Management for Professionals

Tymoteusz Doligalski

Internet-Based Customer Value Management

Developing Customer Relationships Online

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Tymoteusz Doligalski
Warsaw School of Economics
Warsaw
Poland

Translation by Maria Wańkowicz and Weronika Mincer

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Preface

Customers play a particularly important role in the company's operations. They provide companies with cash incomes and other values. The values delivered by customers help companies to deepen their relationships with other market participants, such as shareholders, suppliers, or employees. As a result, customers start to be perceived as a company's asset, the value of which can be measured and maximised. Hence, customer relationship-oriented actions become a condition for the company's development, value increase, and improvement of income level.

Changes in management theory and practice are accompanied by technological and social transformations. Application of modern technologies, including the Internet, gives a new dimension to relationships between customers and companies. In contrast to traditional mass media, the Internet became a space which offers the possibility of multi-sided communication, information search, transaction making, and even value co-creation. Consequently, the role of the Internet in building relationships between the company and customers becomes more and more pronounced, since it helps to acquire tangible benefits, such as decreasing costs or acquiring new customers.

Merging of the two areas customer relationships and the Internet presents an important challenge for companies. Its main purpose is to elaborate stable and profitable customer relationships often on new markets, inaccessible in any other way. Companies willing to engage in such an activity have to display an innovative approach, adjusted to the challenge of building value based on a particularly valuable asset: the customers.

In the monograph entitled *Marketing Theory: Evolution and Evaluation*, Sheth Gardner and Garrett (1988: 5) argue that marketing rests inexorably on two pillars: thorough understanding the consumer needs and behaviour; and critical analysis of opportunities for competitive advantage. The thematic area of this book will be centred mainly on the second pillar. The books seeks to answer the question how customer value to company (customer lifetime value) should be managed on the Internet, and more specifically, how to incorporate the Internet in the process of delivery of proposed value to customer in order to increase their lifetime value and thus increase the value of the company and generate value to the company's shareholders and other stakeholders.

The main goal of this paper is to present the possibilities of Internet-based customer value management and a model describing this process. Problems of current state of knowledge of online customer needs and behaviours, associated with the first pillar, are not the main focus of the paper, for the author's intention is to concentrate on the presentation of the concept in form of a model, and not to describe current tendencies, acquired data or prognoses. This approach stems from the stand taken by Shapiro and Varian in the monograph *Information Rules: A Strategic Guide to the Network Economy*, where the authors stress that they 'seek models, not trends; concepts, not vocabulary; and analyses, not analogies' (Shapiro & Varian 1998).

Compared to numerous publications on the use of the Internet in marketing, this paper attempts rather at describing a managing approach to customer relationships than at presenting a particular tool of e-marketing. Moreover, the deliberations are not limited by branches or sectors—differences in the approach towards customer value management are perceived through the prism of different types of value exchange between the company and customers. The author believes that particular types of value exchange have a greater influence on the differentiation of actions associated with online customer value management than the type of market (B2C/B2B) on which the company operates.

Chapter 1 presents the nature of the customer value management, as well as models and concepts associated with relationship marketing. In Chap. 2, the concept of value to customer and the influence of the Internet on this element were described. Chapter 3 proposes a conceptual model of Internet-based customer value management. Finally, Chap. 4 briefly presents financial aspects of customer value management.

This publication is directed, among others, at:

- Persons responsible for customer relationship development
- Managers of all levels of company management, especially from marketing departments
- Students of widely perceived marketing, management and strategy
- PhD students and academic staff

The author will be grateful for any comments, remarks and polemics regarding the publication.

Warsaw, Poland Tymoteusz Doligalski

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Characteristics of the Concept of Customer Value Management

1

1.1 Introduction

The following chapter aims at characterising the concept of customer value management and presenting chosen models and concepts which help to better understand this approach. The focus will be on characteristics of customer value management, such as perceiving customer relationship as a value exchange, customer orientation, customer lifetime value measurement and customer knowledge management, portfolio approach towards customer relationship, focus on customer-oriented processes, connection of customer relationship-associated actions with company's value, and acknowledging of the customer role in the company's business model. In the following considerations it will be stressed how the Internet influences particular dimensions of customer value management within traditional companies and what form it takes within online companies. Afterwards, a comparison between customer value management and mass marketing, and between customer value management in traditional service companies and online companies will be presented.

