# SERVICE AMERICA!

## DOING BUSINESS IN THE NEW ECONOMY

Karl Albrecht—Ron Zemke

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# PREFACE

We believe a powerful new wave is about to hit the already turbulent business world. It's the wave of *service,* or more specifically a new and intense preoccupation with the quality of service. People are getting more and more critical of the quality of service they experience in their everyday lives, and they want something done about it.

The times have changed and we no longer live in a manufacturing economy. We now live in a very new economy, a *service economy,* where relationships are becoming more important than physical products. Just as America experienced an industrial revolution around the turn of the century, so we are now experiencing a service revolution. What was once Industrial America has become Service America.

Glance around you please, and notice how much of your personal experience is involved with companies and institutions that exist for the purpose of delivering services of various kinds. Restaurants, hotels, airlines, hospitals, banks, public utilities, colleges and universities—all have the problem of gaining and retaining the patronage of their customers.

Many other organizations, such as department stores, mail-order firms, and even sellers of hard goods are finding that the invisible product—the service component—is becoming an important competitive weapon.

The times call for a new focus on service, for a number of reasons which we will explain in this book. This new *service imperative* will mean that the old customer service department will probably fade into obscurity as executives and managers work to transform their entire organizations into customer-driven business entities. The quality of the customer's experience is becoming a hot topic in board rooms and executives suites, not only in the United States but in many other countries as well. We believe this is a world-wide phenomenon.

We have tried to do several things in this book. First, of course, we want to alert forward-thinking business people, especially executives and middle managers, to the potential of this new competitive weapon of service quality. Second, we have tried to isolate some of the key factors that govern service quality, and offer examples of organizations that manage service well and of some that manage it poorly.

More important, we have tried to highlight a critical gap which we feel exists in current management thinking, namely the lack of a consistent model or framework for managing service. As a result of our experiences with many different kinds of organizations and considerable research into the operation of effective service enterprises, we have discovered an approach that we believe can help managers think about their businesses in a new and effective way. This *service management concept* is the principal contribution we hope to make with this book.

Before you read what we have to say about the management of service, it may be fair for us to declare certain points of view, so you will know what biases we bring to this subject. First, as a result of working in and with organizations, we are biased to believe that high-quality service at the front line has to start with a concept of service that exists in the minds of top management. This service concept must find its way into the structure and operation of the organization. There must be a customer-oriented culture in the organization, and it is the leaders of the enterprise who must build and maintain this culture.

We also believe in the value and importance of measuring service. An intimate and objective knowledge of how you are doing—in the customer's eyes—is critical. Market research, the service audit, and a process for measuring service quality and feeding back this information to the frontline people are crucial ingredients in moving an organization to a high level of service orientation.

We believe that *management itself is a service,* and that this point of view will become more and more prevalent as competition gets tougher and service becomes more and more a competitive weapon. Managers need to see their roles in the context of helping service people do their jobs better. The role of management in a service-driven organization is to enhance the culture, set expectations of quality, provide a motivating climate, furnish the necessary resources, help solve problems, remove obstacles, and make sure high-quality job performance pays off.

We believe this new era of service management will call for a return to the most fundamental principles of leadership and in many cases to a rethinking of the organization's basic reasons for being. Those leaders who fail to grasp the real significance of service quality will face tough times. Those who do will see their organizations thrive and prosper.

Karl Albrecht
Ron Zemke

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# The Service Imperative

> McDonald's has more employees than U.S. Steel.
> Golden arches, not blast furnaces,
> symbolize the American economy.
> —*George F. Will*

Ours is a service economy, and it has been one for some time. Trend analyst John Naisbitt marks the beginning of this new period as the year 1956, when, "for the first time in American history, white-collar workers in technical, managerial, and clerical positions outnumbered blue-collar workers. Industrial America was giving way to a new society."

Naisbitt labeled this new era the "information society." Earlier, Harvard sociologist Daniel Bell noted the same events and trends, and pronounced us entered into the "postindustrial society." Call it what you will, the fact remains that we live in an America, perhaps in a world and time, dominated by industries that perform rather than produce.

