Customer Orientation of Electricity Retail Sales Companies

B. A. Bokarev, D. G. Sandler, and M. V. Kozhevnikov

1 Introduction

There is a fairly large number of negative factors that affect electricity retailers, including a general trend among consumers to delay payments, major industrial consumers moving away from last resort suppliers, a lack of a clear strategy on the part of the government as to how to develop electricity markets as regards tariff regulation, energy conservation and legal provisions.

Evidence from many countries that had their electric power sector restructured shows that regardless of the environment that electricity suppliers operate in, they lose their monopoly-induced competitive advantages as the electricity and capacity markets develop. The competitive advantages of electricity retailers can only stem from their intrinsic potential that consists of their:

- Social capital
- Key domain-specific competencies
- *Focus on current and potential needs of customers*
- A management system that makes it possible to maintain and develop the above-mentioned factors

There is, therefore, a need to create a methodological platform for implementing a customer-oriented approach to ensure the sustainable development of electric power companies and, more specifically, retail sales companies.

B. A. Bokarev
JSC "Atomenergosbyt", Moscow, Russia

D. G. Sandler · M. V. Kozhevnikov (✉)
Ural Federal University, Yekaterinburg, Russia
e-mail: m.v.kozhevnikov@urfu.ru

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2 Customer Orientation Issues in Electric Power Industries

The key principles of customer orientation can be outlined as follows:

1. A customer (or group of customers) is selected within the Company's management system.
2. The Company provides a targeted response to the customer's demands and clearly expressed needs.
3. The customer is evaluated and ranked on the criteria of revenue and other specific characteristics that matter for the achievement of the Company's strategic goals.
4. Effective projects and measures are developed and implemented in a systemic way to manage the satisfaction of the customer's known demands and clearly manifested needs.
5. The perceived and created customer value of the Company's products is studied.
6. Systemic projects are implemented that are aimed at managing the created and perceived value of the Company's products for the customer. The characteristics and range of products and services are adjusted, and the operational functions of the business are re-engineered accordingly.
7. The Company engages customers in value chain management.

A customer-focused approach implies that pinpointing and satisfying the needs of customers whom the company "knows personally" is the only way to ensure its leadership in the industry, to make its products competitive and, ultimately, to meet the objectives set by its owners and reach various (financial, social and other) goals of the company. The electricity sectors of developing countries remain highly monopolized despite reforms, and consumers are not given priority as the prime factor of business development.

An energy company can opt for one of two tariff policy options that differ critically in terms of customer relations:

1. The strategy of short-run profit maximization aimed at gaining the maximum yield from customers "today"
2. The strategy of long-run profit maximization aimed at encouraging effective demand, i.e. at supporting and building up a customer base as the only source of income

The advantages and disadvantages of each strategy are outlined in Table 1.

The majority of Russian electricity companies are now implementing the first strategy. Among other things, this results in manufacturing companies losing their competitive edge over similar products imported from abroad because their energy costs become extremely high, while energy suppliers do not make any efforts to reduce energy intensity [1]. Having one's own power generation facilities becomes the only way-out, which naturally leads to lower revenue for energy companies. This creates a vicious circle in which consumers and, eventually, energy companies themselves are faced with growing prices of goods and services (Fig. 1). Consequently, products generated by the power system become less competitive.

Table 1 Advantages and disadvantages of different tariff strategies

Strategy	Advantages	Disadvantages
Short-run profit maximization	• Excess profit made quickly in the short run • No need to invest in R&D and innovation	Passing on costs to consumers through higher tariffs could lead to: • Lower electricity consumption because of customers converting to alternative energy sources or, when possible, leaving for other electricity suppliers • Non-payment or delayed payment of bills • Unauthorized connections to the grid and resulting losses
Long-run profit maximization	• Stable demand for electricity and growing revenue of the electricity supplier • Social and economic benefits for the state, local government and society as a whole	• Government and financial institutions have to be involved in developing investment and energy programmes

