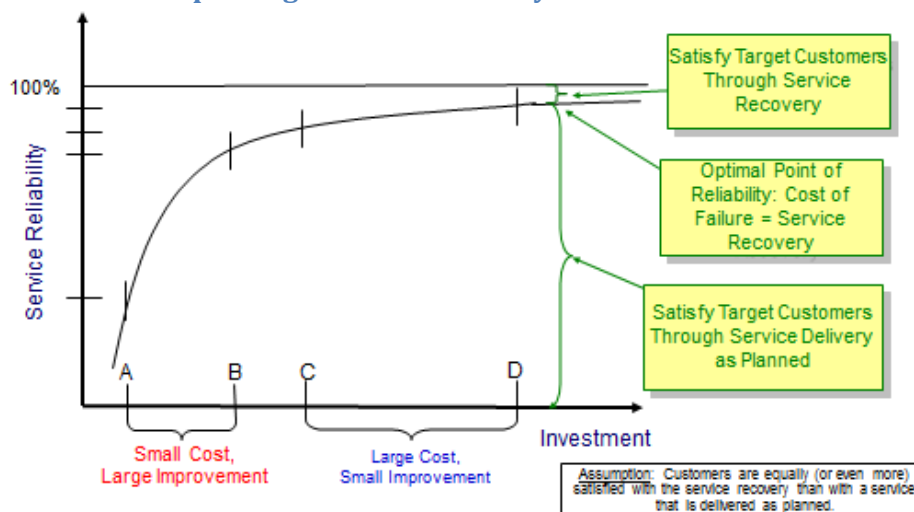
## Blueprinting

- Depicts sequence of front-stage interactions experienced by customers plus supporting backstage activities
- Used to identify potential fail points
  - Where failures are most likely to appear
- Shows how failures at one point can have a ripple effect
- Managers can identify points which need urgent attention
  - Important first step in preventing service quality problems

## Return on Quality (ROQ)

- Assess costs and benefits of quality initiatives
  - ROQ approach is based on four assumptions:
    - Quality is an investment
    - Quality efforts must be financially accountable
    - It's possible to spend too much on quality
    - Not all quality expenditures are equally valid
  - Implication: Quality improvement efforts may benefit from being related to productivity improvement programs
  - To determine feasibility of new quality improvement efforts, determine costs and then relate to anticipated customer response
- Determine optimal level of reliability
  - Diminishing returns set in as improvements require higher investments
  - Know when improving service reliability becomes uneconomical

## When Does Improving Service Reliability Become Uneconomical?



## Productivity in a Service Context

- Productivity: amount of output produced relative to amount of inputs
  - Improvements in productivity means an improvement in the ratio of outputs to inputs

- Intangible nature of service makes it hard to measure productivity of service firms, especially for information-based services
  - Both input and output are hard to define
  - Relatively simpler in possession-processing services, as compared to information- and people-processing services

### Service Efficiency, Productivity, and Effectiveness

- Efficiency: involves comparison to a standard, usually time-based (e.g., how long employee takes to perform specific task)
  - Focus on inputs rather than outcomes and may ignore variations in service quality/value
- Productivity: involves financial valuation of outputs to inputs
  - Consistent delivery of outcomes desired by customers should command higher prices
- Effectiveness: degree to which firm meets goals
  - Cannot divorce productivity from quality and customer satisfaction

## Improving Service Productivity

### Generic Productivity Improvement Strategies

- Typical strategies to improve service productivity:
  - Careful control of costs
  - Efforts to reduce wasteful use of materials or labor
  - Matching productive capacity to average demand levels
  - Replacing workers by automated machines or self-service technologies
  - Teaching employees how to work more productively
  - Broadening variety of tasks that service worker can perform
  - Installing expert systems that allow paraprofessionals to take on work previously performed by professionals
- Although improving productivity can be approached incrementally, major gains often require redesigning entire processes

### Customer-Driven Strategies to Improve Productivity

- Change timing of customer demand
  - By shifting demand away from peaks, managers can make better use of firm's productive assets and provide better service
- Involve customers more in production
  - Get customers to self-serve
  - Encourage customers to obtain information and buy from firm's corporate websites
- Ask customers to use third parties
  - Delegate delivery of supplementary service elements to intermediary organizations

### Implications of Backstage and Front-Stage Changes for Customers

- Backstage changes may impact customers
  - Keep track of proposed backstage changes, and prepare customers for them

- E.g., new printing peripherals may affect appearance of bank statements
- Front-stage productivity enhancements are especially visible in high contact services
  - Some improvements only require passive acceptance, while others require customers to change behavior
  - Must consider impact on customers and address customer resistance to changes