According to the U.S. Department of Commerce, the forecast for the foreseeable future can be summed up in four words: more of the same. There will be continued fast growth in service industries and service jobs, with data processing and hospitality leading the way. Service is no longer an industrial by-product, a sector that generates no wealth but "simply moves money around," as one economist has scoffed. Service has become a powerful economic engine in its own right—the fast track of the new American economy. *Newsweek* columnist George F. Will summarized the look of this new economy succinctly when he observed that "McDonald's has more employees than U.S. Steel. Golden arches, not blast furnaces, symbolize the American economy." We are only beginning to understand the significance of this change in the way we live and work.

Let's be clear here. We aren't suggesting that U.S. Steel is about to convert its factories into laundries to survive, or that Chrysler Corp. should consider abandoning automobile manufacturing for condominium management. As Wharton School management professor Russell Ackoff has argued, this shift toward a service-centered economy does not mean that fewer goods will be produced and consumed, "any more than the end of the agricultural era meant that fewer agricultural products were produced and consumed. *What it does mean* is that fewer people will be required to produce manufactured goods."[1] To us, that implies the gold and the growth are in services. That's where the jobs are; that's where the energy is; that's where the opportunities will continue to be.

We are persuaded that a real and important shift is under way. The fabric of our economy and the way we do business in this country are changing. This change in thrust, this transformation from a marketplace focused on goods to one focused on services, this phenomenon that Ackoff calls the "second industrial revolution" and Naisbitt refers to as the "beginning of the information society," is real and important. It is our new competitive edge—both domestically and in the world at large. Already 20 percent of the world's need for services is filled by American exports. It is only a beginning.

We contend, however, that this shift from products to services, if it is to be fully leveraged as a driving force, requires a parallel transformation in the way organizations are conceptualized, structured and, most important, managed. We contend that organizations that place a premium on the design, development, and delivery of services are as different from traditional industrial organizations as the factory is from the farm. The distinction applies not only to organizations that market pure service products (the traditional service industries) but also to manufacturers of hard goods and commodities which place a high strategic value on service and treat it as an integral part of the product they deliver. Whether service is valued simply because it is a useful strategy for product differentiation, or because service is an ingrained organizational belief, the result is the same. In those organizations service isn't a function or a department. To them, service *is* product.

## SERVICE IS . . .

What do we mean by service? Several things. Bureaucrats and economists traditionally have talked about the "service sector" and defined it as consisting of "industries whose output is intangible." To the Census Bureau and the Department of Commerce, that definition covers organizations that employ just short of 60 percent of all the people employed in the United States, and applies to four broad segments of the economy:

- Transportation, communications, and utilities.
- Wholesale and retail trade.
- Finance, insurance and real estate.
- Services—the fastest growing part of the "service sector," which includes business services such as accounting, engineering, and legal firms; personal services such as housekeeping, barbering, and recreational services; and most of the nonprofit areas of the economy.

All four of these groups offer service in the classic "Help Me" sense: help me with my taxes, help me get from point A to point B, help me find a house, help me pick out a new pair of shoes. There is nothing intrinsically wrong with this traditional approach to defining who is and who isn't in the service business. It does, however, mask the full impact of service in today's marketplace.

Management expert and social scientist Peter Drucker is even more emphatic that the term *services,* as used to describe the largest portion of our contemporary economy, is a singularly unhelpful description. In a recent column in *The Wall Street Journal,* he surveys the world economy, the slump in commodity prices, and the slow recovery of manufacturing compared to the rapid growth of the service sector and states:

> We may—and soon—have to rethink the way we look at economics and economies, and fairly radically. "Information" is now classed as "services," a 19th-century term for "miscellaneous." Actually it is no more services than electrical power (which is also classed under services). It is the primary material of an information-based economy. And in such an economy the schools are as much primary producers as the farmer—and their productivity perhaps more crucial. The same in the engineering lab, the newspaper and offices in general. (January 9, 1985)

We heartily agree with Drucker's argument that service, as we know it today, is very much a primary product. It is, indeed, this argument that service is not a single-dimensioned "thing" that is at the core of our contention that service is as much a commodity as an automobile and as much in need of management and systematic study.

