Defining Value

The distributor was obviously frustrated. "How," he asked, "can you sell value to somebody who is only interested in price?"

According to the distributor, most of his customers were like that.

The short answer to his question, of course, is that you can't sell value to someone whose only interest is price. But that was probably not the most helpful answer for his situation.

The real answer is that the value that actually makes an impact on the sale, increasing customer satisfaction and decreasing price pressures may not have been the value that the distributor was talking about. Probably he was talking about what he — the distributor — considered value or value added. And that's not what counts.

Peter Drucker said it very succinctly. Hidden away in small type in a footnote on page 30 of his *Managing for Results,* Drucker writes, "'Value added' is the commonly used term. It would be much better to speak of 'cost added,' whether in manufacturing or in distribution. In the first place, only the customer adds value. All manufacturer or distributor can do is to add costs. Secondly, what one wants to find out is what part of this added cost is being turned into value and how much is friction and waste."

That, in a nutshell, is how value is defined — by determining what part of what we do or intend to do is perceived as value by the customer.

Once this sinks in, we realize that too many of us start at the wrong end, with what we think rather than what the customer wants. Because we begin at the wrong end, we don't discover that there is a significant difference in our opinions and our customers' until we, like the distributor mentioned earlier, sees that what we've termed as "value" isn't working.

In the hotel industry there was a study of what customers really wanted in their coffee breaks. So far as hotel management was concerned, customers were most interested in well-presented pastries and good coffee. When the researchers asked the customers what was important, the top two answers were nearby rest rooms and plenty of telephones so that they could stay in touch with the office.

Without asking the customer, the hotel could have spent a lot of money into the aesthetics of the coffee break and — unless they provided the rest rooms and the phones — still had very unhappy customers.

Starting at the wrong end is one problem in defining value. A second, somewhat related problem is assuming that last year's answers are still true today. We all recognize that the distribution business has changed; we sometimes don't use that knowledge in our decision making.

What was widely considered "value added" five years ago may today be a minimum acceptable level. Often this once-valuable service doesn't differentiate your company from the competition; it's simply the ticket of admission, allowing you to move to the next step, the one where the customer attempts to slash your prices and squeeze your margins.

The most obvious problem distributors have in defining value is that they don't talk to their customers. But even when they do, they often do it in such a way that the results are not fruitful; they are often counter productive.

The first problem is that the distributor talks to the wrong people. Distribution, as a sales-driven business, has taught us to value all of our customers, even when some of them are not valuable at all. In a business where the bulk of our profit is generated by a small percentage of our customers, and 20% of our customers are probably not generating any profit at all, it makes little sense to give all of their opinions equal weight.

The first rule for defining value is to concentrate on important customers, that is customers who are profitable or customers who would be profitable if we were dealing with them properly.

The second most common error distributors commit in gathering information is that they ask questions the wrong way. In companies where research is done, the "customer satisfaction survey" is popular. A questionnaire is mailed to customers along with a letter from the president of the company. In terms of defining value, this type of research is usually misleading and sometimes downright wrong — for a variety of reasons.

The first is that the customer knows who is asking the question. It is, in research terms, "sponsor identified." And when people know who is asking the question, they fashion an appropriate if not necessarily truthful answer.

The second difficulty with this type of research is the low response rates. Often response rates run 20% - 25% and sometimes less than that. One professional research organization selling mail customer satisfaction surveys made the bold step of guaranteeing a 15% response. The opinions of 15% of your customers is adequate, except in this case you don't get to choose which 15%.

But the greatest difficulty by far is that the typical customer satisfaction survey is quantitative rather than qualitative. The essential difference is that qualitative research such as focus groups or unstructured interviews asks the customer what he or she thinks is important. Quantitative research asks the customer to comment on, rank or prioritize what *we* think is important. And too often we miss the point completely

The method is simple. First, determine who your important customers are by ranking them by profitability.

Then, do the research, either by hiring a professional, hiring a student from the local college's marketing department or — worst case — doing it yourself. The question that you want answered is "What can a distributor do to make you money, save you time, or — more generally — contributing to meeting your goals?".

According to the Journal of Marketing Research, "research indicates that if a channel partner makes large contributions to another partner's goals, the latter will be more satisfied with it's overall relationship with the former." Translated from the academic, this simply means that our customers judge us in terms of how well we help them meet their goals and objectives. That, to our customers, is value defined.

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