BAB 4

SIMPULAN

Simpulan yang dapat diajukan berdasarkan hasil pembahasan yang dilakukan, antara lain adalah sebagai berikut :

1. *Relationship Value Management* (RVM) bertujuan untuk mengatur seluruh kesepakatan perusahaan dengan pelanggan baru potensial, dan juga merupakan bisnis dan penerapan teknologi yang menggunakan sistem informasi bagi keseluruhan proses bisnis yang dikelilingi oleh interaksi perusahaan dengan pelanggan penjualan, pemasaran dan pelayanan.
2. Pendekatan karyawan dilakukan dengan menggunakan *behavior base* yaitu pendekatan perilaku ini sangat penting dan masuk akal dalam penerapan kompetensi pada masing-masing karyawan. Melalui pendekatan ini tidak hanya memudahkan karyawan yang bersangkutan dalam mengukur penerapannya, namun juga bagi atasan dan mungkin juga konsultan dalam melakukan penilaian.
3. Pelanggan merupakan penilai terakhir dari kualitas dan oleh karena itu prioritas utama dalam jaminan kualitas adalah memiliki piranti yang handal dan sahih mengenai penilaian konsumen terhadap perusahaan, maka diperlukan kerangka dalam manajemen kualitas dengan dua alasan pokok, yang meliputi: orientasi pemasaran dan orientasi internal perusahaan
4. Perlakuan yang sama terhadap para pemegang saham; peranan semua pihak yang berkepentingan (*stakeholders*) dalam *corporate governance*;

transparansi dan penjelasan; serta peranan Dewan Komisaris dan Komite untuk meningkatkan keberhasilan usaha dan akuntabilitas perusahaan guna mewujudkan nilai pemegang saham dalam jangka panjang dengan tetap memperhatikan kepentingan *stakeholder* lainnya, berlandaskan peraturan perundangan dan nilai-nilai etika.

DAFTAR KEPUSTAKAAN

Assad,. 2003. *Psikologi Industri*. Yogyakarta: BPFE.

Darmawati, D., Khomsiyah, dan Rahayu, R.G., 2005, Hubungan *Corporate Governance* dengan kinerja Perusahaan, *Jurnal Riset Akuntansi Indonesia* Vol 8 No.1.

Kotler, Philip, 1997, Majemen Pemasaran I, Edisi bahasa Indonesia, Prehalindo, Jakarta.

Mowen, John C., 1995, *Customer Behavior*, Fourth Edition, International Edition, Prentice Hall Inc: Englewood Cliffs, New Jersey.

Raphel, Murray, Raphel, Neil dan Janis S Raye. 2007. Panduan Lengkap untuk Kesetiaan Pelanggan. Jakarta: Gramedia Pustaka Utama.

Payne, Adrian. Holt, Sue dan Frow, Pennie. 2001. *Relationship Value Management Exploring the Integration of Employee, Customer and Shareholder Value and Enterprise Performance Models*..Journal of Marketing Management. 17.785-817.

Tjiptono, Fandy, 1997, *Strategi Pemasaran*, Edisi II Cetakan Kedua, Yogyakarta : Andi Offsets.

Tjiptono, Fandy dan Diana, Anastasia., 2003, *Total Quality Management*, Edisi kedua, Andi Offset Yogyakarta.

Yamit, Zulian, 2004, *Manajemen Kualitas Produk dan Jasa*, Ekonisia. Yogyakarta.

Journal of Marketing Management, 2001, 17, 785-817

Adrian Payne[1], Sue Holt and Pennie Frow

Cranfield University

Relationship Value Management: Exploring the Integration of Employee, Customer and Shareholder Value and Enterprise Performance Models

Value as a theme in the relationship marketing literature is gaining increasing attention. In particular, the synthesis of value concepts with a multi-stakeholder approach to relationship marketing has been the subject of recent interest. Building on earlier work, this article explores how key elements of relationship value can be integrated through a focus on three key stakeholder groups: employees, customers and shareholders. The linkages between employee value, customer value and shareholder value, including the research on the service-profit chain, are explored. The paper also explores the extent to which linkage models or enterprise performance models, which integrate these components of value, have been adopted by organisations. Two case studies are used to illustrate the practical application by organisations seeking to develop enterprise performance models.

Keywords: Customer Value; Employee Value; Enterprise Performance Models; Linkage Models; Service-Profit Chain; Relationship Value; Shareholder Value.

Introduction

Value and, in particular, relationship value has received increasing attention in the relationship marketing literature (Wilson and Jantrania 1993, 1994; Ravald and Grönroos 1996; Grönroos 1997; Tzokas and Saren 1998; Payne and Holt 1999; Gummesson 1999). Building on earlier research on relationship value management (Payne and Holt 1998), this paper seeks to integrate core concepts from the value literature with the multi-stakeholder approach to relationship marketing that has been the subject of much interest for a number of researchers (e.g. Christopher, Payne and Ballantyne 1991;

[1] *Correspondence*: Prof Adrian Payne, Cranfield School of Management, Cranfield University, Cranfield, Bedford, MK43 0AL, UK. Tel: +44 1234 751122, Fax: +44 1234 751806, email: a.payne@cranfield.ac.uk

ISSN1472-1376/2001/07/800785+32 £4.00/0

Kotler 1992; Morgan and Hunt 1994; Doyle 1995; Gummesson 1995). The authors explore this integration from the perspective of linkage or enterprise performance models (Merz 1999) and more specifically, with reference to the service-profit chain model (Heskett et al. 1994; Heskett, Sasser and Schlesinger 1997).

While many of the multi-stakeholder models of relationship marketing present a number of stakeholders ranging from six (Christopher et al. 1991) to thirty (Gummesson 1995), we suggest that three stakeholders groups are emerging as the core focus for organisations. These key stakeholders are *employees, customers* and *shareholders* and they represent the critical components of relationship value management.

This paper explores the concepts of employee value, customer value and shareholder value in the context of relationship marketing. It first briefly examines the concepts of employee, customer and shareholder value. It then looks at the emergence of the service-profit chain concept, which can be more generally described as a linkage model. Using findings from our research, the extent to which companies have adopted some of the key measures related to the service-profit chain is then examined.

While the service-profit chain concept has been the subject of recent academic interest, our research suggests that very few organisations are advanced in developing sophisticated enterprise performance models across the entire service-profit chain. To illustrate the potential of this approach we present two short case studies - one from the business-to-consumer sector and one from the business-to-business sector. These two case studies are used in this paper to show the linkages between employee, customer and shareholder value and to investigate how organisations are now seeking to develop enterprise performance models, which more completely measure the elements of relationship value. Finally, some conclusions regarding benefits of such models, barriers to their adoption, and future research in this area are discussed.

Relationship Value Management

The six markets model originally developed by Christopher et al. (1991) and more recently updated (Peck et al. 1999) is a multi-stakeholder model of relationship marketing. It classifies the organisation's stakeholders into six market domains including: customer markets, internal markets, supplier/alliance markets, referral markets, influence markets and recruitment markets. Payne and Holt (1998) used this model together with core concepts from the literature on value to propose a *relationship value management framework* (see Figure 1).

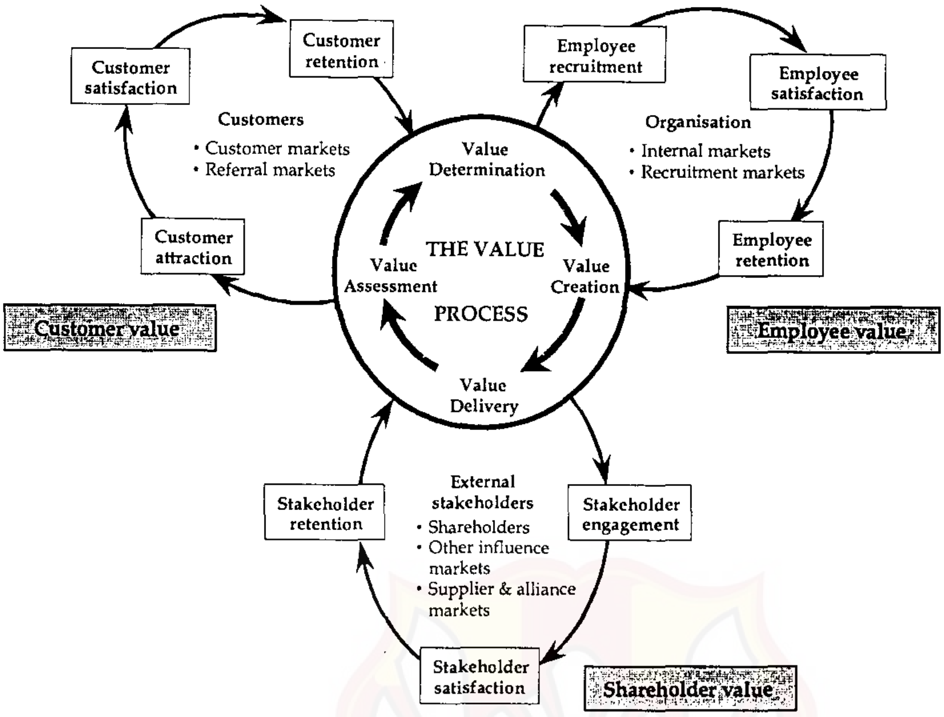

Figure 1. A Framework for Relationship Value Management
Source: Payne and Holt (1998)

This framework categorises the six stakeholders into three key stakeholder groups. Each of the three major stakeholder groups represents opportunities for value creation and delivery. Within these there are a number of key activities that have been represented as three circular sub-processes. The activities within the customer group are *customer attraction,* creating *customer satisfaction* and ensuring *customer retention.* Within the organisation group, they are *employee recruitment, employee satisfaction* and *employee retention.* The external stakeholder activities involve *stakeholder engagement* (engaging the right stakeholders, e.g. investors, suppliers and alliance partners), *stakeholder satisfaction* and *stakeholder retention* (retaining them and ensuring that their needs, e.g. shareholders, are satisfied). We argue that of the *external* stakeholder group *shareholders* are, for most companies, those of greatest significance in terms of value management. While these three stakeholder groups are shown as separate sub-processes, their *interdependence* also needs to be taken into account.

We contend that these three stakeholder groups or value domains, *employees, customers* and *shareholders* are emerging as the core focus for organisations in terms of value management and performance improvement.

Organisations need to focus on these groups not just for managing their relationships, but also for creating and delivering value (employee value, customer value and shareholder value) and for maximising and measuring their profitability and performance. This approach is endorsed by Reichheld (1996) who argues that these three key stakeholders - employees, customers, shareholders - are the 'forces of loyalty' and, while other stakeholders can have a major role to play, it is these three that are central to achieving success.

If the *value process* in the relationship value management framework is implemented for each stakeholder group, then the outcome should be the creation and delivery of *value* for each group; *employee value, customer value* and *shareholder value.* In implementing a value management approach, organisations need to take an *integrated* approach to managing these stakeholders by focusing not only on the relationships but also on the *linkages* between employee value, customer value and shareholder value. These linkages are now explored with reference to the literature.

Linkages Between Employee Value, Customer Value and Shareholder Value

Customer value and shareholder value as individual concepts have received considerable recent attention in the literature. For reviews of the literature on customer value see: e.g. Woodruff (1997) and, for shareholder value, see Wenner and LeBer (1989), Day and Fahey (1990), Stewart (1991), Slater and Olsen (1996), Bannister and Jesuthasan (1997), Cornelius and Davies (1997), and Dobbs and Coller (1998). The concept of employee value is probably less developed; for some discussion see Dolmat-Connell (1999) and McDonald et al. (2001). However, it is not the purpose of this paper to review these literatures but rather to explore those aspects of the literature that concentrate on the *linkages* and *relationships* between the concepts of employee, customer and shareholder value.

