



## Services growth options for B2B product-centric businesses

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### ABSTRACT

Many B2B companies that have traditionally been product-centric businesses (PCBs) are addressing the services opportunity (servitization), providing services aligned with customers' operations and/or that address products from other suppliers. The purpose of this paper is to create a new typology through which PCBs' services strategies can be categorised using these two dimensions, which is used to explore four services strategies and three growth options. Companies selling less complex products predominantly use services to enhance product differentiation, whereas those selling more complex products often undergo servitization, with opportunities and risks from each growth option. The risks of providing operations services are particularly noted since their successful provision requires significant changes to a PCB's activities. The results provide a critique of resource-based theory, specifically those resources that enable PCBs to create market differentiation through services. The importance of relational resources increases as services strategies involve products from other suppliers and customers' operations.

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### 1. Introduction

This article concerns companies which have been traditionally product-based and which are now using services as a strategy for market differentiation: the 'servitization of manufacturing' as described by Neely (2008). The word 'traditionally' is used because some such companies have re-aligned their focus towards services, which may now represent the majority of their revenue. For this research, these companies have been termed product-centric businesses or PCBs (Brechtbühl, 2004), the focus of the study being on business-to-business (B2B) markets in the United Kingdom (UK). The range of companies within this categorization is broad, it being possible to identify three groups according to Mathieu's (2001a) typology based on 'organisational intensity', i.e. the strength and scope of the impact of services on the firm. Firstly, there are those companies with a 'tactical' commitment to services, which undertake specific actions within the product marketing mix that have a limited impact on the company overall, e.g. an extended product warranty. Secondly, there are those with a 'strategic' commitment to services, which involves adding a key competency to a firm's portfolio, without changing its mission, e.g. a new technical support service. Thirdly, there are those with a 'cultural' commitment to services, which reshapes the mission of the firm, e.g. redefining the company as a services rather than product organisation.

Oliva and Kallenberg (2003) offer three contentions as to why B2B PCBs enter the services market, these being competitive, economic and customer-based, which are set out here together with other authors making similar contentions. Firstly, in terms of competitive arguments, services are harder for overseas competitors to imitate and for customers to procure via online reverse auctions, since they are intangible and provide a supplier with flexibility as an important element of a differentiation strategy (Michel, Naudé, Salle & Valla, 2003). Secondly, in terms of economic arguments, services can deliver a new sustainable source of revenue to the company (Potts, 1998) and re-build company profits (Mathe & Shapiro, 1993). In addition, sales of services are to some extent counter-cyclical to sales of products (Davies, 2003) and in some industries the services market is four or five times the size of the product market (Bundschuh & Dezvane, 2003). Thirdly, the customer-based arguments assert that customers of PCBs are increasingly focusing on their core operations and outsourcing many of their other business activities (Brown, 2000). A supplier that has already provided products is potentially well placed to win this business since it already has an established relationship with the customer and perceived expertise concerning these products (Wise & Baumgartner, 1999).

This research is focused on 'services', rather than 'service', with Parasuraman (1998) describing the former as 'intangible products' and the latter as more akin to the overall quality of service provided by a supplier as perceived by the customer, which will always accompany the core offering be it tangible or intangible. The baseline criterion for companies involved in this research is, therefore, that they offer services, although as Lovelock and Wirtz (2007) stated, services may be offered 'free' (i.e. the cost bundled in with that of the product) or charged for separately. Within the scope of services, there

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are those closely linked to a company's products, e.g. equipment installation ('product services' as defined by Mathieu (2001a)) and those that are more standalone entities, e.g. consultancy ('service as a product' as defined by Mathieu (2001a)). Although the importance of services for PCBs is accepted by most commentators, there is less unanimity about which services strategies should be followed, with some commentators noting the importance for PCBs of moving from offering services closely aligned to their own products (e.g. Frohlich & Dixon, 2001) to offering those more closely aligned with customers' business operational activities (e.g. Gebauer, 2008). Other commentators note the importance of services which relate to other original equipment manufacturers' (OEMs') products (e.g. Davies, Brady & Hobday, 2007).

Given the lack of clarity in the extant literature about which services strategies PCBs should adopt, the purpose of this paper is to propose a unifying typology which enables the placing of each PCB within a broad grouping based on the strategy it is currently following. This will enable managers in PCBs to assess the opportunities and risks involved in changing their strategies as part of the servitization process. The first objective of this paper is, therefore, to create a new typology through which PCBs' services strategies can be categorised. The typology is based on two dimensions: firstly, the product or customer orientation of a PCB's services, i.e. services are either closely linked to products (product-attached services) or to the customer environment (operations services). Secondly, the multi-vendor orientation of a PCB's services, i.e. a company's focus is on its own products or includes other companies' products as well, which may be competitive in nature. The second objective of the paper is to make a contribution to the theory underpinning this research, namely the resource-advantage (R-A) theory (Hunt, Arnett & Madhavaram, 2006), in particular the issue of how a company's resources are used to create competitive advantage. R-A theory emphasizes the potential of operand and operant resources to achieve this aim whilst other academics stress the pre-eminence of operant resources (Vargo & Lusch, 2006), relationships within a firm's network (Gadde, Huemer & Håkansson, 2003) or its relationships with customers in particular (Parvatiyar & Sheth, 2000). The relative importance of these approaches is discussed in light of the strategies derived from the typology.