### A Note of Caution on Mere Cost Reduction Strategies

- Without new technology, firms improve service productivity by eliminating waste and reducing labor costs
- Multitasking can reduce productivity
- Excessive pressure breeds discontent and frustration among customer contact personnel
- It is often better to search for service process redesign opportunities that lead to quantum leaps in improvements in productivity and service quality at the same time

### Summary

- Service quality has five key dimensions: Tangibles, Reliability, Responsiveness, Competence, Courtesy
- GAPS model can be used to diagnose and address service quality problems:
  - Gap 1: The Knowledge Gap
  - Gap 2: The Policy Gap
  - Gap 3: The Delivery Gap
  - Gap 4: The Communications Gap
  - Gap 5: The Perceptions Gap
  - Gap 6: The Service Quality Gap
- Customer feedback systems are used to:
  - Assess and benchmark service quality and performance
  - Institutionalize customer-driven learning and improvements
  - Create a customer-oriented service culture
- Efficiency, productivity, and effectiveness need to be distinguished when measuring service quality
- Customer-driven approaches to improving productivity include
  - Changing timing of customer demand
  - Involving customers more in production
  - Asking customers to use third parties
  - Use cost-reduction strategies with caution if they are not driven by new technology or process redesign – they may reduce service quality!

### Appendix

#### SERVQUAL

- Survey research instrument based on premise that customers evaluate firm's service quality by comparing:
  - Their perceptions of service quality actually received with

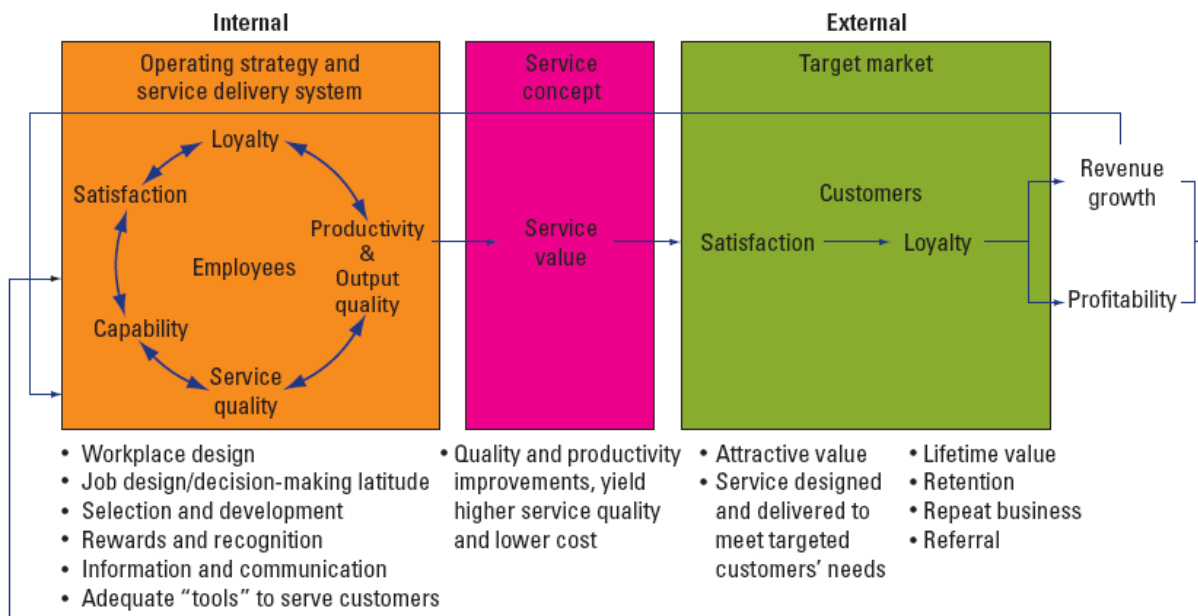
- Their prior expectations of companies in a particular industry
- Poor Quality: Perceived performance ratings < expectations
- Good Quality: Perceived performance ratings > expectations
- Developed primarily in context of face-to-face service encounters
- Scale contains 22 items reflecting five dimensions of service quality
- Scale may have to be customized to the research context as recent research suggests that it is not generalizable

### Tools to Analyze and Address Service Quality Problems

- Total Quality Management (TQM)
- ISO 9000
  - Comprises requirements, definitions, guidelines, and related standards to provide an independent assessment and certification of a firm's quality management system
- Malcolm Baldrige Model Applied to Services
  - To promote best practices in quality management, and recognizing, and publicizing quality achievements among U.S. firms
  - Many countries around the world have adapted the Malcolm Baldrige Model
- Six Sigma & Lean Six Sigma
  - Statistically, only 3.4 defects per million opportunities (1/294,000)
  - Has evolved from defect-reduction approach to an overall business-improvement approach