It is appropriate to start with a consideration of some of the key concepts that underpin the notions of employee, customer and shareholder value. Building on the key elements introduced above, Figure 2 outlines our view of the main themes which underpin these three value domains. This section of the paper examines some of the key linkages between the value domains and their component parts.

We reviewed a considerable amount of literature relating to these value domains and especially the linkages between them. Some of the literature deals with linkages between two variables while some explores a greater number of variables. The area is complex with many intervening and mediating variables and not every one of these variables and linkages has been fully explored in existing research. Further, the position of such variables in a sequential chain of variables, the paths between them and the most appropriate definition of the variable are still subject to some debate (Zahorick and Rust 1992; Roest and Pieters 1997; Hellier 1999).

Employee Value
- *Employee satisfaction*
- *Employee retention and loyalty*
- *Employee commitment*
- *Employee productivity*
- *Leadership*
- *Internal Service Quality*

Customer Value
- *Customer attraction*
- *Customer satisfaction*
- *Customer loyalty*
- *Customer retention*
- *Customer profitability*

Shareholder Value
- *Shareholder engagement*
- *Shareholder satisfaction*
- *Shareholder retention*
- *Lifetime profit flows*
- *Company growth*
- *Shareholder profitability*

Figure 2: Main Themes Underpinning the Employee, Customer and Shareholder Value Domains

In an attempt to bring some structure to this broad range of literature we have classified it into three areas, as follows: research exploring relationships between two or more variables which examines some (but not all) of the linkages within and across the value domains; the 'Harvard' service-profit chain stream of research; and other models, some later empirical testing of the service-profit chain and recent work towards building enterprise performance models. Some authors have contributed to more than one area. A map of this classification of research is shown in Figure 3. We now examine these three categories of literature and discuss a representative selection of key contributions from each category.

Research Exploring Relationships between some Variables Within and Across Elements of the Three Value Domains

A number of researchers have focused on the links between *employee satisfaction* and *customer satisfaction* and there is growing evidence that there is a relationship between employee satisfaction and customer satisfaction (Schneider 1973; Schneider, Parkington and Buxton 1980; Czepiel, Soloman

Figure 3: Mapping the Three Categories of Value Integration Literature

Research on *Specific Variables* and linkages within and across the three Value Domains

Employee Satisfaction and Customer Satisfaction: (e.g Schneider 1973; Schneider et al. 1980; Czepiel et al. 1985; Schneider & Bowen 1985a, 1985b; Schlesinger & Zornitsky 1991; Schlesinger & Heskett 1991; Wiley 1991; Rosenbluth & Peters 1992; Bycroft & Voegele 1994)

Employee Satisfaction, Customer Satisfaction and Customer Retention: (e.g Kelley 1990; Clark 1997)

Employee Satisfaction, Customer Satisfaction and Profitability: (e.g. Bernhardt et al. 1994)

Customer Value and Shareholder Value: (e.g Corpulsky 1991; Leemon 1995; Slywotsky 1996; Cleland & Bruno 1996, 1997; Slywotsky & Linthicum 1997; Laitamaki & Kordupleski 1997)

Customer Satisfaction and Customer Profitability: (e.g. Rust & Zahorick 1993; Rust et al. 1995)

Customer Satisfaction and ROI: (Anderson et al. 1994)

Customer Satisfaction and Customer Loyalty: (e.g Rust & Zahorik 1991; Fornell 1992; Boulding et al. 1992; Anderson & Sullivan 1993; Jones & Sasser 1995)

Customer Loyalty, Customer Retention and Customer Profitability: (e.g Reichheld & Sasser 1990; Reichheld & Kenny 1990; Dawkins & Reichheld 1990; Reichheld 1993,1996;)

Research on the 'Harvard' stream of work on the *Service-Profit Chain*

Early Influences on Research on the Service-Profit Chain thinking: (e.g Bennis 1970; Lawler 1973; Blau 1974; Sasser & Arbeit 1976; Parkington and Schneider 1979; Schneider & Bowen 1985a, 1985b; Johnson & Seymour 1985; Czepiel, Soloman & Surprenant 1985)

Services Research: (e.g. Heskett 1986; Heskett & Sasser 1990; Schlesinger & Heskett 1991; Heskett, Sasser & Hart 1990; Heskett & Schlesinger 1997)

Corporate Culture and Performance: (e.g. Kotter and Heskett 1992)

Service-Profit Chain: (e.g. Heskett, Jones, Loveman, Sasser & Schlesinger 1994; Heskett, Sasser & Schlesinger 1997; Hallowell 1997; Schlesinger and Hallowell 1993; Rucci, Kern & Quinn 1998; Sherman 1997; Loveman 1998; Laabs 1999; Loveman & Heskett 1999; Hallowell & Schlesinger 2000, forthcoming)

Alternative Approaches, Developments and ***Enterprise Performance Models***

Quality Models as Enterprise Performance Models: (Baldridge quality award – e.g. Garvin 1991; Main 1991 Blackburn & Rosen 1993; Taylor 1994. EFQM quality award - e.g. Hakes 1994; Nakhai and Neves 1994; Porter, Oakland & Gadd 1998)

The Balanced Scorecard as an Enterprise Performance Model: (e.g. Kaplan & Norton 1992, 1993)

Research on Related Models: (e.g. Bycroft & Voegele 1994; Bycroft 1996 a; Bycroft 1996 b)

Later Research on the Service-Profit Chain: (e.g Roth, Chase & Voss 1997; Rucci, Kern & Quinn 1998; Loveman 1998; Barber, Hayday & Bevan 1999)

Definition of an Enterprise Performance Model: (Merz 1999) and Surprenant 1985; Schneider and Bowen 1985a, 1985b; Schlesinger and Zornitsky 1991; Schlesinger and Heskett 1991; Wiley 1991; Rosenbluth and Peters 1992; Bycroft and Voegele 1994). Clark (1997) went further than simply looking at links between employees and customers by examining the impact of employee-customer relationships on customer retention rates thus adding a further link in the chain. Researchers also found that those employees in contact with customers (those in 'boundary roles') could suffer from a lack of role clarity. This in turn led to reduced levels of employee motivation and job satisfaction which could manifest itself in poor customer satisfaction and customer retention (Parkington and Schneider 1979; Kelley 1990). The links between employee satisfaction, customer satisfaction and profitability have also been explored (Bernhardt, Donthu and Kennett 1994). Understanding the impact of employees becomes more critical when applied to the services sector, because the intangibility of services often leads customers to rely on employee's behaviour in forming opinions about the service offering (Clark 1997).

The links between *customer value* and *shareholder value* have also been explored. There seems to be a hypothesis in much of the academic and practitioner literature that customer value drives shareholder value (e.g. Corpulsky 1991; Leemon 1995; Slywotzky 1996; Slywotzky and Linthicum 1997; Laitamäki and Kordupleski 1997) whilst others take the view that shareholder value drives customer value; by focusing on maximising shareholder value, it almost automatically necessitates pleasing customers (Cleland and Bruno 1996). Cleland and Bruno (1996, 1997) also argue that business strategies involving an understanding of the interdependencies between customer value and shareholder value should seriously be considered by organisations.

There is also increasing evidence that there is a positive link between *customer satisfaction* and *customer profitability*. Rust and Zahorik (1993) and Rust, Zahorik and Keiningham (1995), for example, outline procedures for assessing the impact of satisfaction and quality improvement efforts on customer profitability. Research by Anderson, Fornell and Lehmann (1994) also established positive relationships between customer satisfaction and return on investment.

From a slightly different perspective, Jones and Sasser (1995) looked in detail at the relationship between *customer satisfaction* and *customer loyalty*. Many other researchers (Rust and Zahorik 1991; Fornell 1992; Boulding et al. 1992; Anderson and Sullivan 1993) also reported a significant positive relationship between customer satisfaction and loyalty as described by Loveman and Heskett (1999).

Links between *customer loyalty*, *customer retention* and *customer profitability* have also been the focus of interest. Much early work in this area, e.g.

Reichheld and Sasser (1990), was undertaken by consulting firm Bain & Company. Loveman and Heskett (1999) describe how interest in this area (and indeed the links between customer satisfaction and profitability) was stimulated by the work of Buzzell and Gale (1987) and their Profit Impact of Market Share (PIMS) project. Reichheld and Sasser's research strongly suggested that it was customer loyalty rather than market share that was the primary determinant of profitability. Other influential work by Reichheld led to a stream of publications in this area, e.g Reichheld and Kenny 1990; Dawkins and Reichheld 1990; Reichheld 1993; Reichheld 1996. Grant and Schlesinger (1995) also looked at the mechanisms for improving customer relationships and customer profitability over time. These researchers recognised that simply acquiring customers was not enough. Companies needed to concentrate on retaining customers if they want to maximise their profitability. Indeed, Bain & Company brought customer satisfaction into the equation as well - "one of the key elements of business success and profitability is customer satisfaction, the more satisfied the customer, the more durable the relationship. And the longer this lasts, the more money the company stands to make" (Buchanan and Gillies 1990).

The above summary covers a representative selection of the work in this area. While much of this research established strong linkages or relationships between, for example, employees and customers, or customers and shareholders, none of it comprehensively linked employees, customers and shareholders in a single model. Indeed, in 1993 Rust and Zahorik concluded that there existed no published studies that had examined the entire chain of stakeholders. However, much of the above research has been directly influential in the development of a model that does link these three core areas - the *service-profit chain* developed and described by Heskett et al. (1994) and Heskett, Sasser and Schlesinger (1997). The history and development of the model is now discussed.

The 'Harvard' Service- Profit Chain Stream of Research

A number of scholars at the Harvard Business School coined the term service-profit chain to describe a significant body of research carried out by them within the Service Management Unit. In introducing the concept of the service-profit chain, shown at Figure 4, they recognised the importance of understanding the relationships between employees, customers and organisational performance. Heskett et al. (1997) state that there are 'direct and strong' relationships between 'profit; growth; customer loyalty; customer satisfaction; the value of goods and services delivered to customers; employee capability, satisfaction, loyalty and productivity'. Importantly, *value* is a central tenet of the service-profit chain.

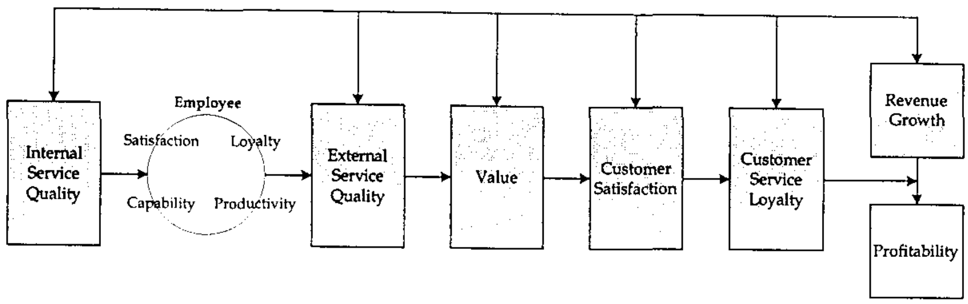

Figure 4: The Service-Profit Chain
Source: based on Loveman and Heskett (1999)

The service-profit chain model has its roots further back than in the literature discussed above. In their history of the service-profit chain, Loveman and Heskett (1999) describe what they call ' the service profit chain idea trail'; also see Hallowell and Schlesinger (2000). They state that the ideas underlying the concept can be traced back to the work of Bennis (1970), Lawler (1973) and Blau (1974) and their work on the organisation of work and its impact on quality, productivity and employee satisfaction and later research by Sasser and Arbeit (1976), Parkington and Schneider (1979), Schneider and Bowen (1985a, 1985b), Johnson and Seymour (1985) and Czepiel, Solomon and Surprenant (1985). The Harvard researchers' work is also derived from research undertaken by them in services management (e.g. Heskett 1986; Heskett and Sasser 1990; Schlesinger and Heskett 1991) and corporate culture and performance (e.g. Kotter and Heskett 1992). The work of Reichheld and Sasser (1990) on customer satisfaction and loyalty was also influential (Loveman 1998).