The questions for this research are firstly, to investigate which services strategies PCBs currently adopt, based on the new typology, and secondly, to hypothesise which growth options might be most appropriate, based on the opportunities and risks of each. The research is based on interviews across a wide range of industrial sectors with 40 senior managers in 25 large PCBs that are using services as a market differentiator. For example, it includes companies selling commodity products such as metals, chemicals and products from quarrying. Equally, it includes companies selling complex electrical products in the information technology (IT), telecommunications, medical equipment, transport and aerospace sectors (see Appendix A for an anonymized list of participating companies).

The paper starts with a literature review, which is followed by the methodology, results and conclusion. Finally, the managerial implications of the study are discussed and possible areas of future research were suggested.

## 2. Literature review

### 2.1. Theoretical framework

The theoretical framework for this research is based on the resource-advantage (R-A) theory (Hunt et al., 2006). According to R-A theory, competition in an industry is based on firms seeking comparative advantages over rivals using the heterogeneous resources they control that will yield competitive advantage and potentially superior financial performance. Resources are either financial (e.g.

cash), physical (e.g. plant), legal (e.g. trademarks), human (e.g. the skills of individual employees), informational (e.g. knowledge from consumers), relational (e.g. relationships with suppliers and customers) or organisational (e.g. company policies or culture). Hunt and Madhavaram (2006) note that these resources are either 'operand' (financial, physical, and legal) or 'operant' (human, informational, organisational, and relational). The authors propose that under R-A theory, each firm will have some resources that are unique to it which could represent a source of long-term competitive advantage.

Whilst R-A theory signifies operand and operant resources as potentially able to deliver competitive advantage to firms, the importance of operant resources is emphasized by Vargo and Lusch (2008) through their analysis of two logical positions – goods-dominant (GD) logic, which is based on tangible products as units of output (although it could also include intangible services), and service-dominant (SD) logic, in which 'service' is the fundamental purpose of economic exchange and is how customer value is created. The authors reject the traditional classification of goods and services, with goods seen as appliances that serve as alternatives to direct service provision. In a previous paper (Vargo & Lusch, 2006) the authors argue that GD-logic is synonymous with operand resources including the firm's products whilst SD-logic is synonymous with operant resources including the knowledge and skills of the firm's employees. Lusch and Vargo (2006) also emphasize an important principal of SD-logic, namely that the customer is a co-creator of value rather than value being something that is added to products in the production process, which the authors see as being synonymous with GD-logic.

R-A theory provides a valuable framework for assessing the services strategies PCBs might follow, based on three broad approaches: firstly, PCBs developing services related to their own products, for which the products are important physical resources; secondly, PCBs adopting a stronger focus on services in the customer's operational environment, for which relationships with customers are important relational resources, although own products are also still important; and thirdly, PCBs developing services which are less dependent on their own products, with relationships with customers and other suppliers important relational resources.

### 2.2. Services linked to a PCB's own products

Services which are closely linked to a PCB's own products are often used to help create product differentiation (Michel et al., 2003). Service makes up one part of what Porter (1998) describes as the 'Value Chain' with sustainable competitive advantage (SCA) being achievable through each activity in the chain. Porter (1998) proposes that market differentiation comes from firms in the same industry having a different value chain and, therefore, competing on a different basis from each other. For activities that maintain and enhance the product's value, he gives examples of customer support, repairs, installation, training, spares, spare parts management and upgrades. Frohlich and Dixon (2001) adopt a similar approach to Porter (1998) and view after-sales services as a 'competitive capability' for manufacturing companies, along with others including price, flexibility, product quality and delivery. Other academics also note the importance of PCBs selling services, e.g. Kotler (1999) states that services provide 'relevant' and 'distinctive' product differentiation; Grönroos (2000) declares that manufacturers have started to see the strategic value in the combined package of products and services they offer to customers to develop and maintain SCA; Michel et al. (2003) suggest that the key factors for success in a B2B environment could be service-based, e.g. presales, after-sales or based on the skills of the salesforce. Gebauer (2008) defines companies following this strategy as 'After-sales Service Providers' or ASPs, whereby services are standardized, pre-defined and priced individually.

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