## Chapter 15: Striving for Service Leadership

### The Service-Profit Chain



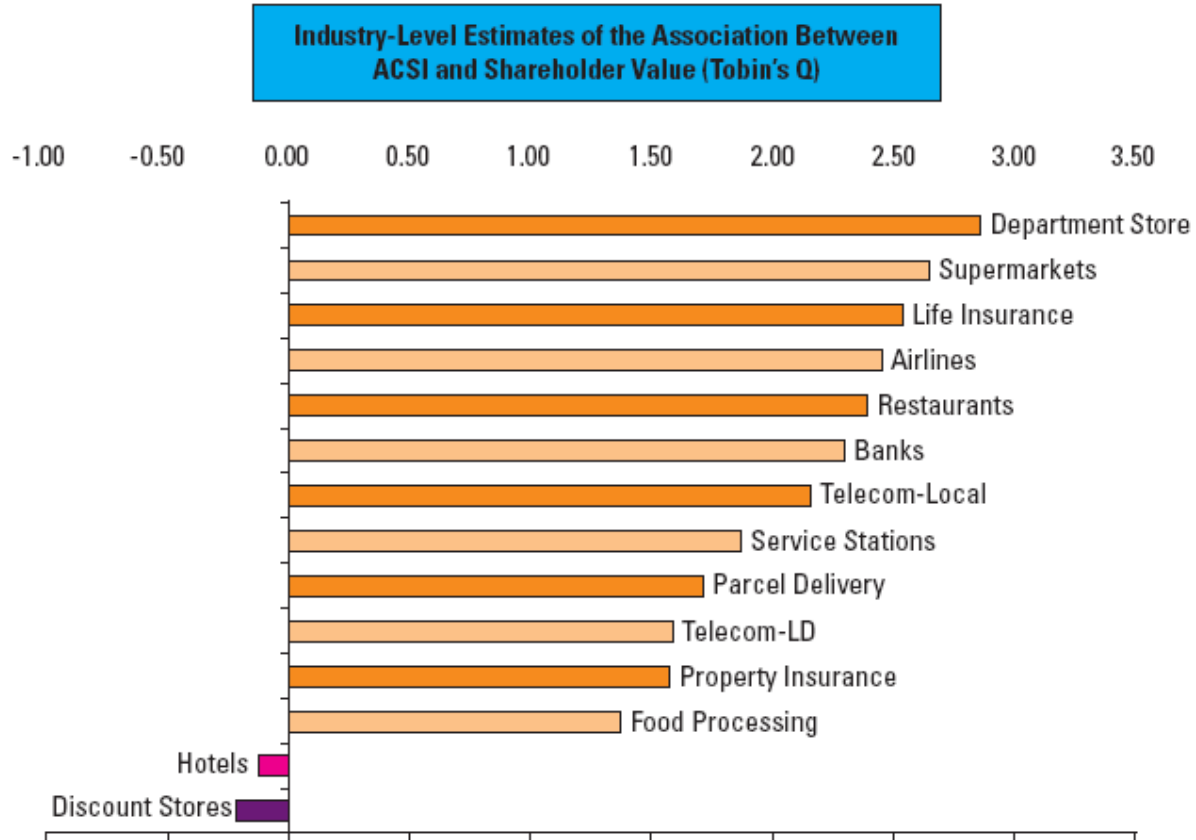
#### SOURCE

Reprinted by permission of *Harvard Business Review*. From Putting the service-profit chain to work. By Heskett, J.L., Jones, T.O., Loveman, G.W., Sasser Jr., W.E., & Schlesinger, L.A. (March–April), p. 166. Copyright © 1994 by the Harvard Business School Publishing Corporation; all rights reserved.

### Links in the Service-Profit Chain

1. Customer loyalty drives profitability and growth
2. Customer satisfaction drives customer loyalty
3. Value drives customer satisfaction
4. Quality and productivity drives value
5. Employee loyalty drives service quality and productivity
6. Employee satisfaction drives loyalty
7. Internal quality drives employee satisfaction
8. Top management leadership underlies the chain's success

## Firm Value Created by Customer Satisfaction



### SOURCE

Claes Fornell et al., *The American Customer Satisfaction Index at Ten Years*. ACSI, 2005: 42 (service industry data extracted from larger table).