Throughout the 1990s the service-profit chain was developed and tested. Much of this research was done by case study work in a variety of service industries. These case studies included a considerable range of leading US organisations including Banc One, MBNA, Taco Bell, USAA and Southwest Airlines. They documented many relationships between elements of the chain based on this data. However, they noted that few firms had related all the linkages in a truly comprehensive way (Heskett et al. 1997: p31). Companies moving in this direction discovered strong and significant relationships between certain of the elements including: customer loyalty and company growth and profitability; employee satisfaction and customer satisfaction; and employee satisfaction and capability.

More recently, the researchers' work was extended to a regional bank. Here they investigated relationships more fully across the entire service-profit chain (Loveman 1998; Loveman and Heskett 1999). They found that customer satisfaction and employee satisfaction have a clear relationship and that it is possible to relate customer satisfaction to customer loyalty and to retention. They also report that the financial consequences of differences in customer behaviour are significant. Their main findings were: customer loyalty and customer satisfaction are positively correlated with profitability; customer satisfaction is positively correlated with customer loyalty; employee satisfaction is positively correlated with customer satisfaction; employee satisfaction is positively correlated with stated employee loyalty; and internal service quality is positively correlated with employee satisfaction. They state that, in summary, the bank data supports nearly all of the relationships posited by the service-profit chain.

However, they also recognise that more work needs to be done to properly establish *causality*. Work is still continuing on the development and refinement of the service-profit chain model with collection of longitudinal data that will allow the identification of 'causes and effects among elements in the chain' (Loveman and Heskett 1999).

While the Harvard team's work on the service-profit chain is the best known example of a *linkage model* that measures different elements of an organisation's performance, other work has also been undertaken to develop performance-based frameworks, enterprise-wide approaches and to further explore linkage models.

Alternative Approaches, Later Development of the Service-Profit Chain Concept and Enterprise Performance Models

In addition to the service-profit chain a number of other models have been developed which are concerned with measuring enterprise-wide performance. The service-profit chain model has close connections to earlier models developed in the quest for 'total quality' such as the Malcolm Baldridge award (e.g. Garvin 1991; Main 1991; Blackburn and Rosen 1993; Taylor 1993) and the European Foundation for Quality Management (EFQM) award (e.g. Nakhai and Neves 1994; Hakes 1994; Porter, Oakland and Gadd 1998). These quality models represent systems of measures for monitoring, controlling and communicating within the enterprise. In particular, they emphasise the importance of *measuring* employee satisfaction, customer satisfaction and business results in monitoring business performance.

However, while the quality models encouraged many organisations to measure their performance in terms of employee satisfaction, customer satisfaction and financial results, the measures were generally not linked together to identify the relationships between them. What some research suggested, however, was that although some companies using the Baldridge model had better performance than non-users on a number of key internal areas, a company may not demonstrably improve profitability if it lacks a clear front-end market focus (Roth, Chase and Voss 1997). Thus the importance of business results in such models should be emphasised. This reinforces a view that simply measuring individual elements from an *internal* perspective, which tends to be the focus of the earlier quality models, may not in itself improve profitability. The *relationship* between the elements in these quality models needs, in our view, to be explored more explicitly.

The work of Kaplan and Norton (1992, 1993) on the *balanced scorecard* is an example of another model which emphasises the importance of measuring and managing employees, customers and shareholders in an enterprise-wide manner. They proposed that organisations needed to measure their performance, not just in terms of their financial measures (including shareholder value), but also in terms of innovation, employee measures (e.g. retention, satisfaction and turnover), and customer measures (e.g. retention, satisfaction and profitability). However, while three out of their four key areas for measurement match those in the service-profit chain, once again they are not fully integrated in a way that shows the *relationships* between them. (There is little treatment in their published work on this aspect except for a brief reference to one company, Echo Engineering (Kaplan and Norton 1996)). It does, however, emphasise the importance of measuring different elements within the organisation. Loveman and Heskett (1999) acknowledge the contribution of the balanced scorecard in validating their emerging hypotheses on the service-profit chain.

Some other researchers are undertaking research related to the service-profit chain concept. For example, Bycroft and Voegele (1994) looked at the *service value chain.* This recognised that the chain extends from within an organisation to the external (customer) environment and the value added benefits perceived by the customer. The final link in the chain is revenue, profit and growth for private sector companies and the achievement of programme and community objectives for public sector organisations. Bycroft reports that empirical evidence exists of a positive relationship between employee job satisfaction and customer satisfaction (Bycroft 1996a) and job satisfaction and performance (Bycroft 1996b).

Roth et al. (1997) attempted to apply the full service-profit chain model to a set of company data. They found that, in all but two of the individual linkages, the correlations were exceptionally strong. Their findings also suggested that profits may not be put back into the people support functions.

A further piece of empirical research was undertaken by Barber, Hayday and Bevan (1999). They developed a model that contains many key elements of the service-profit chain. They established strong links between employees, customers and business performance. The prime objective of the study was to identify the relevant employee attitudes that underpin behaviours associated with business performance. They argue that simply knowing customers and staff are satisfied stops short of telling a richer story and that "customer satisfaction *per se* does not necessarily result in increased sales or a guarantee of loyalty". They found that *employee commitment* was a key mediating link which had three routes into increased sales performance; directly, via customer service satisfaction and through a reduction in staff absence as shown in their case study attitude chain. Another key link identified in this research was between employee satisfaction and *leadership*. By successfully exploring the linkages, the research showed that, for the retail chain of stores studied, a one point increase in employee commitment could lead to an identifiable and significant monthly increase in sales per store.

The empirical research carried out by Loveman (1998) also finds support for the hypotheses that comprise the service profit chain. He reports *correlations* between many of the elements but stresses that more work is needed in some areas e.g. to better model and measure employee loyalty. He also stresses that his work still does not make claims of *causality*. This point can be levelled at much of the empirical work that has been carried out on the service-profit chain.

However, possibly the most interesting case study work is that undertaken by Rucci, Kirn and Quinn (1998) on Sears Roebuck & Company, a large US department store chain. The Sears management used a modification of the service-profit chain which they termed the *employee-customer-profit chain* to drive through a change in the logic and culture of the organisation. They recognised the drawbacks of using regression analysis which measures correlations without establishing causality. To address this issue they went to Claes Fornell International Group (CFI Group), a leading firm of consultants and econometricians, who have been identified as the prime service vendor for this project (Sherman 1997). CFI Group used causal modelling techniques to establish inferences, with reasonable predictability, of causality. They tested several measures from each of the three key elements of the chain and identified the existence of some significant *causal* relationships which they then used to improve the management of the business. Using these insights enabled Sears to experience both an increase in revenue growth and an identifiable increase in profitability and shareholder value.

From the above review of the literature, and in particular from the service-profit chain research, it is clear how an increasing interest developed in *linkages, correlations* and possible *causal relationships* between concepts such as leadership, employee satisfaction, employee retention, customer satisfaction, customer loyalty, customer retention, customer profitability and shareholder value. A number of people, including practitioners and consultants, are now working on the integration of these variables through developing what we term (following Merz 1999) an *enterprise performance model*. This model is based on the service-profit chain or linkage model approach, but is distinguished from them by its emphasis on the identification of causality.

What is an enterprise performance model? Merz (1999) has defined an enterprise performance model as an *integrated system of measures* for monitoring and controlling enterprise performance. He proposes five key characteristics of an enterprise performance model; it needs to be *knowledge enhanced, market centred, causally related, focused on change* (predictive and prescriptive), and *potentially "real time" in nature*. It is this more holistic and integrated approach, *with an emphasis on identifying causality*, that makes this approach so appealing. This emphasis on causality and empirical verification can be used to distinguish enterprise performance models from linkage models, which may only measure correlations. With these developments in mind, we were interested in learning of companies' adoption of such approaches.

Adoption of Key Service-Profit Chain Measures and Enterprise Performance Model Approaches

Given the general interest in business performance improvement and the widely exposed academic research work on the service-profit chain model by Heskett and his colleagues at Harvard, we wanted to understand the extent to which companies have recognised the importance of such frameworks and have started to use them. More specifically, we wished to identify examples of companies adopting linkage models and the extent to which UK companies were utilising key measures within them. If companies were both measuring these key variables in the service-profit chain conceptualisation *and* monitoring the relationships between them, they would be in a more favourable position to adopt linkage models in the future.

We therefore undertook two phases of empirical enquiry. Phase 1 sought to identify the extent to which companies were using certain key measures which formed part of the service-profit chain. Phase 2 sought to determine the adoption of linkage models by companies utilising all (or most) of the elements of the service-profit chain; and to identify specific companies which might assist in this project by providing case studies. We were also interested to learn if many companies had adopted more sophisticated enterprise performance models.

The primary focus of our research was large companies in the UK. However, in Phase 2, as explained below, we extended our search for companies which had adopted such models to a number of other countries.

Phase 1: Determining the Extent to which Companies were Using Particular Measures Related to the Service-Profit Chain

To identify the extent to which companies were focusing on relationship value management through the adoption of a service-profit chain approach, we needed to know the extent to which they *measured* a number of specific elements. We focused on several key measures that would, in aggregate, provide us with a view regarding the extent to which a given company was highly advanced, or not, in this area. The measures we selected, based on our review of the literature, included: employee satisfaction, employee retention, customer satisfaction, customer retention and individual customer profitability. We also explored the extent to which they attempted to monitor the relationship between employee and customer related measures. From our pilot study, described below, we learnt that managers did not know about their company's measurement of shareholder value, so we did not attempt to use this measure.

We undertook a study of directors and senior managers in large UK organisations to provide an overview of how UK managers attempt to measure key aspects within the service-profit chain. As service-profit chain models are, by their nature, cross-functional, we were interested in determining the views of directors and senior managers who had a broad corporate-wide view of their businesses. In particular, we needed views regarding the employee-based measures within the service-profit chain. For this study we therefore used a sample of directors and senior managers from the human resources, corporate affairs and communications areas within their organisations.

An initial questionnaire dealing with a range of issues relating to business performance was designed and piloted with two groups: 30 mid-career managers and 23 senior executives. The questionnaire was revised as a result of the pilots, combined with some other questions relating to organisational and personal data and mailed to a sample of directors and senior managers. The sample was drawn from the invited guests on 'The Human Resources Forum' and 'The Communications Directors Forum' events. These annual events attract directors and very senior managers from the largest UK organisations and are very representative of the top 500 UK organisations.

A total of 225 useable responses were received from the mailed survey. This represented a response rate of 45%. This high response rate for a mail questionnaire is possibly explained by the fact that the respondents had been invited to these prestigious three day events and because they had a strong interest in the topic of the research. We found no obvious bias between respondents and non-respondents or the groups of senior managers .

The aim of this exploratory research was to find out the extent to which organisations were using the specific measures outlined above and whether they had made progress with monitoring relationships between employee and customer measures. Our findings were that whilst most organisations measured the *individual* factors we surveyed, as follows: employee satisfaction (64%), employee retention (83%), customer satisfaction (89%), customer retention (67%) and profit per customer (51%); very few (only 16%) claimed to monitor the *relationship* between employee and customer related measures.