The focus of the second part of the chapter will be on models and concepts which on the one hand explain the complexity of relationship marketing and on the other served as a source of inspiration for the conceptual model of Internet-based customer value management presented in a subsequent chapter.

1.2 Characteristics of Customer Value Management

V. Kumar identifies customer management with measurement and maximisation of the customer lifetime value (Kumar, 2008). Blattberg, Getz, and Thomas (2001: 3) provide an extensive definition of customer equity management, perceived by the authors as a 'dynamic, integrating marketing system that uses financial valuation techniques and data about customers to optimise the acquisition of, retention of, and

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selling of additional products to a firm's customers, and that maximises the value to the company of the customer relationship through its lifecycle'.

For the needs of this paper, customer value management will be understood as a managerial approach, in which customers are perceived as the company's asset, the value of which may be measured and increased through organisation of the processes around customer relationships. The features of customer value management are as follows:

- Perception of customer relationships as value exchange,
- Customer orientation,
- Measurement of customer lifetime value and customer knowledge management
- Portfolio approach towards customer relationships,
- Focalisation on customer-related processes,
- Connection of customer relationship-oriented actions with the company's value,
- Perception of the role of customers in the company's business model.

It is worth noticing that probably the most important feature of customer value management—actions aimed at increasing customer lifetime value—was not mentioned, for it comes as a result of customer orientation, focalisation on customer-related processes, and the portfolio approach.

The attempt at characterising customer value management presented in the following part of this chapter synthesises approaches presented by various researchers, who frequently apply different concepts to describe the same phenomena. Consequently, seven features of such concepts were discerned. It should be emphasized that the outcomes are subject to many limitations resulting from the subjectivity of the author's perception. In other words, it is possible to characterise customer value management in a different way, which may lead to other conclusions.

1.2.1 Perception of Customer Relationships as Value Exchange

The substantial element of customer value management, which appears also in traditional approach to marketing, is the value exchange (exchange of values) between companies and customers. In the exchange process, the companies provide customers with a set (proposition, stream, bundle) of benefits (constituent values),[1] receiving in exchange customer-generated values. In order to fulfil the needs of

[1] In marketing literature there is an alternative approach which relates to the concept called *service dominant logic*. According to it, companies do not create "value to customer", but only "value proposition", which can be accepted or rejected by customers. The value is then created by customers themselves during the consumption act.

customers, companies supply them with value, by means of *marketing instruments* (product, price,[2] promotion, distribution) enhanced with the company's brand (reputation, image, credibility, trustworthiness, etc.). *Value to customer* may be perceived as a sum of benefits (constituent values of which the value proposition is comprised) reduced by the price and non-financial customer costs. Value to customer seems a more accurate concept than marketing instruments, for it represent the outcomes of actions carried out by the company from the customer's perspective.

From the company's point of view, value exchange should provide the company with diverse streams of *values from customers*, since they are indispensable to the company's proper functioning. Incomes translate into company's liquidity and profitability, and therefore make it possible to deliver value to other stakeholders. An important category of customer-generated values consists of recommendations given to a third party. On the Internet, a major role is equally played by benefits created by customers for other customers, such as content published on websites. At each stage of company development, different benefits may play the crucial role. E.g. in early phase of product development, the most important element are customer-provided information and later on recommendations and incomes.

1.2.2 Customer Orientation

For better understanding of customer value management, the concept of market orientation and customer orientation should be introduced. J. Naver and S. Slater described *market orientation* (or rather marketing orientation) as one 'that most effectively and efficiently creates the necessary behaviours for the creation of superior value for buyers and, thus, continuous superior performance for the business' (Narver & Slater, 1990). In one of earlier elaborated definitions, Jaworski and Kohli (1993) perceive market orientation through the prism of three sets of activities: 'organisation-wide generation of market intelligence pertaining to current and future customer needs, dissemination of the intelligence across departments, and organization-wide responsiveness to it'. According to the research conducted by Kumar et al., market orientation perceived in such a way leads to the situation where profits increase much more than sales, which results from higher retention of satisfied customers (Kumar, Jones, Venkatesan, & Leone, 2011). Benefits associated with market orientation may be obtained in long term or in short term. The most important benefits are acquired by companies that are the first to employ market orientation. Such companies are able to gain competitive advantage, which is hard to gain by the companies that decide to employ such a *modus operandi* later, for it is likely to become solely a cost of competing (i.e. an action that reduces the risk of bankruptcy). The research has also proved that market

[2] The price represents costs of access to given values, but it is also frequently perceived as a value driver.

turbulence has a positive impact on market orientation benefits and technological turbulence has a diminishing effect (Kumar et al., 2011).

