The value concept and relationship marketing

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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.

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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

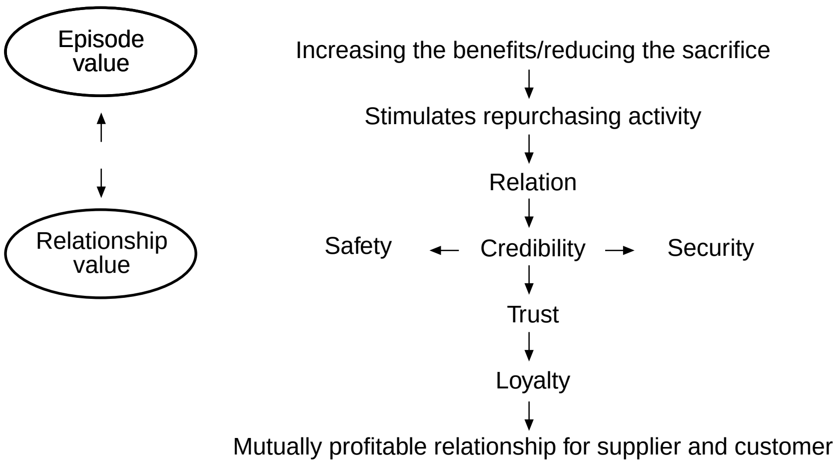

Figure 1.
The effect of value-adding strategies in a long-term relationship

level as well as on a relationship level.

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.

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