CUSTOMER VALUE IN BUSINESS MARKETS – A RESEARCH SUMMARY AND PROPOSAL FOR AN EXTENSION

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ABSTRACT

After pioneering, but insular, work on the conceptualization and measurement of customer value in business markets undertaken in the 80s and 90s, interest in this topic has increased substantially since the beginning of this decade. Despite this recent interest, marketing scholars concur that value in business markets is still an under-researched subject. This contribution to the debate is twofold. The paper proposes an own model of customer value conceptualization in business markets; based on several rounds of testing this theoretically grounded model in managerial practice indications exist to conclude that this model may offer benefits over current models. Two case studies, one involving the pricing decision for a major product launch at a global chemical company, the other involving value delivery at an industrial equipment manufacturer, illustrate the practical applicability of the proposed framework.

INTRODUCTION

Recent times witness a surge of interest in the concept and application of customer value, especially in understanding the definition and measurement of customer value in industrial settings (see, for example, Anderson, Thomson & Wynstra, 2000; Flint, Woodruff & Gardial, 2002; Homburg, Küster, Beutin & Menon, 2005; Lyndgren & Wynstra, 2005; Ulaga, 2003; Ulaga & Eggert, 2006). Despite this interest, the concept of customer value in business markets is ill defined. Building on the current literature, the paper proposes an own model of customer value conceptualization in business markets which fills gaps which the current literature recognizes.

CUSTOMER VALUE IN BUSINESS MARKETS: THEORY DEVELOPMENT

This paper expands on two topics concerning the construct of customer value in business markets. First, properties of customer value and, secondly, dimensions of value. Regarding its properties, Ulaga (2003) provides a summary of the current state of the art: The construct of customer value is (1) a subjective concept, it is (2) a trade-off between benefits and sacrifices, it is (3) multidimensional, since benefits and sacrifices can be "multifaceted"; (4) value perceptions are relative to competition. In an earlier paper Ulaga and Chacour (2001) note that value is relative to customer segments and specific use situations.

The concept of value in business market has one additional, fundamental trait which these characterizations do not capture. Value in business markets is future-oriented (see also Hogan, 2001). Value in business markets is necessarily and unconditionally a future-oriented construct: Two parties exchange resources (e.g. money, goods, services, rights, or intellectual property) in the expectation of certain future benefits resulting from consuming these resources. Being a future oriented concept, the concept of value in business markets thus necessarily and unconditionally shares the properties of a probabilistic utility function: outcomes have a certain expected value, a distribution around an expected value, a skewness, and they are, above all, uncertain. This uncertainty is due to the inherent uncertainty of the future, and uncertainty is further compounded by possible opportunism on the part of the supplier (Hogan, 2001), adverse selection and the circumstance that value in business relationships is jointly built and may thus be substantially bigger than initially assessed by mutual will and design of both the customer and the supplier. This trait of uncertainty and future orientation could lead to the representation of customer value as a range of expected values, rather than representing customer value as a single (certain) number. Taking Ulaga's (2003), Ulaga and Chacour's (2001) summaries as a basis and adding the element of uncertainty, the present paper thus summarize the characteristics of value in business markets as follows: value is (1) a subjective concept, value is (2) a trade-off between benefits and sacrifices, value is (3) multidimensional, value is (4) defined relative to competitors, value is (5) segment specific, and value is (6) future-oriented.

On the dimensions of customer value in business markets Ulaga and Eggert (2006) reiterate that "research on customer value in business markets is still in an early stage"; this paper sees shares this view and sees this as incentive to further advance current theory. In a qualitative study with ten purchasing managers of US-based industrial companies Ulaga (2003) and Ulaga and Eggert (2006) identify six dimensions along which suppliers create benefits and three dimensions along which suppliers reduce costs for their customers. The six benefit dimensions identified are: (1) product quality, (2) delivery

performance, (3) service support, (4) personal interaction, (5) supplier know how and (6) time to market. Costs are sub-divided in to (1) direct costs, (2) acquisition costs and (3) operation costs (as in: Cannon & Homburg, 2001).
The six benefit and three cost components provide a useful, theoretically rigorous conceptualization of value in business markets. From the standpoint of the supplier, this framework allows to assess value delivered along the nine dimensions. From the standpoint of the customer, the framework allows to compare value delivered by a set of alternative suppliers.

