Managing Customer Value is Critical to Achieving Full Profit Potential

Value

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"The value decade is upon us", stated Jack Welch, CEO of General Electric in 1992 when describing one of the key trends of the 1990's.

It is generally accepted today that for a company to grow and achieve its full profit potential it must maximize customer value. Even though we are well into the value decade, there still remains much confusion as to:

1) What is meant by customer value?

2) How do you measure customer value?

3) How do you manage customer value?

To the first question, "What is customer value?" We have developed a definition (see box) which underlies its work with clients. Understanding what customer value is will be discussed further on Pg. 2 of this newsletter.

Instrumental in managing customer value, is the question of "How to measure customer value?" As the saying goes, "You can't manage what you don't measure". In the feature article on Pg. 2-3 of this newsletter, we have outlined the key elements of value from
the customer's perspective, together with a useful approach to assist you in beginning to measure the value delivered to customers relative to competition.
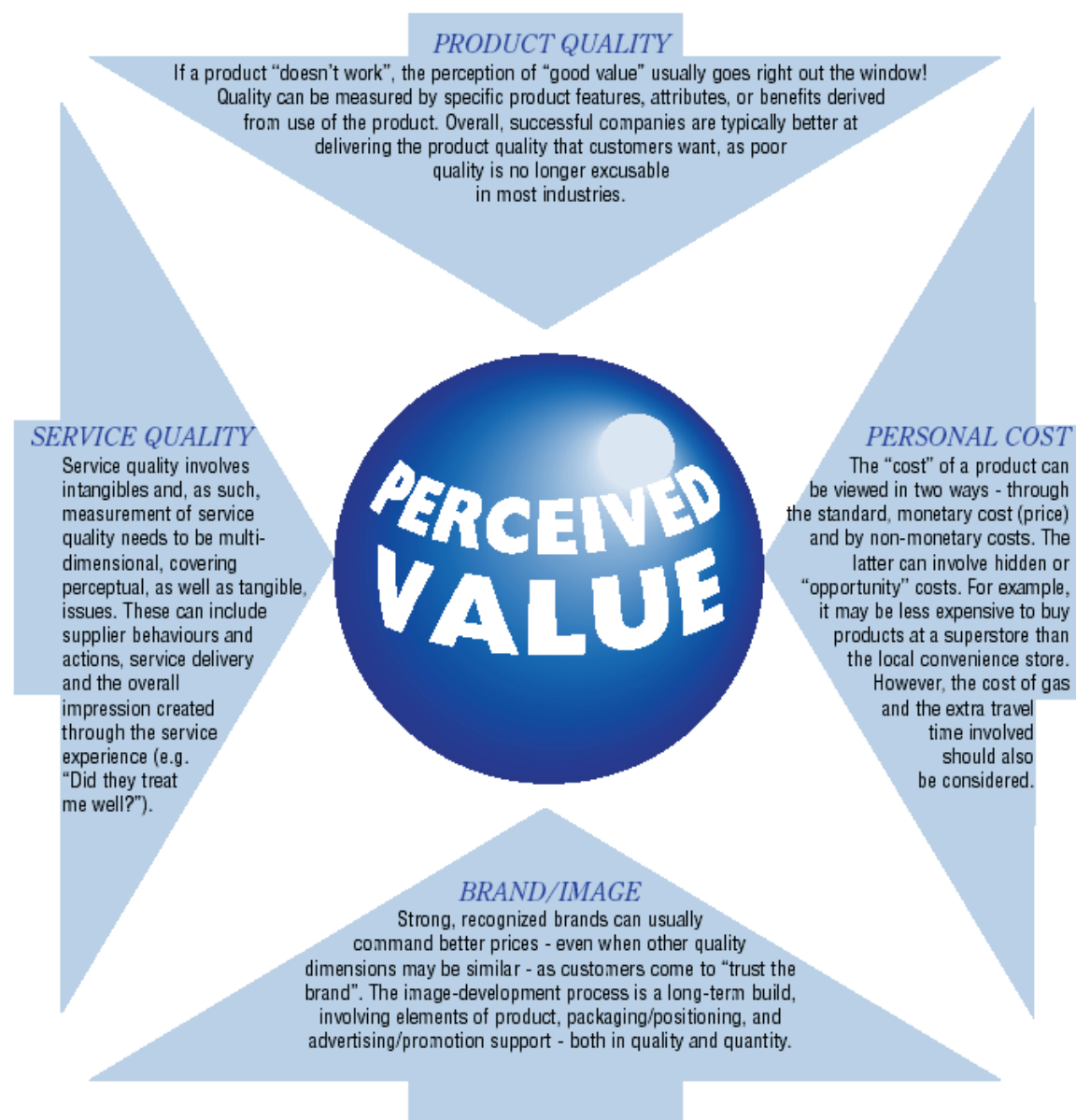
A COMPANY GROWS IN THREE WAYS:	THE ROLE OF CUSTOMER VALUE:
1. Acquiring New Customers	• Ensuring customers see more value in their relationship with your company than with competitors
2. Enhancing Profitability of Existing Customers	• Offering added-value/value added • Focusing on high profit customers that see high value in your offering • Optimizing the price customers are willing to pay
3. Extending Duration of Customer Relationships	• Maximizing retention/minimizing defections

