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Value quantification capabilities in industrial markets

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ABSTRACT

This study explores the origins and benefits of value quantification capabilities in industrial markets. After polling 131 US industrial sales and account managers, this study finds that value quantification capabilities improve firm—but not individual sales manager—performance. Second, in stable markets, the effect of value quantification capabilities on firm performance is stronger than in dynamic markets. Third, the study finds that the following psychological traits are positively related to the individual value quantification capability: risk taking and creativity, sales manager questioning style, customer-oriented selling, and cross-functional collaboration. This study suggests that value quantification capabilities benefit firm performance especially in stable markets, it explores attitudinal and behavioural traits underlying value quantification capabilities, and it highlights the need for further studies exploring the circumstances under which value quantification capabilities improve individual sales manager performance.

1. Introduction

What sets pricing in business markets apart? After all, the activities required for effective pricing in consumer markets—an analysis of customer needs, customer willingness to pay, competitive advantages, competitor price levels, and cost structures—are equally relevant for pricing in business markets. What is it that fundamentally distinguishes pricing in B2B from pricing in B2C?

The fundamental difference is this: in business markets, pricing is all about quantifying value, documenting that the price is less than the quantified sum of customer benefits. Anderson, Narus, and Van Rossum (2006, p. 96) observe: "To make customer value propositions persuasive, [B2B] suppliers must be able to demonstrate and document them." Value quantification is clearly not necessary in consumer markets: Coca Cola does not have to quantify to customers that its price premium over its main competitor—typically around 10%—is less than the incremental customer value provided. Individual consumers implicitly make this value quantification and then decide accordingly (i.e., purchase/no purchase).

In B2B, by contrast, purchasing managers quantify the value of alternative offers in their supplier selection decisions (Plank & Ferrin, 2002). In addition, these purchasing managers demand that B2B sellers themselves quantify value: A survey of 100 IT buyers at Fortune 1000 firms reveals that 81% of buyers expect vendors to quantify the financial value proposition of their solutions (Ernst & Young, 2002); a subsequent survey asks 600 IT buyers about major shortcomings in their suppliers' sales and marketing organizations (McMurchy, 2008): IT buyers consider an inability to quantify the value proposition and an inability to clarify its business impact as important supplier weaknesses. These surveys indicate that purchasing managers consider the ability to quantify the financial impact of the value proposition as very important in the vendor selection process. How well do sales managers quantify value? Both practitioner (Ernst & Young, 2002) and academic research (Anderson, Kumar, & Narus, 2007; Hinterhuber, 2008) suggest that most companies struggle to convert their value propositions into quantified customer benefits. There is thus a gap between the capabilities that industrial buyers demand and the capabilities that industrial sellers have regarding value quantification.

This gap raises a question: Does value quantification improve performance in industrial markets? Academic research suggests that it does; however, sparse evidence from practitioners appears, surprisingly, mixed. Qualitative research indicates that the performance of sellers in B2B—measured via realized price levels and win rates—improves as a result of value quantification (Anderson, Narus, & Narayandas, 2008; Töytäri, Brashear, Parvinen, Ollila, & Rosendahl, 2011). Practitioners are split on the question of whether value quantification is beneficial in B2B. On one side, companies such as SKF, SAP, HP, Grainger, Metso, Applied Industrial, Maersk and others recognize the benefits of value quantification. Tom Johnstone (2007), CEO of SKF, states: "One of the most important tasks we have today throughout the SKF Group is to create, deliver, and document the value that our products and solutions bring to our customers." Similarly, Matti Kähkönen (2012, p. 21), CEO of Metso, says: "Understanding of customers' businesses and KPIs [key performance indicators] create[s] a solid basis for quantifying the business impact for the customer."

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Other industrial companies, such as Black & Decker, seem to take a different view: having lost its position as market share leader to Makita, the company regained the number one position in industrial power tools in the mid-1990s in one of marketing history's most spectacular turnarounds. A key element of Black & Decker's strategy, the launch of DeWalt in the professional power tool market, was an exclusive focus on product attributes, specifications, and features in marketing communication, thus leaving it to B2B customers themselves to understand and quantify value (Dolan, 1998). Communicating product benefits and value risked, according to Joe Galli, VP of marketing and sales, “consumerizing” an essentially industrial product (Dolan, 1996).

Contrasting views on the benefits of value quantification are evident also from the interviews underpinning this study. One interviewee (Hinterhuber & Heutger, 2017, p. 154) suggests that value quantification is always beneficial (see Section 3 for details):

> And even if you're not obliged to quantify the value to get the business, I would still advocate doing it. You can always go to the customer at a later date and say, “Hey! Look, this is what we did for you.” This certainly helps to keep customers loyal and increase renewal rates . … I think it [i.e., value quantification] does always work.
> [Heutger, SVP Strategy and Marketing, DHL]

Another interviewee suggests that value quantification is not beneficial in highly commoditized markets (see Section 3 for the detailed quote). According to that interviewee, the benefits of value quantification are contingent on market characteristics.