The author has tested this framework in workshops conducted with 35 marketing managers, general managers, and sales managers working in four different industrial businesses: the chemical industry, food/food processing industry, energy delivery and mechanical engineering in Germany, Austria, and China. The framework is useful but not exhaustive: the framework does not capture the full variety of possibilities for suppliers to add customer value. In particular, discussions with executives participating in these workshops spur further efforts to investigate the question whether additional possibilities for suppliers to add customer value exist. In addition, the author undertakes an exhaustive literature survey to explore sources of customer value, both in consumer goods as well as industrial businesses. In a subsequent round of discussions, practicing executives comment on these findings.

In particular, one construct stands out: the construct "easy to do business with". Bolton and Drew (1992) examine the impact of this construct on customer value. They refer to this construct as the customer's overall assessment of its supplier's policies and practices on whether these policies and practices make the service encounter easy and pleasant. Bolton and Drew (1992) find that this construct has an important impact on customer perceived value and is as important as quality in predicting value. More recently, Hammer (2001), one father of the re-engineering movement, presents "a set of nine emerging business concepts that underlie how the best companies around are mastering today's turbulent environment". One of these concepts is "easy to do business with" or "ETBW": Hammer (2001) argues that ETBW will become one of the most important sources of competitive advantage in this decade. In extensive empirical tests by telephone interviews with more than 1,000 industrial customers Kumar and Grisaffe (2004) find the impact of the construct "easy to do business with" (or "customer focus" in their wording) to have the overall highest impact on both perceived quality and customer value in B2B purchasing contexts. They conjecture that it may be "quite common to see a firm whose quality and prices are comparable (or even slightly lower priced) losing out to competitors perceived as being easy to do business with" (Kumar & Grisaffe, 2004, page 65). In addition to order handling procedures, the construct "easy to do business with" also captures complaint handling procedures. In an empirical survey involving more than 2,000 respondents in industrial companies Homburg and Rudolph (2001) find that satisfaction with complaint handling procedures have a strong impact on the overall satisfaction of industrial customers which exceeds the impact of the satisfaction with product related items. The construct "easy to do business with" (i.e., order and complaint handling procedures) merits to be treated as a separate source of customer value in business relationships. Furthermore, discussions with participating managers lead to the exploration of the construct self enhancement, the idea that suppliers can confer to their customers intangible benefits such as prestige, social status or other aspiration benefits. In consumer goods industries this concept is, in contrast to industrial industries, already well established: BBDO, a leading advertising agency, uses the terms "identity building brands" and "mythological brands" to refer to a product's ability to provide self-enhancement to its consumers (BBDO, 2001). Identity-building brands contribute to define the consumer's perceptions and self-awareness. This "identity is the product of interplay between producer and consumer to create a suitable brand environment. Interactive communication provides the framework for this, a process which necessitates active involvement on the part of the consumer. The brand is integrated into the consumer's personality (self share), i.e. the brand exhibits an overlap with the consumer's own self-image. … At this level of brand leadership, consumers define themselves via the brand (and the brand via its loyal customers), relying on it for self-expression and identity formation" (BBDO, 2001). Mythological brands go one step further and assume "the function of a guide or mentor offering insight into the meaning of life". Coca-Cola, Marlboro, Rolex and Harley-Davidson and Ferrari are examples of identity building and mythological brands, respectively (BBDO, 2001). Purchase and consumption in industrial contexts are less intertwined with the customer's personality and individual values than in consumer goods industries. However, also in industrial businesses suppliers have the opportunity to provide intangible benefits to customers such as prestige, social status, or other aspiration benefits. Ward, Light, and Goldstine (1999) state: "It is true that most of our knowledge about brand strategies come from the accumulated experience of consumer-packaged-goods-companies like Procter and Gamble, Nabisco, and Nestle – and a wealth of enduring and highly profitable brands. But just because a concept evolved in consumer good markets is no reason to reject it in business-to-business markets." Ward at al (1999) document which psychological and emotional benefits brands such as Intel, IBM, EMC, and Microsoft create in high-tech and industrial businesses. They demonstrate that also in industrial contexts well-managed brands make industrial customers "feel better" about themselves. Ingredient brands are a further case in point. Stainmaster, a brand by DuPont, stands for a special plastic fiber used in industrial carpets which need a strong protection against stains. DuPont originally sells Stainmaster as an ingredient brand to carpet manufacturers with the intent of allowing carpet manufacturers to display their own brand name along its ingredient brand. The intrinsic qualities and