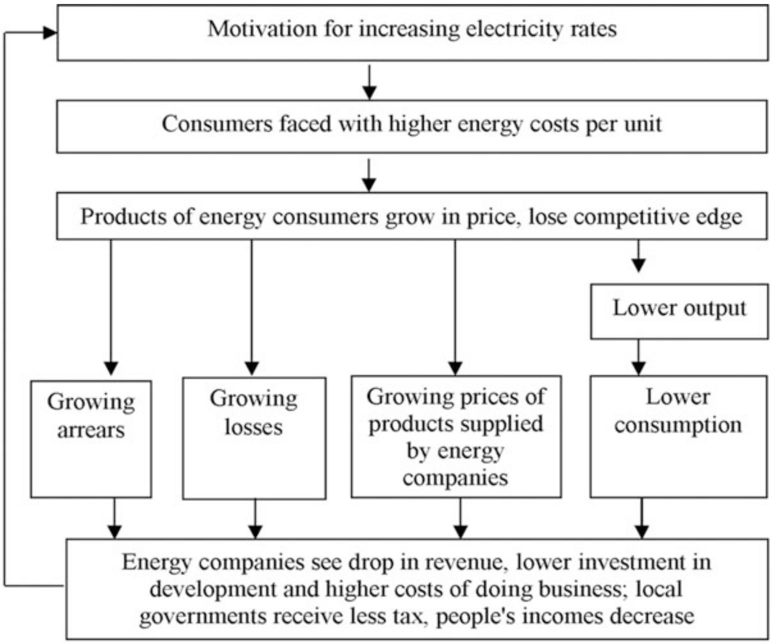

Fig. 1 Consequences of short-run profit maximization

3 Methodology for Assessment of Customer-Oriented Management Approach

Figure 2 depicts the customer structure of an energy retailer. It is worth noting that all too often some business partners whose interests the company seeks to satisfy are mistakenly excluded from the ranks of its customers because they do not consume its key product/service.

To assess the customer-oriented management approach, we shall use a system that will be drawn as a radar chart where the number of axes represents the number of customers (or groups of customers) of the Company and the scale on the graph characterizes the strength of the Company's focus on a specific customer (or group of customers) by means of anchored data markers with detailed labels. The number of axes for the chart is selected specifically for each business and might represent either the list of objects of focus (Fig. 3a) or an expanded group of identical objects (Fig. 3b).

We refer to the customer mix of the Company as its orientation field. The resulting star chart that illustrates the expert evaluation of the Company on the suggested scale characterizes the level of orientation.

We shall refer to the gap between the current and target level of customer orientation of the Company (as envisaged in its development strategy) as its orientation potential. The size and shape of the orientation potential in the chosen orientation field will determine the choice of the ways and means for implementing the customer-focused management approach.

The frequency of adjusting the customer orientation of the system, as indicated in the classification in Fig. 3, might be one-off, regular and constant. If it is enough for the Company to adjust its customer focus once, in most cases, there will be no need for changing the business structure or business process re-engineering. If orientation