Interestingly, few organisations understood which factors are likely to have the greatest impact on long-term performance and even some factors considered as important are not measured. For example, life-time value was only measured by 21% of respondents, even though 75% considered that it may have an important positive impact on long term financial performance. Further, the results suggested that if an organisation *is* measuring the linkage between employee and customer measures, then it is likely that senior management will act upon this information.

Phase 2: Identifying Companies which have Adopted more Sophisticated Enterprise Performance Models Based on the Service-Profit Chain

Given the findings from the service-profit chain research on the impact of employee satisfaction, it is interesting how few of the organisations surveyed measure *all* the important variables. We reviewed the overall responses of the 36 companies (16% of respondents), claiming to monitor the relationship between customer and employee related measures. Our view, based on their responses to other questions, led us to conclude that none of the companies could be described as advanced in terms of adoption of service-profit chain or enterprise performance model approaches. This led us to conclude that none of these companies were suitable for more detailed case study research. This is, perhaps, not so surprising. Few of the companies formally participating as part of the Harvard service-profit chain research had explored *all* the linkages across the model.

This research confirmed that UK companies appear to have been slow to adopt such models. As one purpose of the research was to identify companies for more detailed case study investigation on the adoption of service-profit chain or enterprise performance model approaches, further steps were then taken in an attempt to identify companies for more detailed examination. We outline briefly the steps we undertook, although the outcome, in terms of identification of potential companies, was somewhat disappointing.

Step 1: A total of five focus group discussions were also held with senior managers associated with the Forums described above. However, no suitable companies were identified for further research.

Step 2: We sought to identify examples of companies adopting such approaches from participants at large conferences in a number of countries. This included a total of approximately 630 senior managers in the USA, France, Denmark, Italy, South Africa and the UK. These audiences were asked (after an explanation of the concept in some detail) if their company, or one they knew of, had adopted service-profit chain or advanced enterprise performance model approaches. Whilst a number of possibilities were suggested, subsequent investigations yielded only two companies. One of these was already known to us, Sears Roebuck, the other was Nortel Networks. These two companies ultimately became the case studies reported in this paper.

Step 3: We reviewed the academic literature to identify companies reported to be utilising service-profit chain approaches. Most of these were already the subject of study by the academic researchers mentioned above so it was deemed inappropriate to approach those organisations. Further, most were not comprehensively measuring linkages across *all* aspects across the chain.

Step 4: We conducted interviews with two existing companies who were well-advanced users of service-profit chain models (identified in Step 2 and who we use as case studies below) and with CFI Group, a firm with a specialised practice in linkage modelling. These interviews confirmed that although this area had received considerable interest from managers, only a handful of companies were really advanced in terms of developing integrated enterprise performance models.

Towards Enterprise Performance Models: Two Case Studies

We have described above our somewhat disappointing search for a number of appropriate case study examples. However, whilst only the two cases now described were identified, these two provide especially rich examples of the use of linkage models by organisations operating within two very different industries and sets of business conditions.

The first case study reports on a company in the business-to-consumer sector. Sears, Roebuck and Company is a large US retailer with a single continent focus. Sears is in a mature industry and has had to overcome gigantic losses. This case study is based partly on existing published material (which focuses primarily on the turnaround at Sears between 1992 and 1995), e.g. Rucci et al. (1998), Sherman (1997), Laabs (1999) and partly on interviews and meetings conducted with Sears and with CFI Group. Sears utilise the more developed form of linkage model, the enterprise performance model. The second case study reports on a company in the business-to-business sector. Nortel Networks is a large player in the rapidly growing global telecommunication market. The company has been very successful, but is facing considerable competitive challenges. This case study is based on a series of meetings and interviews with Nortel staff, as well as primary and secondary publications and research material.

Case Study 1: Sears, Roebuck and Company

The turnaround of Sears, Roebuck and Company, in the period 1992 to 1995, has been described in some detail (Rucci et al. 1998). Sears is almost certainly the best and most powerful illustration of an organisation that has implemented a service-profit chain enterprise performance model.

In 1992, Sears, Roebuck and Company reported massive losses of $3.9 billion on sales of $52.3 billion. A new CEO, Arthur Martinez, was appointed in 1992 to head the merchandise group and he undertook a streamlining of the business. He closed 113 stores and terminated the 101 year old Sears catalogue, which was a household institution within the US. He also set about changing the service strategy, focusing on women who were the most important buying decision makers. As a result, in 1993 the company reported a net income of $752 million - a dramatic reversal of fortunes for a mature company such as Sears.

Martinez set up four task forces (customers, employees, financial performance and innovation) to define world-class status in each specific area, identify obstacles and define metrics for measuring progress. The task forces spent months listening to customers and employees, observing best practice in other organisations and establishing measures against objectives. Gradually it became apparent that what was needed was a model to show *direct causation* from employee attitudes, through customer satisfaction to profits. The company needed to know how management action, such as investment in sales force training, would directly translate into improved customer satisfaction, retention and higher revenues. What was needed was an operationalisation of what they termed *the employee-customer-profit chain*. The revised model of this is shown in Figure 5.

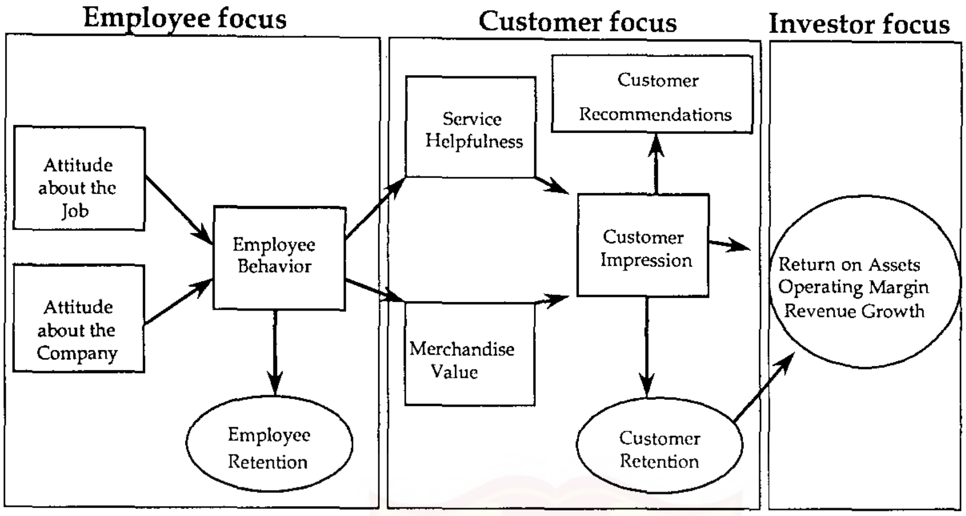

Figure 5: The Revised Employee-Customer- Profit Chain at Sears
Source: based on Sears, Roebuck and Company

Sears defined a set of measures based on its objectives. These were broken down into three objectives that focused on making Sears - 'a compelling place to *work*, to *shop* at and to *invest* in'. This represented a key focus on the three value domains described earlier in this paper. Relationships between changes in key metrics were identified using causal pathway modelling. The econometric modelling of the relationships was undertaken by CFI Group.

Sears enterprise performance model was built using data from over 800 stores. It used 20 customer measures, 25 employee measures and 19 financial performance indicators by store (these included measures of productivity, revenues, margins, payroll costs, number of transactions, etc).

The results of this work were impressive. Direct causal links were identified between employee measures, customer measures and revenues so total profit indicators for the company could be established. Employee attitude towards the job and company were found to be critical to employee loyalty and behaviour towards customers, whilst customer impression directly affected customer retention and the likelihood of recommendations. After further refinement, the model was used as a predictor of revenue growth: a 5 unit increase in employee attitude drives 1.3 unit increase in customer impression, a 0.5 increase in revenue growth and a quantifiable increase in store profitability.

To implement the service profit chain model successfully it was necessary for Sears to change the behaviour of its senior managers and encourage them to take responsibility for the company's culture and understand how this impacted on revenues. In addition, employee rewards needed to be aligned to the model for financial and non-financial measures. Later, a further change was made by streamlining their information systems. Previously there were 18 separate legacy databases; today there is a single, integrated data warehouse.

Following the implementation of the enterprise performance model, employee satisfaction at Sears has risen by 4% and customer satisfaction by almost 4%. More than $200 million additional revenues have been achieved through this value creation process. Figure 6 shows the relative performance improvement on selected measures including profitability, customer satisfaction and associate (their term for employees) attitudes between 1992 and 1998.

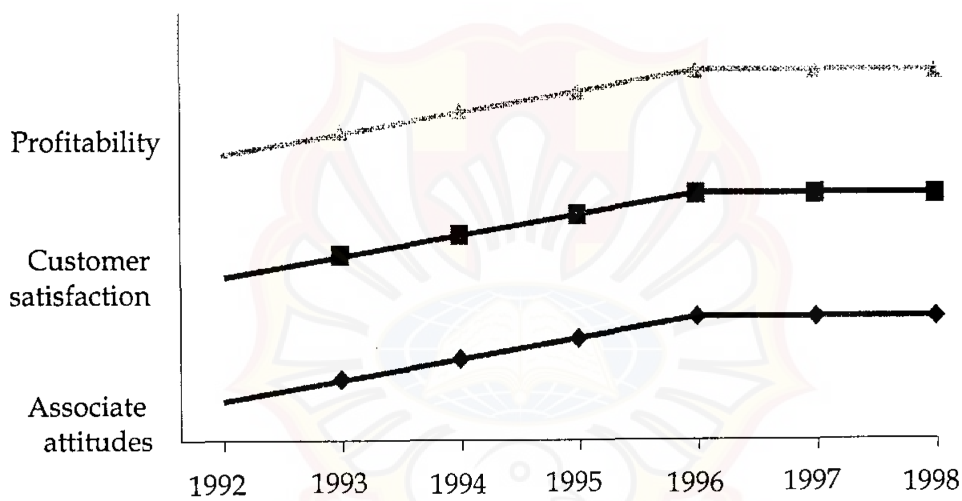

Figure 6: Sears, Roebuck - Selected Performance Measures, 1992-1998
Source: Sears, Roebuck and Company

Confidence in the data was such that Sears computed 30 per cent to 70 per cent of its executive compensation from these measures. Sears delivered earnings of US $ 1.3 billion in 1997. In terms of shareholder value, the total return to investors between September 1992 and April 1997 was 298 per cent. This was a remarkable improvement for a firm in such a mature business. Sears is now using this measurement system to estimate and improve future revenues and profits.

By 1998 a new challenge had emerged, the lack of sales momentum. However, Sears are not complacent. In 1999, President and CEO Arthur

Martinez said "Now, what we need is renewed energy. We need what I'm calling a Second Revolution - a second revolution and our marketing communications to our customer to send a stronger message about who we are and what our value proposition is." Sears are in a very difficult and highly competitive sector. To address these challenges Sears responded with a new re-organisation, a major new marketing campaign and other initiatives. These were met with favourable approval by US financial analysts.

Case Study 2: Nortel Networks

Nortel Networks is an example of a company competing highly successfully in the business-to-business market. This Canadian corporation operates in the global telecommunications market employing 80,000 staff with revenues of US $18 billion in 1998. The impressive performance of the company during the 1990s has been achieved in market conditions of intense competition and rapid change. Nortel has been transformed over this period from being primarily a manufacturer of equipment to being mainly a service organisation, offering network solutions. This change in focus required very different skills and resources, putting pressure on the organisation to be extremely flexible whilst continuing to deliver high quality customer service.

Understanding how value is created and delivered across the three major value domains discussed earlier has played a critical role in their success. Nortel have developed their own model of value creation. Their approach has been influenced by work they have done on benchmarking leading organisations such as Xerox and Disney, and from their work on quality. They are winners of a number of quality awards and are advocates of the US Baldridge and the European EFQM awards. They have worked with leading external experts to develop aspects of their sophisticated model including Brad Gale, the CFI Group, Ray Kordupleski, and others.