A notion related to market orientation is *customer orientation*, which was described by Brilman (2003: 88) as the conviction that customer's needs and satisfaction are of the greatest importance to the company, and therefore all the company's assets and processes should be subject to the creation of value to customer. K. Mazurek-Łopacińska states that customer orientation relies among others on: listening to customers and incorporating customer-delivered information; providing customers with desired value; building relationships with customers (especially the key customers); involving employees in the creation of increasing value to customers; measuring the level of provided services and customer satisfaction (Mazurek-Łopacińska, 2002: 18).

In the context of online companies, it seems of importance to present the typology introduced by Schindehutte, Morris, and Kocak (2008), which includes technology orientation and entrepreneurial orientation. Within the scope of technology orientation, 'technology and innovation are prioritised over the customer' and the company focuses on disruptive technologies, in hope for creating and dominating new markets. Nevertheless, such an approach may produce a situation when the company 'is too far ahead of the customer or is addressing a problem that does not translate into a substantive customer need'. Entrepreneurial orientation consists of three dimensions: innovativeness, risk taking, and proactiveness.

1.2.3 Measurement of Customer Lifetime Value and Customer Knowledge Management

Another dimension of customer value management is the measurement of customer lifetime value and management of customer knowledge. These actions are of particular importance, since they serve as the basis for various managerial decisions, such as dividing customers into segments to which different value proposition will be delivered. The most commonly mentioned element is *measurement of customer lifetime value* (monetary value of the future benefits for the company acquired through customer relationships, reduced by customer-generated costs), customer profitability (monetary value of the benefits acquired by the company through customer relationships, reduced by customer costs in a given period), satisfaction measurement, and loyalty measurement. The main feature of customer value management is a greater focus on the measurement of effectiveness of customer-related proceedings than on the proceedings associated with other marketing resources, such as brand, product, or distribution channel.

Apart from financial data, information on the structure of the customer portfolio and the number of included customers are of equal importance. These dimensions refer to the number of customers with which the company maintained or is currently maintaining relationships and to the division of past, present and potential customers within customer portfolio. Moreover, the structure of customer portfolio provides information on other characteristics of the company's customers, including demographic, psychographic, and behavioural data. On the Internet, the information on the level of customer participation in the relationship with the company gain a particular importance. The customers may play the role of passive buyers, company advocates, and co-creators of value designed to fulfil their own needs or the needs of other customers.

Proper customer value management resides in the knowledge of widely perceived customer reactions to the value acquired from the company. Such reactions may contribute to the appearance of satisfaction, loyalty, trust and involvement in relationships with the company. It is also particularly important to include information on the course of customer relationships (continuity and regularity of product purchase or service use). Another important dimension of customer knowledge is understanding customer risks and company risks associated with them (delay or lack of financial incomes, risk of increased costs, risk of information disclosure, etc.).

The Internet has an important impact on customer knowledge acquisition. The use of web analytics in the form of web traffic statistics helps to acquire accurate information on customers' behaviour on a particular website. Such data may be obtained on the spot or with a minor delay. Based on such information the company may identify customer behaviours on a particular website, which is particularly important for optimisation of actions aimed at customer acquisition. Optimisation of such proceedings may take form of budget allocation to the customer acquisition methods that display the highest efficiency in short- or long-term. Optimisation may be focused on the tools of promotion (display advertisement, e-mailing, web positioning, sponsored links), on their shape (content, design, suggested actions), target group, context (e.g. phases entered in search engines), time (working days, holidays), etc.

On the other hand, the Internet-based development of relationships is frequently associated with a lack of direct contact with customers, which commonly become the source of knowledge about customers' needs or problems associated with a given product or service, and which may serve as a basis for innovating value to customer.

A certain solution may be provided by including social media in the dialogue with the customer. Social media may be used to enter into a direct contact with customers, by listening to their suggestions, answering their charges, and solving their problems. Some researches show that social media may be also employed to maintain close relationships with customers as well as to shape their behaviours, especially in the scope of loyalty (*Small* eMarketer, 2010a, 2010b).

Customer knowledge may not be perceived as static. The information on customers acquired by the company results from the implementation of a marketing information system. S. Sobolewska (2010) describes *customer knowledge management* as a complex approach towards the problem of gathering, creation and application of knowledge, which aims at gaining competitive advantage through value to customer. Sobolewska discerns the following stages of the model of customer knowledge management: planning of knowledge-associated resources, development of customer knowledge, knowledge codification, its diffusion and knowledge application.