Harvard Business School professor Theodore Levitt agrees that the service and nonservice distinction becomes less and less meaningful as our understanding of service increases. "There are no such things as service industries. There are only industries whose service components are greater or less than those of other industries. Everybody is in service," he writes. At Citibank, half of the organization's 52,000 employees work in back rooms, never seen or heard by the public. They spend their time writing letters of credit, opening lockboxes, processing transactions, and scrutinizing everything done by the public contact people. Is Citicorp any less a manufacturer than International Business Machines Corp.? And is IBM, half of whose 340,000 employees deal directly with the public, any less a service provider? Service is everybody's business.

## "FIX IT" SERVICE

The second dimension—after "Help Me" service—is service in the "Fix It" sense. It sometimes seems we are a nation of broken toys. The car is in the shop, the phone is out of order, and this computer you sold me isn't working so well either. Service in this sense is underaccounted for in the economy and marketplace, but seldom undervalued in the eye of the contemporary consumer.[2] The quality of a company's "Fix It" service is already a significant factor in its marketplace success. The capacity of an IBM, a General Electric (GE), or a Caterpillar Tractor to deliver high-quality "Fix It" service as a matter of routine—while others offer excuses, complex requirements, or failure—sets each apart in its industry and in the marketplace as a whole. We are not suggesting, of course, that manufactured goods have never before needed fixing. Far from it. But only recently have so many products become too complex for users to repair and maintain on their own. At the same time, consumers have come to expect—to demand really—that a manufacturer's obligation to guarantee the performance of a product should extend further past the point and date of purchase than ever before.

Such changes in consumer expectations can be both a bane and a blessing. It is the growing demand for high caliber "Fix It" service in the personal computer business, falling on the deaf ears of most dealers and manufacturers, for example, that is behind the spate of start-up companies, like Sorbus Service Inc. and Computer Doctor Inc., which specialize in servicing electronic products. The same demand is enticing large-computer manufacturers and the few service-savvy micro producers into the development of aggressive, third-party service subsidiaries.

And what an opportunity it is! Every day a thousand Macintoshes come rolling off the Apple Computer assembly lines in Cupertino, California, while an equal number of IBM-PCs hit the road north from Florida. If we add the 3 to 5 million "orphaned" personal computers and computer peripherals in this country (which were gear-manufactured by companies that no longer exist but owned by users who do), then the need for quality "Fix It" service in the computer area alone is staggering.

According to a study by Arthur Andersen & Co. for the Association of Field Service Managers, the repair of information processing, telecommunications, and other diverse electronic products—dubbed the "electronic products service business" in the study—bills $20 billion annually, and this figure should grow to $46 billion a year by 1990.[3] Yet few manufacturers of high-tech gear are interested in the opportunities presented by this obvious void. This is so despite the fact that a well-run service operation can, by Andersen's estimates, contribute as much as 30 percent to a manufacturer's revenues. Is it any mystery that the few companies which do see the handwriting on the wall—TRW Inc., Control Data, Bell & Howell Co., Western Union Telegraph Co.—are doubling their efforts to establish solid reputations and names for themselves in the service end of the electronic future while others are content only to manufacture?

This naiveté about the value of service among producers of hard goods may be glaringly obvious in the personal-computer world, but it is hardly confined to that world. Automobile manufacturers, big steel companies, machine-tool builders and any number of consumer-product producers have suffered the same malady in the past. The attitude plainly has been, "This would be a great business if it weren't for all the damned customers." Such an attitude almost always proves to be a costly error in judgement, but it's becoming a more deadly mistake every day. Service, it increasingly turns out, can play a significant role in the economic well-being of an organization that produces hard goods. When *your* food processor is distinguishable from the competition's food processor by only a dime's worth of detailing and a dollar on the price tag, your customer service and service reputation become a critical discriminator. The GE commercial that promises, "We don't desert you after we deliver it" plucks a heartstring in a million frustrated consumers. You can count on GE.

An unusually incisive set of studies of consumer complaint behavior was carried out during the Carter Administration for the White House Office of Consumer Affairs by a Washington, D.C., company called Technical Assistance Research Programs, Inc. (TARP). These studies spoke volumes about the positive economics of first-class service.[4] According to their findings, manufacturing organizations that don't just "handle" dissatisfied customers but go out of their way to encourage complaints and remedy them, reap significant rewards.