Stainmaster's brand name are so strong that many smaller carpet manufacturers today find an investment in own brand building activities no longer worthwhile. Thus Stainmaster is frequently the only brand name displayed on industrial carpets. Similarly, industrial customer can perceive value to purchase products from the industry leader, rather than an also ran. Kumar and Grisaffe (2004) find a positive, albeit weak, positive relationship between buyers' perception of supplier firms industry leadership and perceived overall value in B2B relationships. Furthermore, if the relationship between the supplier and the customer allows the customer or the supplier to gain social status or prestige in a network of companies – for example by advertising its status as key supplier or key customer to other companies – then this relationship creates value for the supplier and customer which goes beyond intrinsic product attributes and refer to intangible benefits which are not completely dissimilar to the intangible benefits consumer perceive from purchasing leading brands. The construct self-enhancement – which summarizes the potential of a supplier to enhance the social status, prestige, or provide aspiration benefits to its customers, especially when these customers are part of a wider network of industrial companies – merits to be treated as separate source of customer value in business relationships.

Based on the considerations above and Ulaga's (2003) typology of benefits this paper proposes an expanded model of customer value creation in industrial markets with six dimensions: this paper proposes to collapse Ulagą s (2003) six benefit categories into four and to add two new benefit dimensions:
- product quality: compromising elements such as conformance to specifications, reliability, durability, environmental profile, safety, etc..
- delivery capabilities: delivery speed, delivery reliability, ability to deliver in small lot sizes, delivery flexibility.
- services: installation, application support, information, customization, maintenance, repair, performance guarantees, warranties, capabilities to operate plants on behalf of customers, financial services (capabilities to extend credit services, to offer leasing or buy-back option after product use).
- ease of doing business: ease of ordering, ordering costs and time, responsiveness to order-related enquiries, flexibility in accepting customer orders via alternative channels, reachability to accept customer orders, complaint handling procedures.
- vendor: vendor know how, vendor competencies, new product development capabilities, vendor personnel, capability to offer solutions in addition to product offerings (Penttinen & Palmer, 2007).
- self enhancement: social status, prestige, aspiration benefits.

Graphically, a chart of the type shown below visualizes the value added by different suppliers. This chart allows comparing the abilities to add value of different suppliers; this way of graphically representing customer value furthermore allows tracking supplier value creation over time. Building on insights from these studies the model includes the following definition of customer value in business markets. Value to the customer of a company's product, service, relationship, competency or intellectual property offering is equal to price of the customer's best alternative plus the expected (positive or negative) value along the six dimensions – product, delivery capabilities, services, easy to do business, vendor, self enhancement – along which this offering is differentiated from the alternative. This definition references received value of customers – the value customer actually experience through specific product-customer interactions – and not customers' desired value – the value customers want from products and services and their providers (Flint & Woodruff, 2001). The definition proposal further satisfies key elements which are relevant for customer value measurement approaches, namely the requirement of (1) subjectivity (customer specificity), (2) identification of benefits and sacrifices, (3) multidimensionality, (4) relativity of value to competitive standards, (5) segment/use situation specificity and (6) future orientation.

Customer value in this definition refers to the maximum amount a customer would pay to obtain a given offering, that is, the price that leaves the customer indifferent between the purchase and foregoing the purchase (i.e., the "reservation price"). Customer value includes the full set of customer benefits and sacrifices – except the purchase price. The advantage of excluding price from the definition of customer value is that this leads to a conceptualization of customer value which is independent from a company's pricing strategy. This approach thus allows exploring alternative value delivery and pricing strategies without affecting the conceptualization of value. In other words, in this conceptualization customer value is completely independent from price – and this independence is a distinct advantage.