1.2.4 Portfolio Approach Towards Customer Relationships

The portfolio approach is another element of customer value management. Portfolio methods are employed in the process of making decisions on the company's assets and were developed in the 1950s by H.M. Markowitz. They rely on conscious development of the asset structure by careful choice of elements and sometimes by further creation of assets themselves. Application of the portfolio approach seems advisable, since different customers provide the company with different values (e.g. incomes, information, recommendations, economies of scale and scope). Therefore, the *selection of customers* who will generate a stream of values desired by the company seems of particular importance. The stream of customer-delivered values desired by the company changes with the company's development, which entails the need of to modify the customer portfolio.

Another important component of the portfolio approach is *customer segmentation*, i.e. division of customers into groups, according to their characteristics and reactions to the company's actions. Customer portfolio segmentation serves as a basis for differentiation of actions aimed at different groups of customers, which on the one hand may contribute to more comprehensive satisfaction of their needs, and on the other—to increasing their value to company.

The use of the Internet for developing customer relationships highlights the differences between customers, for they gain possibility not only to buy products, but to publish online product reviews, promote a company or fight against it. Such behaviours appear also within the scope of traditional market, nevertheless on the Internet they are more pronounced, for they have a wider range.

Frequently, online companies act as intermediaries between two complementary groups of customers (e.g. online auctions, advertising services). In such a situation venture success depends on maintaining a correct proportion between the two groups of customers, which results in a necessity to employ the portfolio approach, consisting in well-considered customer selection which will have an important impact on further development of the relationship. The mechanisms by means of which the company may influence customers from different groups include value to customer and its subcomponent of price.

Customer portfolio segmentation is a particularly important constituent of customer value management, for it serves as a basis for differentiation of actions regarding various groups of customers and therefore enables organisation of managerial processes around particular customer segments (or even single customers). Focalisation of actions on particular customer segments may result in switching from the measurement of product, distribution channel and brand effectiveness to analysis of customer profitability and value.

1.2.5 Focalisation on Customer-Related Processes

Another important feature of customer value management is the focalisation on customer-related processes and not on the instruments that create the marketing mix, which in terms of traditional marketing are used to influence the market. Marketing composition has transformed with the number of instruments it incorporated. In the most popular version, it relies on four instruments (4P—product, price, place, promotion), which in order to reflect a specific character of the service market were extended to seven elements (people, processes, and physical evidence)(Booms & Bitner, 1981). In traditional concept of customer value management, existing instruments are not ignored, but are not in the centre of attention, since the focus is on customer-related processes. This situation is reflected in the models of customer equity, individualised marketing, and delivering value to customers presented in the further part of the chapter.

The set of instruments associated with 4P loses in applicability in the context of developing customer relationships on the Internet. The reasons for such a situation are numerous. Content (articles, broadcasts, transmissions), as well as many online services (related to communication, information management, etc.) are frequently offered for free. Thus the price, perceived as one of the tools for gaining competitive advantage, becomes then irrelevant. Owing to wide availability of websites, the importance of distribution also decreases. In the areas where distribution (place) plays a particularly important role, it often overlaps with promotion. The company's presence in search systems or presentation of its products on the websites of intermediaries may be perceived both from the perspective of place and promotion. Staying in the convention of traditional marketing instruments (4P), online company competition may often be reduced to two instruments: product and promotion (communication).

The role of traditional marketing instruments has also lost in importance in the case of e-commerce. In terms of place—perceived as delivering products to customers—online stores offer similar services, as they co-operate with the same delivery companies. Moreover, they also communicate in a similar manner, to a great extent employing the presence in search results, both in terms of organic results and sponsored links. Competing with price also seems difficult since price differences are not very pronounced. Nevertheless, online sales are associated with an additional dimension, that is—seller's reputation, which is frequently built by various intermediaries (online auctions, price comparison engines) based on customers' opinions. Due to the fact that many companies offer products at particularly low prices and exhibit a reputation which does not significantly differ from the reputation of other competitors, the use of such instruments does not seem to guarantee competitive advantage.

In view of the above, the importance of competing through customer-related processes seems to gain in importance. Such processes, according to Blattberg, Getz and Thomas, include customer acquisition, add-on selling (selling of additional products within the scope of existing relationships), and building customer