Once again: Does value quantification always influence firm performance? And if so, under which circumstances are value quantification capabilities less beneficial? The existing literature does not appear to answers these fundamental questions. If value quantification indeed benefits firm performance, it should be clear what makes some sales managers more effective and others less so in value quantification. It is not. The purpose of the present study is to explore whether value quantification improves sales performance in B2B.

To answer these questions, this study surveys 131 US B2B sales and account managers to explore antecedents and consequences of value quantification. This study finds that value quantification capabilities are positively related to firm—but not to individual sales manager—performance. The data also suggest that this positive relationship is weaker in highly dynamic markets. Finally, this study identifies the psychological characteristics and behaviors at the level of the individual sales and account manager that are positively related to the value quantification capability. These characteristics are risk taking and creativity, sales manager questioning style, customer-oriented sales, and cross-functional collaboration. This study contributes to the understanding of the micro-foundations of value quantification capabilities at the level of individual sales managers and highlights the benefits of quantifying value in industrial markets. The study finally points towards the need to better understand the relationship between individual value quantification capabilities and individual performance.

2. Theoretical foundations

Three main research streams constitute the theoretical foundations of this paper: research on customer value, on selling, and on value-based pricing. Keränen and Jalkala (2013) and Terho, Haas, Eggert, and Ulaga (2012) provide thorough summaries of the literature on customer value: in line with earlier research equating value with customer benefits received (Zeithaml, 1988), scholars nowadays tend to conceptualize value in B2B as the incremental impact of a supplier's offer on the customer's own bottom line (Nagle & Holden, 2002). Value in business markets “is the worth in monetary terms of the economic, technical, service, and social benefits a customer firm receives in exchange for the price it pays for a market offering” (Anderson et al., 2008, p. 6). Customer value is the maximum amount that a customer is willing to pay to obtain the supplier's products and services. In B2B, customer value comes in two forms: quantitative customer benefits (i.e., cost reductions, margin improvements, risk reductions, capital savings) and qualitative customer benefits (e.g., intangible advantages). Value in B2B is subjective, customer-specific, relative to the customer's best alternative, discovered collaboratively with customers, and expressed in monetary terms.

Value and price are two separate constructs: changing one does not change the other (Hinterhuber, 2004; Wouters, 2010). The critical capability in industrial markets is value quantification or value visualization (Kindström, Kowalkowski, & Nordin, 2012): “Understanding customer value in business markets involves monetary quantification of the benefits of a firm's offering, yet, from the perspective of the customer firm” (Wouters, 2010, p. 1101). “A key to becoming part of customers' strategic agenda is the ability to quantify the business impact” (Storbacka, 2011, p. 706). Value quantification is necessary because customers, by themselves, generally fail to recognize value even when they see it: “One of the great misconceptions of quantitative pricing research is that customers who have been using a product know what it is worth to them without being told” (Nagle & Cressman, 2002, p. 33).

Value quantification is thus an important communication tool. Current research suggests that high-performing companies quantify and document value (Anderson et al., 2007; Anderson et al., 2008; Töytäri & Rajala, 2015), but so far this claim has not been substantiated by quantitative evidence. It is—in theory at least—possible that value quantification is an intellectually appealing idea where isolated cases of success studies mask the fact that for most companies the pursuit of this strategy substantially reduces performance, as is true for the popular concept of solution selling (Krishnamurthy, Johansson, & Schlissberg, 2003; Roegner & Gobbi, 2001). It is furthermore possible that the benefits of value quantification are contingent on firm-specific or environmental factors.

Research on selling has witnessed a surge of interest only recently. Traditionally, top marketing journals published a small and declining number of papers on sales management (Plouffe, Williams, & Wachner, 2008; Richards, Moncrief, & Marshall, 2010). This situation has changed: current research recognizes the importance of selling and finds that how selling is performed has a substantial impact on company performance (Haas, Snehota, & Corsaro, 2012). Among different approaches to selling that the literature discusses (Terho et al., 2012), value-based selling is most pertinent to the current study. Value-based selling comprises several overlapping steps: customer identification, customer needs analysis, value proposition development, value quantification, value-based pricing, post-delivery value verification and documentation, and development of case repositories (Terho et al., 2012; Töytäri & Rajala, 2015; Töytäri et al., 2011). Value quantification is a cornerstone and, at the same time, the “biggest challenge” of value-based selling (Töytäri & Rajala, 2015, p. 105). The literature examines the capabilities (Töytäri & Rajala, 2015) and performance implications of value-based selling (Terho, Eggert, Haas, & Ulaga, 2015). The factors that enable sales managers to quantify value, however, are yet to be fully explored.

The value quantification capability refers to the ability to translate a firm's competitive advantages into quantified, monetary customer benefits. The value quantification capability requires that the sales manager translates both quantitative customer benefits—revenue/gross margin increases, cost reductions, risk reductions, and capital expense savings—and qualitative customer benefits—such as ease of doing business, customer relationships, industry experience, brand value, emotional benefits or other process benefits—into one monetary value equating total customer benefits received. Value quantification demands more from sales managers than merely quantifying the total cost of ownership (Piscopo, Johnston, & Bellenger, 2008).

An important clarification concerns the relationship between value-based pricing and performance pricing. Value-based pricing refers to an ex-ante payment scheme where prices reflect customer willingness to