SUMMARY AND CONCLUSION

This paper covers a number of points. First, the paper advances the conceptualization of value in business markets by further developing the model of Ulaga and Eggert (2006), arguably the most rigorous conceptualization of customer value in business markets today. The empirical basis of these advancements is a grounded theory approach where the author captures, summarizes, tests, and validates the experiences of 35 marketing executives. Specifically this empirical work adds two new dimensions – ease of doing business and self enhancement – as sources of value for customers in industrial markets which existing models do not capture well. Based on in depth discussions with managers participating in these workshops, empirically grounded evidence exists that industrial companies are already providing value to their customers along these two new dimensions. Further validation of the proposed model and measurements to quantify value are the next critical empirical steps which are urgently required. On the one side, the property of future-orientation of the construct of value in business markets (par 3) opens up potentially fruitful research questions such as: What is the impact of perceived and and what is the impact of true (i.e., objective) uncertainty on perceived customer value? What is the role of emotions – such as fear – in shaping perceptions of uncertainty which affect perceived customer value? How can companies shape uncertainty to their advantage (increase perceived uncertainty of competitive products, reduce perceived uncertainty of own products)?

In addition, further qualitative studies are needed to understand whether the proposed model of value creation in business markets is exhaustive. Next, LISREL and structural equation models can be used to understand the validity of the entire model and to pinpoint which sub-dimensions of value (product, delivery capabilities, services, ease of doing business, vendor, self-enhancement) are most closely associated with overall customer value: Consider which sub-dimensions of the construct value in business markets relate most closely with overall customer value across industries, across countries, for different members of the buying center, across customer categories, across product categories, across market segments, and across intensity of buyer-supplier relationships. From a theoretical perspective, this step allows the building and validating parsimonious models of value creation and delivery where causal links become evident. From a practical standpoint this step helps managers understand along which dimensions customer value needs to be further increased to maintain, defend or gain a competitive advantage, and, conversely, which dimensions of value matter less. The resulting insight from this understanding will have profound impact on business unit strategies.
Longitudinal analysis finally can help to shed light on dynamic aspects on customer value in business markets: causal relationships triggering shifts in the relative importance of alternative sub-dimensions of value and overall customer value need to be explored. Extant research in this area acknowledges the need for further theory development (Flint & Woodruff, 2001; Flint, Woodruff, & Gardial, 2002). This paper also shows that a relentless focus on competitiveness has major drawbacks: instead of attempting to create and to communicate value to customers, companies risk paying an unjustified attention to current product features of competitors, regardless of whether these features meet customer requirements and truly create superior customer value. Empirical research supports this claim: In a field study involving 20 U.S. Firms over an extended period of time Armstrong and Collopy (1996) find that companies with a pure competitor-oriented strategy are less profitable and less likely to survive than companies with a strong customer orientation. Differentiation from competitors does not per se add value. Differentiation might lead to a sustained investment in product features which do not add any value for customers. Product differentiation strategies have to be preceded by an understanding of the real sources of value for customers, which then will lead to appropriate positioning and pricing. Customer value analysis is a valuable tool even when products are relatively undifferentiated: in this case, insights in the way in which the product adds value can lead to ways to develop the product further and to position the product in ways which add value to customers.

TABLES AND FIGURES

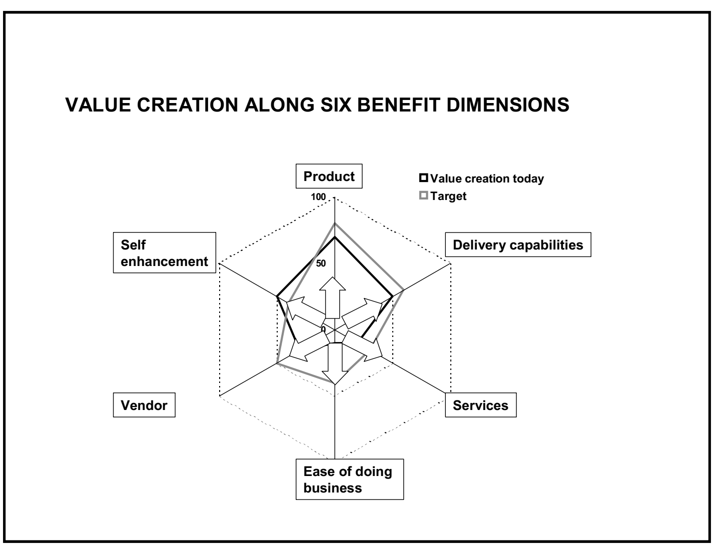

Figure 1: Value creation in industrial markets – six dimensions of customer benefits

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