Gale, well known for his recent work on value (Gale 1994), was an early influence on Nortel. His work on value creation caught the attention of senior management. This led to a recognition that value was created through a linked system of mutual benefit to shareholders, customers and employees.

In order to identify the value creation process Nortel recognised that it needed a sophisticated measurement system. The *Nortel business value cycle*, shown in Figure 7, was developed to link resources, internal and external processes and shareholders. Although the visual depiction of this model is somewhat different to the service-profit chain, it shows many similarities. However, it extends the model to incorporate the *processes* that create value. It also emphasises the important role of leadership.

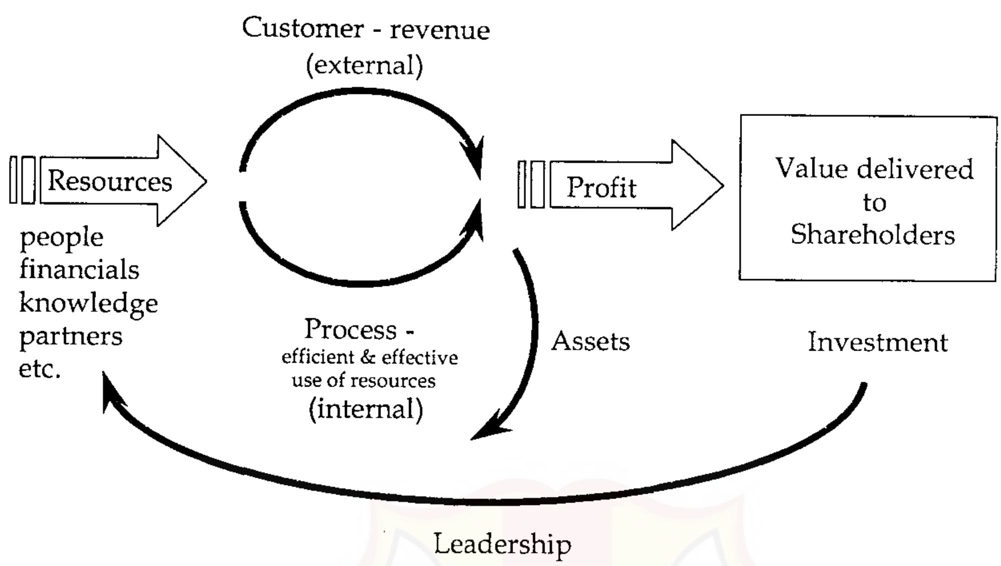

Figure 7: The Nortel Business Value Cycle
Source: Nortel Networks

Logistically, establishing such a measurement system across the global organisation presented a major challenge. However, a significant outcome, made from the effort of establishing it globally, has been the sharing of knowledge across different parts of the business. For example, comparing the satisfaction ratings of a customer in one country with scores in another country has helped integrate management processes across the global operation. Also, initiatives to improve value creation which are tested in one country can, if successful, be adopted in other geographic areas.

Nortel's use of a linkage model has led to them identifying many statistically valid relationships across their version of the service-profit chain. For example, they have identified there are three key drivers of employee satisfaction: leadership, perceived customer focus of the business and the extent that an employee sees obstacles hindering job performance. Leadership accounts for 31% of employee satisfaction and 18% of customer satisfaction; so management recognised that developing the appropriate leadership style and supporting processes was vital. Leadership behaviours that every manager is required to demonstrate are clearly identified and regular appraisals evaluate performance. The organisation emphasises individual empowerment aligned to a carefully formulated and well-communicated business plan.

The value cycle model strongly emphasises the key value of employees to the corporation. Critical to employee motivation are appropriate rewards that are linked to market factors. Nortel has recently redesigned its recognition and rewards system, linking it closely to business results, customer loyalty and employee satisfaction. Seniority has been dropped as a reward criteria. Employees are grouped into one of two teams. The first is a strategic development team that is rewarded on product 'time to market' and market success. The second is a customer facing team that is rewarded by market share and 'share of customer wallet'. Rewards are therefore closely aligned to the value cycle model, so individual employees can understand their contribution to creating value for the business.

Nortel found that employee satisfaction accounts for 52% of customer satisfaction. So, ensuring effective internal processes is critical for succeeding within their customer markets. Nortel has begun a process of refining its employee satisfaction measures. For example, 'high flying' employees are segmented and their impact on customer satisfaction is monitored and compared with other employee segments.

Comparisons are also made between the impact of very satisfied versus merely satisfied employees, on the customer value creation process. Different employee jobs, such as customer interface workers and account managers are compared to identify those that impact most strongly on customer satisfaction. Also, the data is being refined to predict future events, apart from business performance, for example changes in customer behaviour.

More recently, Nortel has focused on understanding the relationship between customer satisfaction and shareholder value. Their analysis suggests that customer satisfaction is positively correlated with revenues and to the share price. Figure 8 shows the relationship between share price and customer satisfaction between 1993 and 1996. Share price continued to increase in 1997. An apparent later dip in share price at the beginning of 1998 was due to a board decision to split the shares and re-issue them on a 2 to 1 basis.

There have been many advantages gained for Nortel Networks from understanding and managing the linkages between employees, customers and shareholders through the application of a formal linkage model. Although the work we have seen does not measure causality, the correlations appear highly significant. Events can be anticipated more effectively so that the organisation can chart a smoother course – vital in the fast changing telecommunications environment. Employees are clearly focused on the most important issues that need to be tackled in order to deliver value to customers. Customers are benefiting from the clear focus that Nortel has in delivering value, whilst shareholders are gaining from the success of the Corporation as revenues and profits increase.

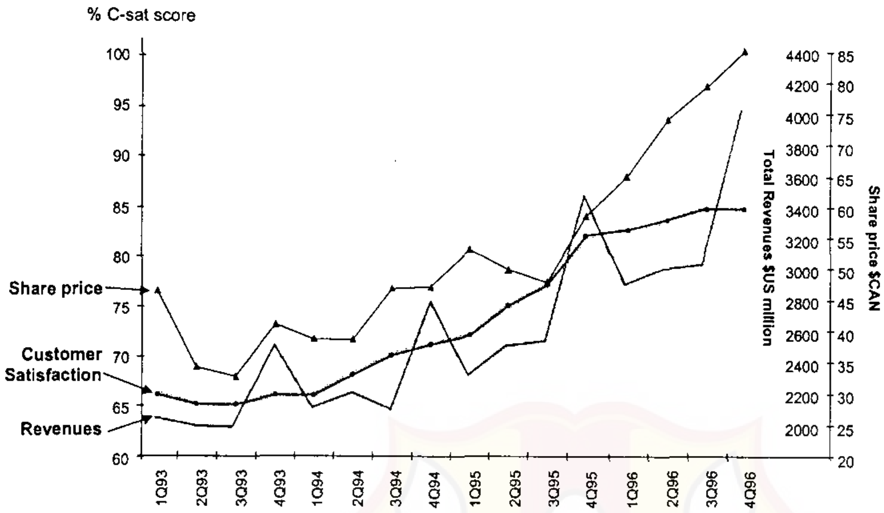

Figure 8: Nortel Networks-Selected Performance Measures, 1992-1996
Source: Nortel Networks

Discussion

This paper has reviewed the literature on *relationship value management,* the links between *customer value, employee value* and *shareholder value,* the *service-profit chain* and *other related models.* The paper then explored the extent of companies' adoption of linkage models and found that few companies to date appear to have adopted such an approach. Two case studies were used to illustrate the benefits of the adoption of a linkage model. This final section of the paper first addresses why more companies would benefit from adopting such models. It then discusses some of the issues relating to their implementation. Finally, it makes some comments regarding future research.

Given the benefits derived by the companies in the case studies used by the 'Harvard' service-profit chain stream of research and companies such as Sears Roebuck and Company and Nortel Networks, it may seem surprising that more organisations have not adopted linkage or more sophisticated enterprise performance models. We consider there are strong arguments why more organisations should consider the adoption of these models. In particular, companies would benefit from: better management of stakeholders; increased understanding of the linkages between employee, customer and shareholder value; improved metrics that will help determine the impact on profitability of changes in employee or customer satisfaction; and a robust means of improving business performance.

Whilst companies often recognise the importance of managing their stakeholders, few actively develop a formal value process that addresses the three key value domains - employees, customers and shareholders - in an integrated manner. This is in spite of companies' concerns regarding the need to improve performance and to develop metrics to measure it. Our research suggests that few companies have reached a stage where their human resource and marketing strategies are subject to rigorous measurement. Further, very few companies appear to have developed metrics which help them understand the *linkages* between employee value, customer value and shareholder value and how these value domains contribute to corporate success. Adopting a linkage or enterprise performance model will make make new and improved metrics available to measure performance improvement *across the business*.

What these models have in common is the requirement to measure performance from a number of different perspectives and integrate these measures. While metrics for measuring shareholder value have received much attention (Cornelius and Davies 1997), marketing as a discipline has generally suffered from a lack of focus in identifying the most meaningful marketing metrics (Shaw and Mazur 1997). Historically, it has been difficult for many marketing managers to justify their actions and to show how marketing and customer-focused activities have contributed to the bottom line. Many organisations, while implementing marketing activities such as customer service, customer relationship management programmes and key account management systems, have failed to convince their boards that these activities have made a major impact on profitability and ultimately shareholder value.

We believe the same to be true for human resource managers. Despite considerable effort by organisations over the last fifteen years in a number of areas, including recruitment, selection, development and empowerment, metrics are frequently not in place to enable them to measure the direct impact of such programmes on productivity, profitability, improved customer focus and organisational flexibility. It can be argued that the problems have been exacerbated by the failure of organisations to realise the need to integrate marketing and human resource activities despite recognition and evidence that these two areas are inextricably linked (Grönroos 1983, 1990).

We consider that one of the best ways in which the drive for better metrics (for both marketing and human resource management) coupled with the need to understand the relationships between employee, customer and shareholder value, can best be realised, is through the adoption of a comprehensive enterprise performance model. Such a model enables the three elements of employee value, customer value and shareholder value to be seen in the context of integrated *relationship value management.* From a relationship marketing perspective, implementing enterprise performance measurement frameworks can not only supply the marketing manager with powerful marketing metrics but should also allow the *organisation* to make an overall assessment of relationship value. It offers a much improved means of measuring the different components of *relationship value.*

Some forms of organisation have the potential to benefit more from implementing these models than others. If organisations wish to move to more sophisticated linkage measurement, Merz (1999) has argued that certain criteria are favorable for modelling the linkages. He suggests five key elements that will help enterprises determine if such modelling approaches are most appropriate to their organisations. These include: delivery of value is through direct customer contact; there are many operational units or outlets, such as branches; there are distinct, isolated, and identifiable groups of customers for each outlet; there are standardized measurement systems across units or outlets; and, managerial and non-contact employees should be excluded from the analysis. If some of these criteria do not apply, then the organisation may not benefit fully or could encounter difficulties in implementation.

A further implementation issue identified in our research is the imperative of top level commitment. Our research and the feedback from the focus groups revealed that although organisations are aware of the links between employees, customers and business performance, they do not attempt to measure this relationship. Investment of significant time and money is needed to develop these sophisticated measurement systems and statistical models. This requires top level commitment, which is hard to get and this may be the main reason why the organisations' adoption of such models is slow.