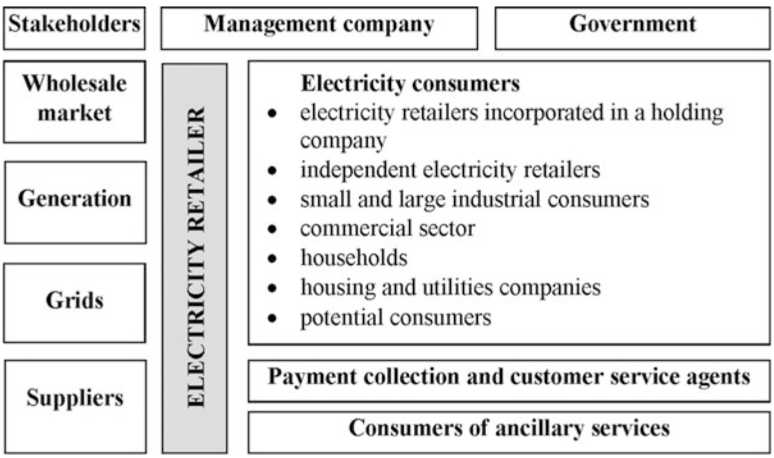

Fig. 2 Customer structure of energy retailer

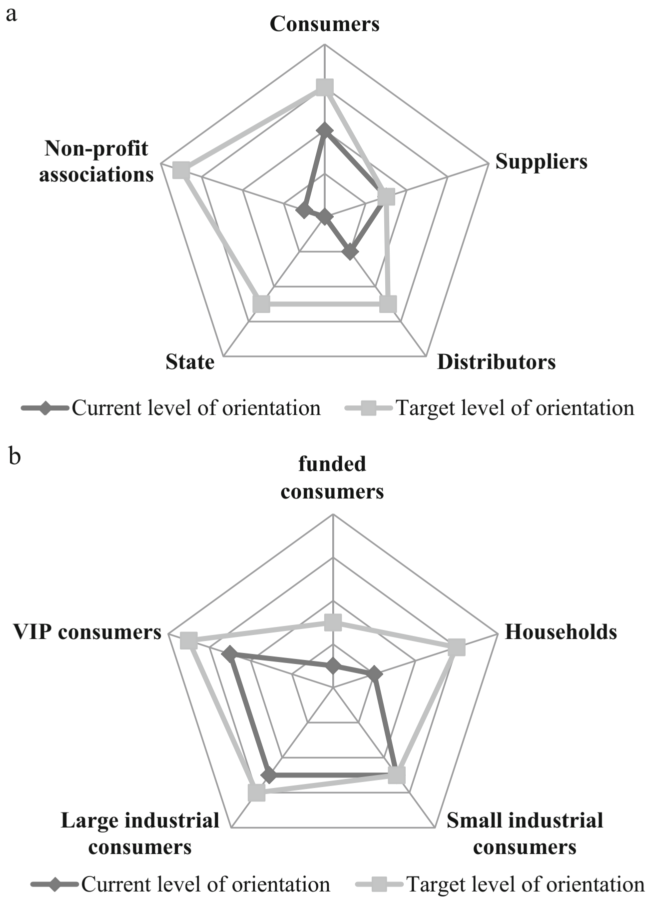

Fig. 3 Example of comprehensive assessment of customer-focused management approach. (**a**) Based on full list of objects of focus. (**b**) Based on expanded group of identical objects

adjustment has to happen regularly or constantly, the Company cannot avoid redesigning its management system and re-engineering its business processes appropriately [2].

Modern information technologies make it much cheaper to launch the orientation process once and keep it up later on, rather than carry out periodic surveys which require a lot of resources. We would like to emphasize that keeping the customer base constantly up to date later on is not only cheaper than periodic surveys but is also less annoying to customers because it occurs unobtrusively in the course of routine transactions.

The next step is to choose a management style of the two available options: management by disturbance and management by exception. Management by disturbance, unlike management by exception, stipulates that the system should be adjusted as soon as changes in the customer mix or individual customer

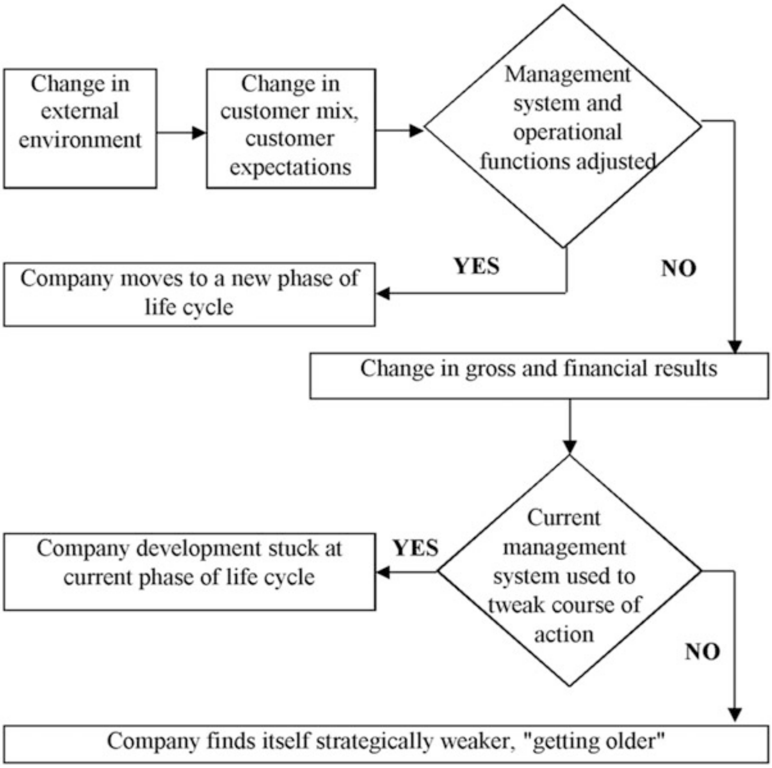

Fig. 4 Advantages of managing customer orientation by disturbance

characteristics are revealed. For the management approach to work, the Company needs to be able to perform monitoring and forecasting, as well as to design control activities within a limited timeframe and respond to them (Fig. 4).