## Qualities Associated with Service Leaders

- Understand mutual dependency among marketing, operations, and human resources functions of the firm
- Has a coherent vision of what it takes to succeed
- Strategies are defined and drive by a strong, effective leadership team
- Responsive to various stakeholders
- Value created through customer satisfaction

## Integrating Marketing, Operations, and Human Resources

### Defining the Three Functions

#### Marketing Function

- Target “right” customers and build relationships
- Offer solutions that meet their needs

- Define quality package with competitive advantage

### ***Operations Function***

- Create, deliver specified service to target customers
- Adhere to consistent quality standards
- Achieve high productivity to ensure acceptable costs

### ***Human Resource Function***

- Recruit and retain the best employees for each job
- Train and motivate them to work well together
- Achieve both productivity & customer satisfaction

### **Reducing Interfunctional Conflict**

- One challenge is to avoid creating “functional silos”
  - High-value creating enterprises should be thinking in terms of activities, not functions
- Top management needs to establish clear imperatives for each function that defines how a specific function contributes to the overall mission
  - Interfunctional transfers will provide a holistic perspective for individuals
  - Establishing integrated project teams
  - Having Interfunctional service delivery teams
  - Appointing formally designated individuals to integrate objectives
  - Internal marketing and training
  - Commitment of top management

## **Creating a Leading Service Organization**

### **From Losers to Leaders: Four Levels of Service Performance**

#### ***Service Losers***

- Bottom of the barrel
- Patronized because there is no viable alternative
- New technology introduced only under duress; uncaring workforce

#### ***Service Nonentities***

- Dominated by a traditional operations mindset
- Unsophisticated marketing strategies
- Consumers neither seek out nor avoid them

#### ***Service Professionals***

- Clear market positioning strategy such that customers within target segment(s) seek them out
- Proactive, investment-oriented approach to HRM

#### ***Service Leaders***

- The crème de la crème of their respective industries

- Names synonymous with outstanding service, customer delight
- Employees are empowered and committed

### Four Hurdles for Moving up the Performances Ladder

- Cognitive Hurdles
  - People cannot agree on causes of current problem and the need for change
- Resource Hurdles
  - Firm is constrained by limited funds
- Motivation Hurdles
  - Prevent rapid execution when employees are reluctant to change
- Political Hurdles
  - Organized resistance forces in forms from powerful vested interests seeking to protect their positions

### Leading Change in a Service Organization Involves 8 Stages

1. Creating a sense of urgency to develop the impetus for change
2. Putting together a strong enough team to direct the process
3. Creating an appropriate vision of where the organization needs to go
4. Communicating that new vision broadly
5. Empowering employees to act on that vision
6. Producing sufficient short-term results to create credibility and counter cynicism
7. Building momentum and using that to tackle tougher change problems
8. Anchoring new behaviors in organizational culture

## In Search of Human Leadership

### Leadership vs. Management

Leadership	Management
Setting direction: <ul style="list-style-type: none"> <li>• Creating visions and strategies that describe a business, technology, or corporate</li> <li>• In terms of what it should become over long term and articulating feasible way of achieving goal</li> <li>• Development of vision and strategies, and empowerment of people to overcome obstacles, make vision happen</li> <li>• Emphasis on emotional and spiritual resources</li> <li>• Works through people and culture</li> <li>• Produces useful change, especially non-incremental change</li> </ul>	Planning <ul style="list-style-type: none"> <li>• A management process designed to produce orderly results, not change</li> <li>• Keeps current situation operating through planning, budgeting, organizing, staffing, controlling, and problem solving</li> <li>• Emphasizes physical resources</li> <li>• Works through hierarchy and systems</li> <li>• Keeps current system functioning</li> </ul>

## Individual Leadership Qualities

- Love for the business
- See service quality as foundation for competing
- Recognize key role of employees
- Driven by a set of core values they pass on
- Make communication a priority
- Work with a team on decision-making
- Know when to change when necessary
- Walk the talk

## Leadership, Culture, and Climate

### Leadership

- Leadership traits are needed of everyone in supervisory or managerial positions, including those heading teams

### Organization Culture

- Represents the shared
  - Perceptions/themes regarding what is important
  - Values, beliefs, and assumptions
  - Shares understanding about what works and what doesn't work
  - Styles of working and relating to others

### Organizational Climate

- The tangible surface layer on top of the organization's underlying culture that requires radical rethinking of:
  - HRM activities
  - Operational procedures
  - Firm's reward and recognition policies

## Summary

- Service profit chain provides summary of relationships between key variables that explain service leadership
- Four levels of service performance
  - Service losers
  - Service nonentities
  - Service professionals
  - Service leaders
- Service leadership must cut across marketing, operations, and human resources
- Leaders need to understand the difference between leadership vs. management, as well as setting direction vs. planning
- Leaders play a big part in nurturing an effective organizational culture that moves an organization towards service leadership