Loveman (1998) suggests a further problem in implementation. The service-profit chain model can require substantial customization to meet the measurement and usage demands of any individual organisation. He points out that few organisations collect all of the measures required and it is difficult to find cases in which all measures are available at the same unit of analysis for a common time period thus making implementation a very difficult task. Similarly, Barber et al. (1999) stress that *one size does not fit all* and models will need to be 'tailored, modified and revised in order to fit and meet different organisations' needs and cultures'.

Following the existing work carried out on the service-profit chain, there is increasing interest from academics and practitioners in the continued development and refinement of linkage models and there remains much scope for future research. We draw attention to four areas of worthwhile research.

First, more work needs to be done to extend the data collection and establish causal links in companies where research has already been done and where the variables show strong evidence of correlation. Whilst the service-profit chain has been developed through in-depth case histories and a significant amount of research has been published, it has been insufficiently tested using large sample data (Loveman 1998).

Second, many of the barriers to adoption are due to potential problems relating to data, including: data identification, data collection and ensuring data collected on, say, employee satisfaction and customer satisfaction are based on the same time periods. Work needs to be done in the development of tools and approaches to assist managers obtain better quality data and collect it in a much more cost-effective and time-phased manner.

Third, while the service-profit chain and other linkage models have been developed primarily for service-related industries and organisations, it is arguable that other organisations, both private and public, could benefit from their application. If managers are to adopt such an approach, then more work needs to be done to understand how the models need to be adapted in different environments.

Finally, from a relationship marketing perspective, the use of the model as a more explicit basis for measuring and managing relationship value requires further exploration and empirical research. This would involve developing a much more detailed understanding of the key component elements of customer value, employee value and shareholder value from a relationship perspective.

Acknowledgement:

The authors thank Gary Bosak of Sears Roebuck & Co and Michael Jones of Nortel Networks for their help during the research. The comments of Russ Merz and anonymous reviewers are gratefully acknowledged.

References

Anderson, E. W., Fornell, C. and Lehmann, D. R. (1994), "Customer Satisfaction, Market Share and Profitability: Findings from Sweden", *Journal of Marketing*, **58**(July), pp.53-66.

Anderson, E. W. and Sullivan, M. (1993), 'The Antecedents and Consequences of Customer Satisfaction for Firms," *Marketing Science*, **12**(2), pp. 125-143.

Bannister, R. J. and Jesuthasan, R. (1997), "Is Your Company Ready for

Value-Based Management?", *Journal of Business Strategy*, **18**(2), pp. 12-15.

Barber, L., Hayday, S. and Bevan, S. (1999), "From People to Profits", *Institute for Employment Studies Report No. 355*, Institute for Employment Studies, Brighton, UK.

Bennis, W.G. (1970). 'Beyond Bureaucracy'. In *American Bureaucracy*. (Ed.), Bennis, W.G. (Chicago), Aldine Publishing Company, pp. 3-17.

Bernhardt, K. N., Donthu, N. and Kennett, P. (1994), "The Relationship Among Customer Satisfaction, Employee Satisfaction and Profitability: A Longitudinal Analysis", *Working Paper*, Georgia State University, January.

Blackburn, R. and Rosen, B. (1993), "Total Quality and Human Resources Management: Lessons Learned from Baldridge Award-Winning Companies," *The Academy of Management Executive*, **7** (1), pp. 49-66.

Blau, P. M. (1974), *On the Nature of Organizations*, New York, Wiley, pp. 80-84.

Boulding, W., Staelin, R., Kalra, A. and Zeithaml, V. (1992), "Conceptualizing and Testing a Dynamic Model of Service Quality", *Technical Working Paper No. 92-121*, Marketing Science Institute, August.

Buchanan, R. W. and Gillies, C. S. (1990), "Value Managed Relationships: the Key to Customer Retention and Profitability", *European Management Journal*, **8**(4), pp. 523-526.

Buzzell, R. D. and Gale, B. T. (1987), *The PIMS Principles*, New York, The Free Press.

Bycroft, P. (1996a), "What is the Service Value Chain and How Can It Be Used to Improve Performance?", *Paper Presented at an IIR Conference*, Melbourne, Australia.

Bycroft, P. (1996b), "The Service Value Chain: a Case Study in Systematic Evaluation of Organisational Performance", *Paper Presented at Australasian Evaluation Society Internationational Conference*, New Zealand, October.

Bycroft, P. and Voegele, K. (1994), "Soft Performance Measures: the Service Value Chain and Service Organisations", *Paper Presented at the Australasian Evaluation Society Conference*, Canberra, Australia.

Christopher, M., Payne, A. F. T. and Ballantyne, D. (1991), *Relationship Marketing: Bringing Quality, Customer Service and Marketing Together*, Oxford, Butterworth-Heinemann.

Clark, M. (1997), "Modelling the Impact of Customer-Employee Relationships on Customer Retention Rates in a Major UK Retail Bank", *Management Decision*, **5**(4), pp. 293-301.

Cleland, A. S. and Bruno, A. V. (1996), *The Market Value Process*, San Francisco, Jossey-Bass Publishers.

Cleland, A. S. and Bruno, A. V. (1997), "Building Customer and Shareholder Value", *Strategy and Leadership*, **25**(3), pp. 22-28.

Cornelius, I. and Davies, M. (1997), *Shareholder Value*, London, FT Financial Publishing.

The value concept and relationship marketing

Annika Ravald and Christian Grönroos
Department of Marketing and Economic Geography, Swedish School of Economics and Business Administration, Finland

Aim

The aim of this article is to deepen the understanding of the value concept as well as to enlighten the role of value in a relationship marketing setting. Any value-adding strategy should take the objectives of relationship marketing, e.g. "...establishing, maintaining and enhancing relationships with customers...at a profit, so that the objectives of the parties are met..." (Grönroos, 1994), into account. The value concept and value adding seem to be one of the most recent and most popular trends today. However, the concept of value is multifaceted and complicated and there is an evident risk that the concept is used without any efforts and commitments to understand really what it means to provide value to customers, how added value should be related to customer needs and the achievement of profitability for the parties involved. Adding value can be done in several ways and we want to emphasize that a successful way of providing value might be to reduce the customer-perceived sacrifice by minimizing the relationship costs for the customer.

Background

Marketing is facing a new paradigm, relationship marketing (Grönroos, 1994). The focus is shifting from the activity of attracting customers to activities which concern having customers and taking care of them. The core of relationship marketing is relations, a maintenance of relations between the company and the actors in its micro-environment, i.e. suppliers, market intermediaries, the public and of course customers as the most important actor. The idea is first and foremost to create customer loyalty so that a stable, mutually profitable and long-term relationship is enhanced.

Value is considered to be an important constituent of relationship marketing and the ability of a company to provide superior value to its customers is regarded as one of the most successful competitive strategies for the 1990s. This ability has become a means of differentiation and a key to the riddle of how to find a sustainable competitive advantage (Christopher *et al.*, 1991; Grönroos, 1994; Heskett *et al.*, 1994; McKenna, 1991; Nilson, 1992; Quinn *et al.*, 1990; Treacy and Wiersema, 1993). By adding more value to the core product (the product quality is improved, supporting services are included into the offering, etc.) companies try to improve customer satisfaction so that the bonds are strengthened and customer loyalty thereby achieved.

European Journal of Marketing, Vol. 30 No. 2, 1996, pp. 19-30.

Customer satisfaction is supposed to be one of the most important criteria for customer loyalty (Heskett *et al.*, 1994). A recent study reveals that overall customer satisfaction is a better predictor of intentions to rebuy than overall or inferred service quality (Liljander and Strandvik, 1995a). A satisfied customer is supposed not to defect but to stay loyal to the company for a long period of time and to buy more and more often than other, not so loyal, customers do. But the issue here is what the underlying construct of customer satisfaction is. In traditional quality models (Parasuraman *et al.*, 1988) quality is supposed to precede customer satisfaction. Perceived service quality has been defined by several researchers, but one of the most accepted definitions explains perceived quality as the difference between expectations and actual performance (Grönroos, 1982; Parasuraman *et al.*, 1988). Quality can also be viewed as an overall judgement of the superiority or excellence of a product (Zeithaml, 1988).

Recently some criticism of the traditional and widely accepted quality models has appeared (Anderson *et al.*, 1994; Iacobucci *et al.*, 1994; Liljander and Strandvik, 1994, 1995a). The fact that the effect of the customer's perceived price or costs are not explicitly included in the customers judgement of the quality in these models is a shortcoming that should be taken into account. Iacobucci *et al.* (1994) claim that the traditional quality models need a simple modification to include financial factors as well, then the customer's evaluation of a given offering would be a comparison of what they got for what they paid. This is where value enters the stage. Howard and Sheth (1969) and Kotler and Levy (1969) also stated that satisfaction depends on value. Perceived value is defined as the ratio of perceived benefits relative to perceived sacrifice (Monroe, 1991).

Hence, if customer satisfaction depends on value, then it must depend on the total costs or sacrifice, too. We must keep in mind that buyers in most buying situations use reference prices (Monroe, 1991) and even reference values (Berkowitz *et al.*, 1994) when they evaluate the attractiveness of an offering. Even though the price sensitivity may decrease by time in a supplier relationship, the price as well as the total costs will have an impact on the customer's evaluation of alternative offerings. Monroe (1991) also claims that customers value a reduction in costs more than a responding increase in the benefits. Emanating from the above, new approaches are needed in order to create customer loyalty. Instead of just putting the focus on how to enhance customer satisfaction by improving the perceived quality, the discussion has to be widened so that the customer's need of this quality and his willingness to pay for it are also included.

So, we cannot just consider what we give the customer, rather we must concentrate on the sacrifice the customer has to make. The usual approach of value-adding strategies is that the supplier adds technical product features or supporting services to the core solution so that the total value of the offering is increased (see, for instance, Christopher *et al.*, 1991). However, far too many companies alienate themselves from the customers and the value added has consequently nothing to do with the actual needs of the customers. A constant "adding more value" approach in those terms can be questioned. Introducing "extras" which are not driven by the needs of the customers can never be more than a short-term solution. New customers may be attracted and the market shares increased, but any long-lasting bonds will hardly be tied. There is also an apparent danger that companies may be trapped in a treadmill, where they are forced constantly to develop and introduce new fascinating complementary services in addition to the core products. Acting in this manner the company only exposes itself to additional costs, which have to be covered by charging a higher price. So, from the customer's perspective, nothing actually changes. He gets more but also has to give more – and the perceived value remains about the same.

Neither are the customers given an undebatable reason to rebuy. The objective of becoming differentiated from the competitors by providing more value has then come to nothing and the resources spent in product development will not yield any returns. The ultimate aim of adding more value to the core product, i.e. to enhance customer loyalty, will hardly be reached if the value added is not customer oriented.

However, what must be of prime concern for any buyer is the sacrifice involved in the relationship with a supplier, since most buyers have a financial limit which cannot be exceeded. We also mentioned earlier that buyers tend to be more sensitive to a loss than to a gain (Monroe, 1991) and these facts constitute an opportunity for the company to improve the customer-perceived value and thereby establish and maintain a long-term relationship. If the company can provide value in terms of reducing the customer's perceived sacrifice, so that the relationship costs are minimized and customer performance improved, the chances of becoming successful are evident. But to be able to provide this kind of value the company must understand the elements of customer-perceived value and how the company's activities influence (positively or negatively) customer performance.

What is customer-perceived value?

