

## Lecture 4: Service Encounter and Guarantees

### Class Outline:

Attributes of Services:

- Intangibility
- Perishability
- Heterogeneity
- Simultaneity

Service Guarantees

Our goal for first phase of course is to accumulate knowledge and formalize what we have now primarily as intuition about services, their attributes, and on ideas on the design of services to meet customer expectations.

Last time we started to look at issues around market segmentation and how it can be tricky to segment customers for a product or service with a short life and high frequency. Among other attributes, we talked about differentiation and saw that creativity is the only limit on the possibilities for differentiation. In other words, there are no mature businesses, only mature ways of doing business. We also talked about expectations by consumers. What matters is what the customer perceives. Examples: when you go Benihana to get personalized service, or go to Disney for fun and enjoyment. Benihana is a production operation as much as Disney is – both organizations process customers and their needs in a controlled way. Disney is a huge production to channel people, managing supply and demand in a clever way. Customers and their needs are being processed even without them knowing it. In these cases, a gap exists by design between what a customer perceives and what we do. So, how do we shape expectations and design our services to meet these expectations?

Ask yourself “what does the customer want to buy?” and then “how can I deliver it?” In services, people typically buy *solutions* and not items.

Our goal today is to show four dimensions, and then talk about service guarantees.

### Intangibility

Services are intangible since they're at the level of thoughts or actions. It is unfamiliar to us for the purpose of analysis, since we're more used to dealing with material items.

Aspects related to the intangibility of services:

- **Understanding of Psychology:** Companies need to make the customer aware that we're worried about them because otherwise they wouldn't know. This requires us to understand psychology and manage effectively.
- **Importance of Physical Aspects:** Because services tend to be intangible, the physical materials that support the service become important. Think of a bank building, lawyer's office, or brochure about a class. These material items are very important for new customers, but are less important for existing clients.
  - **Example:** This is why package delivery companies have rules for their drivers and offer them incentives. Making deliveries on time is simply a prerequisite for being in business. What matters to the customers is not the billions the company has invested in fixed costs, but rather their interactions with the drivers – are they

clean shaven? Did they bring supplies for next time? Successful firms realized this and focus on the employees who interact with customers.

- **It's very hard to get a patent in a service industry.** When the first airline offered coupons for the next trip, other airlines offered coupons *and* accepted competitor's coupons. When a telephone company introduces a new service or a bank offers a new type of account, competitors copy quickly.
- **It is very difficult to be a leader and maintain the leadership position in a service industry.** If you want to be a leader, you need to have an organization capable of introducing new services quickly.

So, your company's technology needs to be able to adapt and grow in the future. And, the culture of your organization needs to change quickly without resistance. The only organizations that don't have resistance to change are ones that change all the time: management has empowered employees to act, everyone is a contributor, everyone is informed, low-level employees can make decisions. There can be pitfalls of this too. Employees don't want to spend even when they should – they can sometimes economize too much. However, empowerment is the outcome of a long process; you can't just hand over decision-making power tomorrow and expect to have it work.

**PSP** = "People Service Profit". The idea here is that if I take care of the workforce and the organization, they are likely to perform well in their service role, and the company is likely to be profitable as a result of satisfied customers.

- **Companies need to materialize the service** – present certain aspects of services in a way that people can consume it. Otherwise, customers are paying for it without knowing it. There are many things companies do that customer don't notice. Example: You get a tag on your shirt from cleaners saying that this button fell off and that they put it back on for you for free. Or, chocolate on your pillow in a hotel room to show they were there serving you.

On the other hand, you can offer too much service that customers don't need or want. You can't try to do everything to serve everybody – firms that over-commit can end up failing.

#### **Class Discussion of Service Guarantees** – in different industries

- Idea for consultants: if you feel the value we gave you was less than the bill, you only pay for the value you perceived – but you probably won't be high on our priority list next time if you don't pay whole bill. In consulting, may be a moral hazard problem?
- Lawyers: only pay if their client wins, but the lawyer prescreens cases to ensure a minimum likelihood of success
- Guarantees are only a function of risk, which is reflected in price. If there's more risk in software, for example, customer takes a fixed price instead. Service guarantees are a sort of insurance, but customer has to pay.
- Need to have clear way to measure your guarantee, which is hard in some industries. How to measure how many customers we've gained or retained in management consulting?
- Who benefits from offering a service guarantee? The customer, yes, but it is also a mechanism for constant improvement in the company.