PRICING
solutions

Finally as to "How you manage customer value?" this is dependent upon what you are trying to achieve. It is important to understand how a company grows and the different roles that value plays in this. For example, the role varies depending on whether: you are trying to acquire new customers; enhance the profitability of existing customers; or, extend the duration of customer relationships. (*See chart on previous page.*)

CUSTOMER VALUE IS …

In setting out to manage customer value, you may grapple first with the concept of how customers **perceive** value. The definition on the preceding page is an all encompassing starting point but to clarify how customers perceive value, the diagram summarizes the **four foundations of perceived value**: Product Quality, Service Quality, Brand Image and Personal Cost.

PRODUCT QUALITY

If a product "doesn't work", the perception of "good value" usually goes right out the window! Quality can be measured by specific product features, attributes, or benefits derived from use of the product. Overall, successful companies are typically better at delivering the product quality that customers want, as poor quality is no longer excusable in most industries.

SERVICE QUALITY

Service quality involves intangibles and, as such, measurement of service quality needs to be multi-dimensional, covering perceptual, as well as tangible, issues. These can include supplier behaviours and actions, service delivery and the overall impression created through the service experience (e.g. "Did they treat me well?").

PERCEIVED VALUE

PERSONAL COST

The "cost" of a product can be viewed in two ways - through the standard, monetary cost (price) and by non-monetary costs. The latter can involve hidden or "opportunity" costs. For example, it may be less expensive to buy products at a superstore than the local convenience store. However, the cost of gas and the extra travel time involved should also be considered.

BRAND/IMAGE

Strong, recognized brands can usually command better prices - even when other quality dimensions may be similar - as customers come to "trust the brand". The image-development process is a long-term build, involving elements of product, packaging/positioning, and advertising/promotion support - both in quality and quantity.

Companies that are successful at determining customer value are good at properly weighting the four value foundations and then determining the specifications that will create the benefits the customer is seeking. Developing specifications that link to the appropriate benefits involves answering the following questions for each of the four foundations:

1) What are the benefits/consequences that the customer is seeking?
2) Which attributes will create those benefits/consequences?
3) What specifications will ensure we deliver on those attributes?

In future newsletters we will provide further insights into how to answer these questions.

MEASURING CUSTOMER VALUE

Understanding what is meant by customer value is only the first step. The following is a systematic approach to measuring customer value referred to as the Perceived Value Measurement Model. It is based upon sound research and can be an extremely powerful management tool. It is a four step process:

1) Identifying key value drivers;
2) Weighting these key value drivers;
3) Benchmarking yourself against competitors; and,
4) Analyzing the results and taking action.

The following example illustrates a simplified approach for measuring perceived customer value. In real world situations, perceived value should be measured both at the benefits/consequences and at attribute levels. However, in this example, we will limit measurement to the attribute level.

<u>**EXAMPLE**</u>

Company: *Mega Corp*
Industry: *Hotels*
Core Market: *Business Customers*
Situation: *Executives of Mega Corp are trying to improve the competitiveness of one of their hotels versus a nearby competitor (Hotel X)*

Step 1.
Identify the attributes which drive value for business customers and influence their buying decisions.

The company undertook Customer Value Determination (CVD) research which identified the value drivers of this customer segment. The table below lists these value drivers as attributes derived from this research and the degree to which they influence the buying decision.

Step 2.
Determine how customers rate you vs. competitors on these value drivers.

Customer satisfaction research and competitive benchmarking show how business customers rate Mega Corp against the competition on the key value drivers (*see Step 2 of table*).

Step 3.
Determine your total perceived value (P V)* relative to competitors.

Perceived value is calculated for both hotels by determining the weighted average of the importance weighting and performance score (ie., Step 1 x Step 2 = P V measurement). (*See Step 3 of the table.*)

Step 4.
Analyze the results and take action.

In this case the results indicate that Hotel X is delivering the most value to the business customer market segment (880 vs. 800). This is the case even though it has the highest price. Better service, more comfortable rooms and better amenities are giving it a value edge. Because Hotel X is delivering more value it will gain market share while Mega Corp will lose market share.
To offset the lower value rating of their hotel, the Mega Corp hotel executives must now identify how they are going to go about improving the position of their hotel relative to its competitor. If they do not wish to lower price even further then they must do one
of the following:

   • *Improve its performance rating on the other attributes;*
   • *Try to alter the attributes used by the customer to determine value (e.g., introduce a loyalty program); or,*
   • *Target segments of the market which are more price sensitive.*

STEP 1		STEP 2		STEP 3	
Value Driver/Attribute	% Buying Decision	Rating of Mega Corp	Rating of Hotel X	P V* Mega Corp	P V* Hotel X
Affordable (Price)	35	10	7	350	245
Good Service	30	8	10	240	300
Comfortable Room	20	6	10	120	200
Good Amenities	10	5	9	50	90
Welcoming Lobby	5	8	9	40	45
Total	100	—	—	(800)	(880)

Total Perceived Value

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