The value concept exists only to a limited extent in the marketing literature. After having studied the theories of several consumer behaviour researchers, we found that "value" is constantly used in a context meaning values of consumers (Engel and Blackwell, 1982; Engel *et al.*, 1990; Schiffman and Kanuk, 1978; Zaltman and Wallendorf, 1983). Peter and Olson (1993), however, discuss another meaning of value – the value or utility the consumers receive when purchasing a product. In services marketing, the value concept appears quite frequently, but any clear definition cannot be found until we turn to the literature on pricing. Monroe (1991) defines customer-perceived value as the ratio between perceived benefits and perceived sacrifice:

$$\text{Customer-perceived value} \quad \frac{\text{Perceived benefits}}{\text{Perceived sacrifice}}$$

The perceived sacrifice includes all the costs the buyer faces when making a purchase: purchase price, acquisition costs, transportation, installation, order handling, repairs and maintenance, risk of failure or poor performance. The perceived benefits are some combination of physical attributes, service attributes and technical support available in relation to the particular use of the product, as well as the purchase price and other indicators of perceived quality.

Zeithaml (1988) defines customer-perceived value accordingly: "...Perceived value is the consumer's overall assessment of the utility of a product based on a perception of what is received and what is given". This definition is almost identical to the one of Monroe (1991), but Zeithaml also points out that perceived value is subjective and individual, and therefore varies among consumers. In addition, a person might evaluate the same product differently on different occasions. The price may be the most important criterion at the time of purchase; a clear and easily comprehensible manual may be of importance at installation and assembly. Zeithaml does not given a reason as to why consumers may have different perceptions of the value of an offering. Our suggestion is that this phenomenon must be related to the different personal values, needs and preferences as well as the financial resources of consumers, since these factors clearly must influence the perceived value.

To be able to understand customer-perceived value to the full, the buyer's value chain needs to be presented. According to Porter (1985) the buyer's value chain is a starting point for understanding what is valuable to a customer and it can be described as "...a series of actions a buyer [i.e. customer] takes in specific contexts with the aim of producing value for that customer..." (Christopher *et al.*, 1991). It represents the sequence of activities performed by an individual buyer or a household with various members in which the product or service is appropriate. For instance, a bank account may be an input into the customer's value chain as a bill-paying device or as an investment for the future. The manner in which the bank account is actually used is determined by the customer's own priorities and values, and these then affect the aspects which are of value to that customer. So, establishing what value the customer is actually seeking from the firm's offering is a starting point for being able to deliver the correct value-providing benefits. According to Christopher *et al.* (1991) the aim must always be to identify what a customer is trying to do with the firm's offering at a particular time and place. We can then draw conclusions about what is valued and why, which subsequently will help the firm to deliver an offer that conforms with the customer's own value chain.

We would like to suggest that the customer-perceived value of an offering, seen through the eyes of the customer and related to his own value chain, must also be highly situation specific. We are referring to the utility or the outcome of buying a good or a service that *per se* raises buyer performance. Think of a situation where your car breaks down and you end up in the middle of nowhere, miles from your destination. Even a very expensive repair (high sacrifice) that turns out to last no further than the destination (low quality) might still result in a high perceived value. The utility of the repair fits into the customer's value chain which in this case is the need of getting to the destination on time.

Any company attempting to provide competitive value to its customers needs to gain a thorough understanding of the customer's needs and the activities which constitute the customer's value chain. If it does not, the task of providing the right value to the right customers may culminate in a hazardous game, where the chances of winning the battle for customer loyalty are highly restricted. However unique an offering might be, the making of it may turn out to be a waste of money and time if it does not fit beneficially into the activities, sequences and links in the customer value chain.

The offering from a relationship marketing perspective

We suggest that the firm's offering should be seen as a "value carrier" and in order to achieve a sustainable competitive advantage the firm must provide an offering which the customers perceive offers a greater net-value than the offerings of the competitors. An interesting issue from a relationship marketing perspective, however, is how the product or the offering is to be defined. The traditional approaches describing the firm's total offering or augmented product[1] (Grönroos, 1990; Kotler, 1994; Levitt, 1983) as a core product supported by surrounding services or goods consider only one episode regarding the customer. The relational aspect as a constituent of the offering is not taken into account. The value of having a relationship, e.g. the value of commitment from both parties, in our opinion also needs to be taken into account when analysing the offering provided and the manner in which it influences the customer's perception of the value. We suggest that the relationship itself might have a major effect on the total value perceived. In a close relationship the customer probably shifts the focus from evaluating separate offerings to evaluating the relationship as a whole. The core of the business, i.e. what the company is producing, is of course fundamental, but it may not be the ultimate reason for purchasing from a given supplier. The reason for purchasing may be simply because the customer has a relationship with this supplier and even though the offering is not exactly the one sought, the parties involved try to come to an agreement where the objectives of both parties can be met. In this situation the point of the discussion is changed. The issue is not what kind of an offering the company provides – rather it is what kind of relationship the company is capable of maintaining.

So, when examining the customer-perceived value of an episode[2] in a relationship, we should note that it probably cannot be derived just from the core product plus supporting services, rather it must also include the effects of maintaining a relationship. In a customer-supplier relationship we would like to use the term "total episode value", which then could be described as a function of both episode value and relationship value:

$$\text{Total episode value} = \frac{\text{Episode benefits} + \text{relationship benefits}}{\text{Episode sacrifice} + \text{relationship sacrifice}},$$

where there exists a special relationship between the elements in the function. As we can see, a poor episode value can be balanced by a positive perception of the relationship as a whole. If the value of having a relationship with a certain supplier is perceived high by the customer (low relationship costs[3] → low sacrifice; the service personnel knows the customer and his needs and preferences well → familiarity and effectiveness; the firm has so far been successful in performing well → improved credibility, etc.) a not so positive perceived value on an episode basis can be balanced and the total episode value kept on a satisfactory level. Here we face the necessity for the firm of being able to maintain a good relationship with the customers, since this apparently makes the customer more tolerant towards occasional inferior performances. The management of any firm should note that the episode value and the relationship value exist in a mutually dependent relationship. Positive episode value enhances the relationship value and a positive relationship value increases the total episode value. The aspects which enhance and constitute a positive relationship value are discussed in the next section.

The value of a relationship

Theories and empirical findings of relationship value exist to a very limited extent. Some attempts have been made in the area of research in industrial marketing, see for instance Wilson and Jantriania (1993). These researchers have studied how value could be measured in relationship development and they conclude that an assessment of relationship value should begin with the economic value, proceed to strategic value and finally estimate qualitatively the value of behavioural elements. However, the study is limited to measuring the value of having an ongoing relationship in a business-to-business market and the results were hard to adopt to a consumer marketing setting.

If we relate to the components or benefits that enhance customer-perceived value on an episode basis, e.g. superior product quality, brand/image, tailoring, supporting services, etc, our conclusion is that these benefits perhaps are not the most valuable aspects to the customer in a long-term relationship. These value-adding attributes are certainly of major importance for the customer when he chooses between different suppliers and the probability for repurchase is undoubtedly greater if the company succeeds in providing something unique and of value to the customer.

In a long-term relationship with the supplier the benefit concept takes on a deeper meaning. We talk about safety, credibility, security, continuity, etc, that together increase the trust for the supplier and thereby support and encourage customer loyalty. After a few successful transactions (the customer is satisfied) the customer starts to feel safe with the supplier – a trust is developing. The customer knows that this company is able to fulfil his needs and wants and is assured that the company will take care of the commitments it has made. For many companies these fundamental aspects of having a relationship with a customer are not always considered, even though this is something every company should pursue in order to retain the customers. Safety, credibility and security contribute to a reduction of the sacrifice for the customer and this is something we believe that the customer finds essential and very valuable. These aspects are illustrated in Figure 1.

It is of extreme importance that the company realizes the need and significance of continuity in a customer relationship. When considering value as a means of strengthening the bonds to customers the discussion should not be limited to value-adding features in the offering. The customer-perceived value needs to get a deeper understanding, a deeper meaning – a meaning which does not relate only to episodes, but to the expectations of the customer and the responsibility of the company to meet these expectations in a long-term relationship. Then the customer-perceived value can be increased on an episode level as well as on a relationship level.

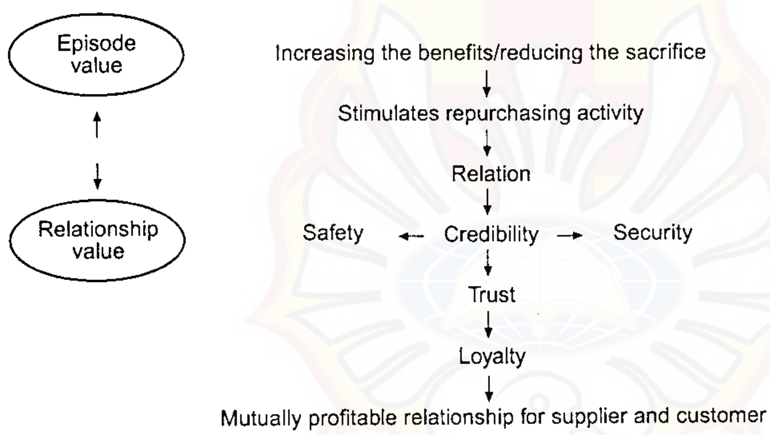

Figure 1. The effect of value-adding strategies in a long-term relationship

Alternatives for creating value

Different authors have different visions of how to increase the value provided to customers. If we use the definition of customer-perceived value by Monroe (1991) the solution is quite simple and easy to comprehend. Either the company tries to provide more benefits or it should reduce the customer-perceived sacrifice. We will discuss these two alternatives below. The emphasis will be on how to increase customer-perceived value by a reduction of sacrifice.

Increasing the benefits

Increasing the benefits for the customer means adding something to the core product that the customer perceives important, beneficial and of unique value. Good core product quality plus supporting services (home delivery, training programmes, warranties, after-purchase service, etc.) increases the benefits for the customer and this affects customer-perceived quality positively. The benefits and the sacrifice can be viewed as two elements that are mutually dependent – increasing the benefits should lead to a reduction in the customer-perceived sacrifice through a minimization of the costs involved in a discrete episode and in the relationship as a whole. The problem, however, is to find an alternative to providing superior value which improves the performance of the company as well as the benefits of the customers in the long run. Our suggestion of a solution to this problem will be presented next.

Reducing the sacrifice

Discussions about value-adding strategies focus on how to add more value to the core product. The expression "add value" gives the impression that something has to be added, an additional product feature, a supporting service, etc. In our view it is also interesting to examine how a company can add value to the offering by reducing the customer-perceived sacrifice. This approach forces the company to look at things from the customer's perspective, which is a central aspect in relationship marketing. In order to be able to reduce the customer-perceived sacrifice, the company needs a thorough understanding of the customer's value chain. The company has to get close to the customer to be able to understand his needs, preferences and all the activities which constitute his value chain. Such a commitment from a company is a prerequisite for survival in the 1990s.

Reducing the sacrifice or effort the customer has to undertake in order to purchase a product on an episode level involves activities like lowering the actual price, increasing the convenience of the purchase (the company delivers the purchased goods to the customer, the availability is improved through changing the opening hours or introducing "call-back-service"). However, when buying a good or a service, there are several incidents that can increase the total costs for the customer, costs of which the buyer was not aware when making the decision to buy. These incidents involve extra, unexpected and often unnecessary costs to the customer. Grönroos (1992) names these costs indirect and psychological supplier relationship costs. Indirect costs are, for instance, costs arising from delayed delivery, costs for time needed to sort out incorrect invoices, etc. Psychological costs are the cognitive effort, the need to worry about whether a supplier will fulfil his promises, and this of course requires mental capacity which could be used more productively.