Among TARP's key findings are the following:

- The average business never hears from 96 percent of its unhappy customers. For every complaint received, the average company in fact has 26 customers with problems, 6 of which are "serious" problems.
- Complainers are more likely than noncomplainers to do business again with the company that upset them, even if the problem isn't satisfactorily resolved.
- Of the customers who register a complaint, between 54 and 70 percent will do business again with the organization if their complaint is resolved. That figure goes up to a staggering 95 percent if the customer feels that the complaint was resolved quickly.
- The average customer who has had a problem with an organization tells 9 or 10 people about it. Thirteen percent of people who have a problem with an organization recount the incident to more than 20 people.
- Customers who have complained to an organization and had their complaints satisfactorily resolved tell an average of five people about the treatment they received.

If automobile industry studies are correct that a brand-loyal customer represents a lifetime average revenue of at least $140,000, then the image of a manufacturer or dealer in a bitter dispute with a customer over an $80 repair bill or a $40 replacement part is plainly ludicrous. Similar logic holds for almost every business sector. In banking, the average customer represents $80 a year in profit. Appliance manufacturers figure brand loyalty is worth $2,800 over a 20-year period. Your local supermarket is counting on you for $4,400 this year and $22,000 for the five years you live in the same neighborhood.

As TARP president John Goodman put it in an address to the Nippon Cultural Broadcasting Company in Tokyo:

> The fundamental conclusion [of our studies] is that a customer is worth more than merely the value of the purchase a complaint concerns. A customer's worth includes the long-term value of both the revenue and profit stream from all his purchases. This becomes particularly important if the customer could potentially purchase a range of different products from the same company.[5]

The Japanese, by the way, are only beginning to see service as important *and* problematic. Decades of concentration on manufacturing quality products and exporting finished goods have left service basically unattended to. The tendency in Japan is, as it has been here, to equate service with servitude and face-to-face attention rather than with customer-centered management.

The pattern of consumer behavior TARP uncovered is as true for industrial sales as for retail sales. There really is no mystery, then, as to why a heads-up company like Procter & Gamble prints an 800 number on all 80 of its products. This year, P & G, the nation's largest producer of consumer products (Ivory soap, Folger's coffee, Crest toothpaste, Pamper's disposable diapers, Tide detergent, and so on), expects to answer more than 750,000 telephone calls and letters from customers. A third of these replies will deal with complaints of all kinds, including those about products, ads, and even the plots of soap operas sponsored by the company. If only half of those complaints are about a product with a 30-cent margin, and only 85 percent are handled to the customer's satisfaction, the benefit to the company in the year, according to a formula developed by TARP, could exceed half a million dollars. Such a sum represents a return on investment (ROI) of almost 20 percent. The "Fix It" dimension of service is most surely an important economic force in its own right.

## VALUE-ADDED SERVICE

The third service dimension shaping the way we do business is the most intangible of all. Value-added service has the feel of simple civility when delivered in a face-to-face context, but it is more than that. When it shows itself in such an ingenious and successful product as the American Express Platinum Card, it looks like perceptive marketing.

Value-added service is more easily understood in experience than in definition; you know it when you see it. Because a cabin attendant pushing the drink wagon on Republic 507 out of Chicago is out of loose change, she gives you back three one-dollar bills from a five for a $2.50 drink. In response to an off-hand comment you made, a calling officer from Wachovia Bank and Trust, who pitched factoring services to you last week, sends you an article on how to use limited trusts to help put your kids through college. A 3M visual-products representative setting up a seminar on how to use overhead projectors in sales presentations stays to help one of your salespeople rehearse for a next-day presentation. All those people are practicing the fine art of value-added service.

Each variation on the same theme is an example from, and an integral part of, the service revolution. The common thread is customer-focused service. None of these examples represents a new definition of what service means. It is rather the value and power they have in the marketplace that is new.

John Naisbitt's "high-tech/high-touch" concept has a lot to do with the development of this need. As new technology is introduced into our society, there is a counterbalancing human response. For example, Naisbitt points out, "The high technology of heart transplants and brain scanners led to a new interest in the family doctor and neighborhood clinics." In that same vein we have noticed that the advent of automated tellers in banking gave rise to a countermand by many for access to a personal banker. The more we are faced with high tech, the more we want high touch. The fewer contacts we have with the *people* of an organization, the more important the *quality* of each contact becomes. All contacts with an organization are a critical part of our perceptions and judgments about that organization. The quality of the *people contacts,* however, are often the firmest and most lasting.