Management by disturbance is more difficult to arrange and costlier to employ than management by exception. It is, therefore, necessary to decide whether it will prove effective for managing customer focus with regard to a certain customer group. In summary, to evaluate the customer-oriented approach used by a company, one should:

- Define the orientation field of the Company, i.e. the customer mix that the Company focuses its business on in order to achieve its strategic goals.
- Establish the current and set the target level of customer orientation for each customer (or group of customers) in the orientation field, thus identifying the Company's orientation potential.
- Determine the frequency of orientation for various groups of customers.
- Identify the current approach to customer-oriented management and set the target one for each group of customers and decide whether management by exception is sufficient or it should be replaced with management by disturbance.

- Map out the current state of customer-oriented interaction and set the target state of customer-oriented interaction, including factors that the company would want to modify when adopting proactive management practices.

4 Differential Electricity Pricing

Dynamic pricing is an example of a customer-oriented approach used by electricity retailers. Dynamic tariffs are offered to consumers who agree to supply interruptions during times of peak demand in return for monetary benefits in the form of discounts. The size of the discount depends on the number of interruptions during the billing period, their duration and the volume of undelivered electricity (capacity) per break. The consumer chooses the desired parameters from a "menu" proposed by the energy company.

Dynamic tariffs are, therefore, designed to reduce systemic costs of electric power companies and lower electricity bills for consumers by increasing prices during peak hours and decreasing them during off-peak hours [3, 4].

Applying various tariffs has different impacts on the level of economic risk borne by energy consumers and utilities. For example, from the point of view of consumers, traditional fixed tariffs are the least risky because the rates do not depend either on the amount of electricity consumed or the time of consumption. On the contrary, such tariffs are extremely inconvenient to the utility because during peak hours it produces electricity at a loss. Figure 5 illustrates how the risk borne by energy market participants depends on tariffs.

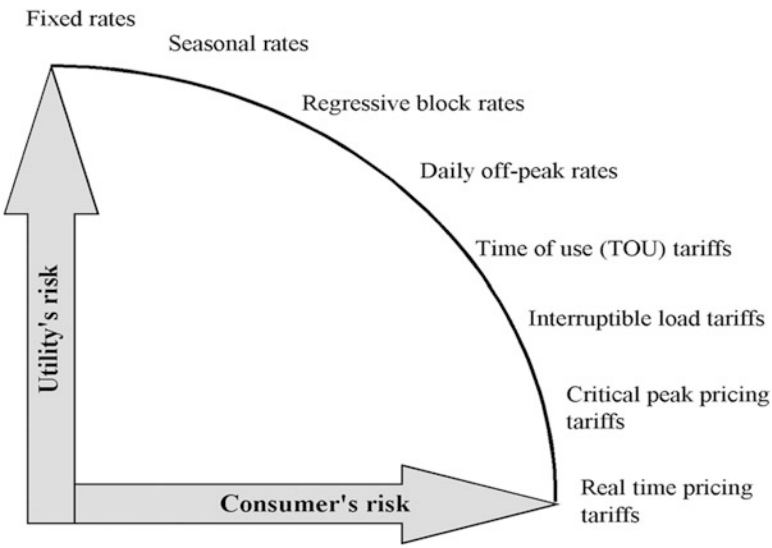

Fig. 5 Markets' risks of the utility depending on the tariff in effect

5 Conclusion

The proposed system for evaluating a customer-oriented management approach makes it possible to clearly and explicitly set objectives for a course of action aimed at transforming the management system in an electricity retail sales company, to build a marketing concept, to structure the current marketing activity integrated into the business processes of the company and to make decisions with regard to its product policy and modify its tariff menu. The combination of these makes the utility more competitive and solidifies its market positions.

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