We would like to claim that these supplier relationship costs are the sacrifice the company should try to minimize for the customer and thereby increase the perceived value. This can be done by improving all routines that in some way affect the customer. A successful reduction of the supplier relationship costs can have a favourable outcome from a company perspective as well. The solution is to improve the internal and external service quality. Thereby the cost efficiency is also improved and this in its turn leads to better profitability. Accuracy, flexibility, efficiency and a zero-defection strategy in production, delivery and after-delivery routines improve the internal efficiency and productivity and this enhances the overall profitability of the company. A reliable long-term quality in all episodes eliminates unnecessary indirect and psychological supplier relationship costs. This adds value on an episode basis as well as on a total relationship basis. Stability and continuity in every action the supplier takes is essential. Then the customer knows what he is getting and what the costs will be, since he does not have to include the costs of problems before, during or after delivery (e.g. delayed delivery, incorrect or defective delivery, billing problems, concern (cognitive activity), lost working time and so on).

This is well in line with the thoughts of Wikström and Normann (1994), who state that the company's search for efficient value-creating processes primarily occurs in two dimensions, which they call cost efficiency and market efficiency. Cost efficiency means that the company tries to increase its efficiency by exploiting resources at its disposal, while market efficiency means trying to develop just those offerings that inject high value into the customers own value-creating processes (e.g. value chains). These offerings appear in two forms: creating added value by relieving the customer and creating added value by enabling the customer. Our conclusions are also in agreement with the ideas of Porter (1985). He claims that a firm creates value that justifies a premium price (or preference at an equal price) through two mechanisms: by reducing buyer costs or by increasing buyer performance. What is essential in Porter's statement is that he points out the opportunity of commanding a premium price. Our conclusions are also that a premium price level is easier to instigate and maintain if the company can prove that it can reduce the total costs for the customer. And above all, the prerequisites for customer loyalty must be increased if the company is capable of providing this kind of competitive relationship.

We consider that the two dimensions of efficient value-creating processes, cost efficiency and market efficiency (Wikström and Normann, 1994), are of extreme importance. Successful performance requires not only satisfaction of customer needs. Cost efficiency and profitability, which improve the financial success of the company, are the foundations for a strong corporate position on the market (McKenna, 1991).

According to Porter (1985) there are no possibilities of merging a cost leadership with a differentiation strategy – he names this combination "stuck in the middle" and by that makes it clear that companies pursuing such a strategy are doomed to stagnation and recess. We prefer an expression coined by Morrow (1992), "luck in the middle", inferring that paying attention to cost efficiency is just as important when trying to differentiate. We wish to emphasize the fact that an optimal strategy could be a combination of cost leadership and differentiation by providing value targeting on the right customers, that is, customers who the company is able to serve profitably. A cost leadership strategy does not necessarily mean that one has to compete with price only, rather it gives the company an opportunity to add extra value to the offering, still commanding a competitive price – and that might be *the* competitive advantage of the future.

Plans for future research

Further research into this area is of course needed. Our plans are to focus on customer-perceived value in long-term relationships with a supplier on the consumer market. In industrial marketing, relationships between suppliers and customers have been investigated quite thoroughly, thanks to the network perspective, which emphasizes the bonds between actors in the network surrounding a certain actor. Buyer-supplier relationships in the consumer market are rather neglected and they therefore constitute a very interesting area for research.

Our intentions with this article were to present ideas which have stimulated our minds recently and the models and assumptions presented can be seen as groundwork for further research. To get an in-depth understanding of customer-perceived value in a relationship marketing setting one needs to study customers' perceptions of value empirically on an episode level as well as on a relationship level. This means that the factors or determinants which maximize customer-perceived value of each episode and the important determinants when considering the relationship as a whole must be investigated. Other important issues are how the relationship itself influences the perceived value on an episode level, as well as the development of perceptions of value over time in a relationship. As regards studying relationships, a dynamic approach is necessary, in order to provide an understanding of how a relationship evolves over time.

As research objects it would be ideal to find those customers who really engage themselves in the relationship with a given supplier (i.e. the commitment is high). Under those circumstances one can assume that there are reasons other than habit, routine, convenience and the effect of different bonds (economical, social, etc.) for the existence of the relationship. If the reasons for that kind of behaviour can be found, we are on our way to solving the riddle of customer loyalty. We suggest that an understanding of customer-perceived value in relationships is fundamental for a solution to this riddle. Once we have come to grips with this phenomenon, it is possible to develop and implement marketing strategies that are market efficient as well as cost-efficient, which in brief can be seen as the objective of any true relationship marketing strategy.

Notes

1. Levitt (1983) suggested that the offer can be viewed at four levels: core or generic product, expected product, augmented product and potential product. The core or generic product consist of the basic physical product, for instance a video cassette recorder. The expected product is the core product together with minimal purchase conditions, for instance a manual and a one-year warranty when buying electronic equipment. The augmented level is where the company has a chance of differentiating itself from the competitors. The aim is to improve the customer-perceived value by adding services and benefits which are preferred by target customers. At the fourth level stands the potential product, namely all the augmentations and tranformations this product might ultimately undergo in the future. It refers to the product's possible evolution over time as the company searches creatively for new ways to satisfy consumers and distinguish its offer.

Kotler (1994) describes the product as consisting of five different levels which are almost identical to those of Levitt – the only difference is that Kotler distinguishes between the core benefit, e.g. the utility the buyer actually wants (a hole) and the generic product, e.g. the actual physical product (a drill).

Grönroos (1990) sees the augmented service offering as a package of a core service supplemented with supporting and facilitating services and goods. In addition to these elements, the augmented service offering also includes accessibility of the service, customers' interaction with the organization and customer participation in the production process.

2. A relation consists of episodes. An episode can be defined as an event of interaction which has a clear starting point and an ending point and represents a complete exchange. In an episode there can exist several interactions, such as check-in, room and breakfast during a stay at a hotel, where the stay represents the actual episode. For a thorough discussion of these concepts and the nature of customer relationships in general, please see Liljander and Strandvik (1995b).
3. Grönroos (1992) discusses three types of supplier relationship costs: direct, indirect and psychological costs. Direct relationship costs are the costs of maintaining a relationship, e.g. insurance premiums, the charge for having a bank account, subscription fee, etc. Indirect relationship costs represent costs for delayed delivery, incorrect invoices and so on. Psychological relationship costs are the cognitive effort needed to worry about whether the supplier will fulfil his commitments or not, time needed to find solutions to problems arising due to poor performance and so on.

References

Anderson, E.W., Fornell, C. and Lehmann, D.R. (1994), "Customer satisfaction, market share and profitability: findings from Sweden", *Journal of Marketing*, Vol. 58, July, pp. 53-66.

Berkowitz, E.N., Kerin, R.A., Hartley, S.W. and Rudelius, W. (1994), *Marketing*, 4th ed., Irwin, Homewood, IL.

Christopher, M., Payne, A. and Ballantyne, D. (1991), *Relationship Marketing: Bringing Quality, Customer Service and Marketing Together*, Butterworth-Heinemann, Oxford.

Engel, J.F. and Blackwell, R.D. (1982), *Consumer Behavior*, 4th ed., Dryden Press, Chicago, IL.

Engel, J.F., Blackwell, R.D. and Miniard, P. W. (1990), *Consumer Behavior*, 6th ed., Dryden, Chicago, IL.

Grönroos, C. (1982), *Strategic Management and Marketing in the Service Sector*, Research Reports No. 8, Swedish School of Economics and Business Administration, Helsinki.

Grönroos, C. (1990), *Service Management and Marketing – Managing the Moments of Truth in Service Competition*, Lexington Books, Lexington, MA.

Grönroos, C. (1992), "Facing the challenge of service competition: the economies of service", in Kunst, P. and Lemmink, J. (Eds), *Quality Management in Services*, Van Gorcum, Assen/Maastricht, pp. 129-40.

Grönroos, C. (1994), "From marketing mix to relationship marketing. Toward a paradigm shift in marketing", *Management Decision*, Vol. 32 No. 2, pp. 4-32.

Heskett, J.L., Jones, T.O., Loveman, G.W., Sasser, W.E. and Schlesinger, L.A. (1994), "Putting the service-profit chain to work", *Harvard Business Review*, March-April, pp. 164-74.

Howard, J.A. and Sheth, J.N. (1969), *The Theory of Buyer Behavior*, John Wiley and Sons, New York, NY.

Iacobucci, D., Grayson, K.A. and Ostrom, A.L. (1994), "The calculus of service quality and customer satisfaction: theoretical and empirical differentiation and integration" in Swartz, T.A., Bowen, D.E. and Brown, S.T. (1994), *Advances in Services Marketing and Management*, Vol. 3, JAI Press, Greenwich, CT, pp. 1-67.

Kotler, P. (1994), *Marketing Management – Analysis, Planning, Implementation and Control*, 8th ed., Prentice-Hall, Englewood Cliffs, NJ.

Kotler, P. and Levy, S.J. (1969), "Broadening the concept of marketing", *Journal of Marketing*, Vol. 33, February, pp. 10-15.

Levitt, T. (1983), *The Marketing Imagination*, Free Press, New York, NY.

Liljander, V. and Strandvik, T. (1994), "A comparison of episode performance and relationship performance for a discrete service", in Kleinaltenkamp, M. (Ed.), *Dienstleistungsmarketing – Konceptionen und Anwendungen* (preliminary title), Gabler Edition Wissenschaft, Berlin.

Liljander, V. and Strandvik, T. (1995a), "The relation between service quality, satisfaction and intentions", in Kunst, D. and Lemmink, J. (Eds), *Managing Service Quality*, Paul Chapman, Vught, pp. 45-63.

Liljander, V. and Strandvik, T. (1995b), "The nature of customer relationships in services", in Swartz, T.A., Bowen, D.E. and Brown, S.T. (Eds), *Advances in Services Marketing and Management*, Vol. 4, JAI Press, Greenwich, CT, forthcoming.

McKenna, R. (1991), *Relationship Marketing – Successful Strategies for the Age of the Customer*, Addison-Wesley, Reading, MA.

Monroe, K.B. (1991), *Pricing – Making Profitable Decisions*, McGraw-Hill, New York, NY.

Morrow, M. (Ed.) (1992), *Activity-Based Management – New Approaches to Measuring Performance and Managing Costs*, Woodhead-Faulkner, New York, NY.

Nilson, T.H. (1992), *Value-Added Marketing: Marketing for Superior Results*, McGraw-Hill, London.

Parasuraman, A., Zeithaml, V.A. and Berry, L.L. (1988), "SERVQUAL: a multiple item scale for measuring consumers' perceptions of service quality", *Journal of Retailing*, Vol. 64 No.1, pp. 12-40.

Peter, J.P. and Olson, J.C.(1993), *Consumer Behavior and Marketing Strategy*, 3rd ed., Irwin, Homewood, IL.

Porter, M. (1985), *Competitive Advantage – Creating and Sustaining Superior Performance*, Free Press, New York, NY.

Quinn, J.B., Doorley, T.L. and Paquette, P.C. (1990), "Beyond products: services-based strategy", *Harvard Business Review*, March-April, pp. 58-68.

Schiffman, L.G. and Kanuk, L.L. (1978), *Consumer Behavior*, Prentice-Hall, Englewood Cliffs, NJ.

Treacy, M. and Wiersema, F. (1993), "Customer intimacy and other value disciplines", *Harvard Business Review*, January-February, pp. 84-93.

Wikström, S. and Normann, R. (1994), *Knowledge and Value – a New Perspective on Corporate Transformation*, Routledge, London.

Wilson, D.T. and Jantrania, S.A. (1993), "Measuring value in relationship development", paper presented at the 9th IMP Conference in Bath, 23-25 September.

Zaltman, G. and Wallendorf, M. (1983), *Consumer Behavior: Basic Findings and Management Implications*, John Wiley and Sons, New York, NY.

Zeithaml, V.A. (1988), "Consumer perceptions of price, quality and value: a means-end model and synthesis of evidence", *Journal of Marketing*, Vol. 52, July, pp. 2-22.