Russell Ackoff sees another dimension to the demand for value-added service: a shifting focus from concern for one's standard of living toward a concern for the quality of life. If some aspects of this phenomenon represent a shift away from materialism and the "I-can-have-it-all" credo, as some claim, other factors that fall under the quality-of-life umbrella certainly signal that with a secure standard of material life, the accessories become more important. A young person's need for a car gives way to a desire for the "right kind" of automobile. Access to discretionary funds sufficient to support frequent air travel gives way to a desire for first-class seating and the best possible amenities. The total experience of obtaining a product or service becomes integrated into a real and palpable quality of the product or service itself.

Warren Blanding, editor and publisher of *Customer Service Newsletter*, suggests that several forces are at work here. Together they create a new understanding of service:

> The trend toward consumerism, the changing competitive climate and the recent recession all have forced companies to reexamine their relationships with customers. As a result, customer service has become a strategic tool. It used to be regarded as an expense. Now it is seen as a positive force for increasing sales—and for reducing the cost of sales.

The constant quest for improvement in the quality of life is not a new phenomenon, only a new mass phenomenon. In the early industrial era of this country, only the wealthy few played tennis, summered in the mountains, or wintered in the Bahamas. Today these are mass cultural experiences. Our parents and grandparents were tickled to have a paid week off, once a year. The paid vacation was a great labor victory. We—or at least some of us—jet to London for a long weekend of shopping and theater in an almost casual manner. As the mass demand for a product or service increases, the ability to deliver it effectively, efficiently, and dependably is taxed. It must be managed. Thus we find ourselves entering the service management era, the age of *systematically* designed, developed, and delivered services.

## SERVICE AS A MANAGED ENDEAVOR

Historically, the terms *service* and *management* haven't rested easily side by side. Service delivery was something most self-respecting business school graduates shunned—with the exception perhaps of rising young bank officers. The concept of management seemed to encourage an orderly image antithetical to service in the traditional "Help Me" sense.

Ronald Kent Shelp, vice president of American International Group (a New York–based multinational insurance company) and chairman of the federal advisory committee on service industries, attributes those perceptions to a confusion of *personal services*—such as those provided by housekeepers, barbers, and plumbers—with the concept of *service as the provision of intangible products in general*. Consequently, service has been misperceived as always involving a one-to-one relationship between provider and receiver, as labor-intensive, and as having productivity characteristics not readily increased by capital and technology.

Characterizing service in today's economy as servitude is as inaccurate as calling Francis C. Ronney, Jr., head of Melville Corp. (the $4 billion-a-year retail chain store conglomerate that started as Thom McAn), a shoe clerk. Today two thirds of the gross national product result from service production; and at the same time, personal service in the traditional sense accounts for less than 1 percent of all service jobs. Here is how Shelp sees it:

> While personal-service jobs were declining, industrialization was calling forth a whole range of new services. Some of these were the result of new found affluence, as more and more people could afford more and better health care, education, amusement, and recreation. Other services were needed to increase the productivity of production—wholesale trade, information processing, financial services, communications. These services and others like them (engineering, consulting, retailing and insurance) became highly productive when modern technology supplied them with computers, satellite and other rapid communications, and systems analysis.
>
> Thus service jobs moved away from the low end of the economic spectrum toward the other extreme. Much of the service-oriented job growth in advanced nations has taken place in professional, managerial, administrative, and problem-solving categories. Increasingly, education became the name-of-the-game in service jobs.[6]

This change in the nature of what a service is, leads to a situation where we see a number of quite different kinds of activities nestled under the umbrella of "service and service-related industries." Shelp sorts these into five types and suggests that each developed in response to a set of stages and parallel economic conditions through which Western society has passed and through which many developing countries are now passing.[7]

**Unskilled personal service.** Housekeeping services for females, military conscription for males, and street vending for both sexes are the primary type of service activity in traditional societies. Historically, these kinds of jobs have provided opportunities for excess population to become socialized into urban life. Though unskilled labor exists today in this country, it is on a very different scale. People plying the trades of housekeeping, street sweeping, janitoring, and the like do exist today, but it is more likely than not that the services they provide are through a corporation like ServiceMaster International and not on a free-lance basis. It is also most likely that these organizations call on technology and mass-production techniques to assist in the delivery of the service